2012/2013 Budget Statement

Turks and Caicos Islands Finances – *"On the Road to Recovery"*

May 21, 2012

Background

The Government of the Turks and Caicos Islands has faced numerous fiscal challenges over the past 5 years since being able to achieve its last fiscal surplus in 2006/2007.

Saddled with large amounts of unpaid debts and unsustainable revenue streams, the last fiscal surplus was achieved in March 2007 when the government ended the financial year with recurrent revenues of $203.1m, expenditures of $200.0m and a small fiscal surplus of $3.0m.

The ensuing years were met by numerous challenges on both revenue and expenditure. Whilst revenues had grown by 76% from $117.1m in 2004 to $206.8m by 2007, during the same period expenditure had outpaced the growth of revenue and had grown by 93% from $122.0m in 2004 to $235.6m in 2007, thus resulting in a major deficit of ($28.8m) in 2007/2008.

This trend continued into 2008/2009 where revenues totaled $197.7m against expenditure of $232.3m, resulting in a further deficit of ($34.6m). This all occurred at the same time as a major worldwide recession which caused revenue to drastically drop from $197.7m in 2008/2009 to $130.4m by 2009/2010. This sharp decline in revenue meant that even with a reduced expenditure budget of $162.0m, TCIG was still unable to fund its operating costs, ending up with a further deficit of $30.7m at the end of 2009/2010.

By the end of fiscal year 2009/2010 TCIG's accumulated deficit had increased to $94.1m in unpaid debts and this was in addition to TCIG's existing public debt of $74.4m. The Government had no reserves to finance the deficit of 2007/2008, 2008/2009 and 2009/2010 and therefore had no choice but to embark on a major reform program to stabilize its finances and return to fiscal normalcy. Of necessity, the reform program included the implementation of numerous revenue measures to stabilize TCIG's income base, as well as the development of major program to review all government expenditure. As the government was heavily cash strapped at the time, saddled with a large level of unpaid bills and faced with various litigation suits, the government had no other choice, but to borrow to finance its unpaid debts and operating deficit.

Borrowing was no easy task; with no reserves intact and no credible financial management systems in place, the government was in effect bankrupt and was no longer deemed a credible entity by financial institutions. Because of this, the government had to seek the assistance of the UK Government which provided a $260m loan guarantee.

As a result of the UK Government guarantee, TCIG is paying a very low effective interest rate of only 3.5% on the vast majority of its outstanding debt, reducing debt servicing costs by more than $10.0m in 2011/12 compared with 2010/2011.

The loan guarantee allowed TCIG to access funds to pay its outstanding creditors, to finance the accumulated deficits of the past 5 years and to cover all other costs until TCIG was able to increase its revenue and reduce its operating costs, all with the aim of achieving a fiscal surplus by 2012/2013.

To this end I am pleased to say that TCIG has now made significant progress in repaying all of its known outstanding creditors; has substantially reduced its major operating costs including manpower, has put in place a proper financial management plan, including increased revenue collection and in order to make further progress towards achieving the milestones set by UK Government, is now able to present a surplus budget for 2012/2013.

This budget shows revenues of $200.6m, expenditures of $180.0m, contributions to the Development Fund of $7.0m for additional Capital Programme funding, bond repayments of $5.9m and an overall surplus of $3.8m.

Expenditure on the Capital Programme of $16.2m is much higher in 2012/2013 than the $5.5m spent in 2011/2012 and includes key infrastructure projects such as the repairs to the North/Middle Caicos Causeway, construction of new buildings at the Ona Glinton Primary School and a new water RO plant for Grand Turk. Provided that the expectations underlying the budget are realized this will result in a substantial investment in various priorities throughout the country.

I must add that the hard work is not over; TCIG's fiscal position is now stabilized, but our country remains very heavily indebted. The coming years will continue to be challenging for the public sector, as TCIG targets paying down its debts to a level in 2016 at which it can finance itself directly from the private sector, without the need for the UK Government's loan guarantee.

2012/2013 Budget Overview

Revenue:

At the end of 2011/2012 total revenue stood at $170.9m, including Fuel Tax of $6.4m. This was above both budget and forecast.

The proposed revenue budget for 2012/2013 totals $200.6m. This is an increase of $29.7m (17%) over the previous year.

Import Duty

Import Duty which continues to be the government's largest revenue earner, ended the 2011/2012 financial year at $47.8m. The budget for import duties for 2012/2013 has been set at $51.7m, which is an increase of $3.9m (8%) over the previous year's actuals.

The increase over the previous years actual is mainly attributed to the decision that was taken in December 2011 to abandon the use of imperial gallons in the calculations of Customs Duties and to instead use US gallons. This had the effect of increasing duty charged on fuel and on alcohol by 20%.

The budget reflects the full year effect of the increases in 'Sin' taxes on alcohol and tobacco that were implemented in December 2011, as well as a small increase in revenue due to increased activity and better compliance. With the Asycuda World IT system now being in place, this should help the Customs Department to more easily detect fraud and it should also help to improve the delivery of customs services.

Customs Processing Fees

Within the Customs Sector, Customs Processing Fees are also performing well, having collected $14.0m in revenue in 2011/2012.

The budget for 2012/2013 includes CPF Fees of $18.5m, which is an increase of $4.0m (27%) over the previous years actual. The budget for 2012/2013 takes into account the full year impact of the 50% increase in CPF from 4% to 6% which was implemented on December 1st, 2011.

CPF Fees are paid by all importers on all imported items, so certain businesses that currently do not pay full Import Duties due to concessions granted in their development agreements do have to pay CPF fees, which reduces a major area of tax loss.

Accommodation Tax

Accommodation Tax performed extremely well during the financial year where collection in this regard totaled $33.1m.

The 2012/2013 Budget projects a $3.8m (12%) increase in collections when compared with last year, resulting in a budget for Accommodation Tax of $36.9m. The budget for

2012/2013 anticipates a 10% increase in activity and a 2% increase that is based on expected improved compliance and enforcement. Strong tourist arrivals, additional airlift, less discounting of rates, increased numbers of condo rooms being added to the rental pool and better compliance are all anticipated in 2012/2013.

Despite a small decrease in arrivals during the month of March 2012, arrivals performed quite well in both January and February and the small overall decrease in arrivals during the first quarter of the year, had absolutely no negative impact on the revenues collected by government. In fact during the first three months of 2012 Accommodation Tax totaled $11.2m compared to $9.1m collected in 2011, which is an increase of 22% compared to the previous year.

The recent travel agent workshop (TACC) held during the week commencing May 7th, 2012 revealed that not only are bookings strong for 2012/2013, but that in a lot of cases average daily rates are also once again increasing. This is demonstrated by the increase in collection during the first quarter of the year, despite an overall decrease in arrivals.

Travel experts: Expedia, Travelocity, US Airways Vacations, Jet Blue Vacations and Travel Impressions have already in the first four months of the year booked over 50,000 room nights for 2012/2013 and some travel agents have already in the first four months of the year booked in excess of 70% of the total amount of room nights booked last year. This of course will translate into additional funds being injected into TCI's tourism economy.

<u>Stamp Duty on Land Transactions</u>

Stamp Duty on land performed exceptionally well during 2011/2012, where actual collection stood at $14.9m against a budget of $8.9m.

The budget for 2012/2013 of $15.5m reflects a $0.6m (4%) increase over the previous year. With the new Crown Land Bill being enacted and the new Crown Land Unit being opened, it is expected that Government Crown Land will shortly be re-opened to the public. This will help to spark further activity in the real estate sector, which is already beginning to rebound.

During the first month of the financial year Stamp Duty collection totaled $2.1m with a total of $2.6m having already been collected to date; this is quite impressive.

<u>Work Permit Fees and Travel/Residency Fees</u>

The area of Work Permits was a challenge in 2011/2012. Here, total collection stood at $10.2m against a budget of $15.2m. This was largely due to the fact that the 35% increase in fees, that was budgeted to come into force in the first quarter of the last financial year, was not implemented until December 5, 2011. Thus the outturn for 2011/2012 only reflects 3 months collection based on the new fees.

The budget for 2012/2013 has been increased to $14.0m to reflect the full year impact of the 35% increase in fees. It also anticipates more compliance activity by the rebranded Employment Services Unit, which was the former Labour Department.

With the new compliance unit being put in place, both employers and employees are being advised to bring their employment status up to date in order to avoid penalties or the prospect of workers being repatriated.

In addition to the issuing of work permits, the Ministry of Border Control is also responsible for the collection of numerous other immigration related fees. Included in the 2012/2013 Budget is collections for: Travel Documents ($0.3m); Visas ($0.3m); Temporary Work Permits ($0.3m); Labour Clearance Fees ($0.45m); Naturalisation Fees ($0.45m), Permanent Residency Fees ($0.45m) and Belonger Status Fees ($0.15m).

Fuel Tax

Fuel Tax, which was previously captured under the Capital Programme is now budgeted as a Recurrent Revenue item and the budget for 2012/2013 is $7.3m against collection the previous year of $6.4M.

Airport Authority Excess Revenue

As per an agreement between TCIG and TCIAA, the Airports Authority is obligated to remit its excess revenues to the government and to this end transferred a total of $8.8m to TCIG in 2011/2012.

Transfers to government from the Airports Authority have been reduced to $3.2m in 2012/2013; however, it is important to note that collection in 2012/2013 has been impacted by TCIAA assuming the responsibility for the Airport Fire Services which previously cost TCIG $4.0m each year.

The Airports Authority will now be responsible for all costs in this regard including not only salaries and operating expenses, but also the provision of protective clothing and repairs and improvements to equipment and infrastructure as well.

As phase 2 of the continued airport redevelopment is about to come on stream, TCIAA must also retain some funding for its 3 year $10m Airport Terminal Improvement Project, so that it does not have to turn to external borrowing.

Ports Authority Excess Revenue

Similar to the Airports Authority, the Ports Authority is also required to transfer its excess revenues to the government. Transfers from the Ports Authority are being budgeted at $1.7m against collection last year of $0.9m. The Ports Authority will be implementing a combination of new fees, increases in fees and expenditure reductions. This will all result in more funds being remitted to government in FY 12/13.

Financial Services Commission Net Revenue

Financial Services Commission revenues are currently budgeted at $2.8m which is on par with the 2011/2012 Budget. However, additional work will be done during the financial year to ensure that the FSC remits above budget to TCIG.

Telecommunication Licences and Communications Tax

Telecommunication Licences and Communications Tax are both budgeted at $3.0m respectively. Communications Tax stood at $2.5m at the end of 2011/2012 and Telecommunication Licences was $2.9m.

EU Grant

The 2012/2013 Budget includes in Other Revenues $5.0m in reference to the EU 9th tranche of funding.

TCIG has made substantial progress against the EU compliance matrix and the funds are expected before the end of the third quarter. These funds were previously frozen by the EU due to a lack of confidence in TCIG's ability to properly manage its finances. The reinstatement of this grant is quite important, sending a very clear message that much progress has been made in terms of the management of TCIG's finances and that we are once again able to secure investor confidence.

Furthermore, the receipt of the EU 9th tranche of funding is quite significant as it leads on to the possible release of the 10th tranche of funding which is in excess of $12m that can be used to directly fund infrastructure projects.

Bank Services Tax and Insurance Premiums Tax

Bank Services Tax and Insurance Premiums Tax were new taxes that were implemented in September 2011, three months later than originally budgeted. Both proved to be quite a challenge where against a budget of $1.5m, Bank Services Tax only totaled $0.6m and against a budget of $1.2m, Insurance Premiums Tax only totaled $0.3m.

Due to the disappointing level of collection in 2011/2012, a conservative budget of $1.5m was set for Bank Services Tax and a further $1.0m has been budgeted for Insurance Premiums Tax in 2012/2013.

Business Licence Fees

With reference to Business Licencing Renewal Fees in 2011/2012, contrary to reports from some quarters that licenced business activities in the Turks and Caicos Islands are on a strong decline, against a budget of $3.0m, the government actually exceeded its budget and collected $3.2m Business Licencing Renewal Fees in 2011/2012. In addition to this a further $0.2m was also collected in the form of Business Licence Application Fees. Thus the total amount of funds collected from business licence renewal and application fees in 2011/2012, amounted to $3.45m. This was an increase of $1.3m (67%) above the total fees collected in 2009/2010 and an increase of $2.2m (200%) when compared with the total fees collected in 2010/2011.

The 2012/2013 Budget forecasts Business Licence Renewal Fees at $3.25m, which is a small increase of $50,000 above the amount collected last financial year and Business Licence Application Fees at $0.25m.

Thus far, during the month of March $700,000 was prepaid in relation to Business Licence Renewal Fees for 2012/2013 and a further $1.2m was collected in the month of April for the same fees.

Business Licence Application Fees on the other hand amounted to $60,000 in the month of April alone, which amounts to 24% of the total amount of application fees collected in 2011/2012. This shows that there is still a strong licenced business presence in the Turks and Caicos Islands.

Sand Mining

An open tender process has been conducted and two successful bidders were chosen for the Sand Mining contracts. The contracts have been drafted and are out for comments from the successful bidders. Once signed and implemented these contracts should yield a minimum of $1.5m in licence revenue for government this upcoming financial year.

SIPT/Civil Recovery Income

Included in Other Receipts is $9m for SIPT/Civil Recovery Income. TCIG has already received $5.0m as a result of the $6.0m grant from FCO. Five million dollars of this sum was earmarked as a reimbursement to TCIG for costs incurred in 2011/2012. The other $1.0m is earmarked for capital works that must take place in order to house the SIPT trials.

Taking into account the $5.0m already received, a conservative estimate of a further $4.0m has been included in the 2012/13 budget for additional recoveries from individuals under investigation. This is extremely conservative based on the fact that there has already been a successful judgment of $9.0m against the Emerald Cay developer and the fact that payment plan arrangements are already in place with numerous other parties.

Other Revenues

Other sources of revenue included in the 2012/2013 Budget are: Vehicle Licences ($2.8m); Drivers Licences ($0.5m); Seaport Departure Tax ($1.4m); Overtime Cost Recovered ($1.2m); Sale of Water ($1.0m); Contributions to Special Scholarships, which are mandated contributions from developers based on development agreements ($0.5m) and Migrant Health Processing Fees ($1.0m); among many other fees and charges.

Expenditure:

At the end of 2011/2012 Expenditure totaled $197.2m. The budget for 2012/2013 includes an expenditure budget of $180.0m which is a $17.2m (8%) decrease compared to the previous years' expenditures, mainly due to substantial reductions in manpower costs, in transfers to NHIB and in historic liability payments

Personal Emolument Costs

Personal Emoluments remain TCIG's most significant costs. Here the 2012/2013 Budget includes $57.6m. This is a substantial decrease of $9.9m (14%) from the previous years' actual expenditure of $67.6m. This is a direct result of the recently completed Voluntary Severance Scheme. As a result of the scheme the government now has a much leaner, but more well defined civil service that is still able to carry out the mandate of the government and provide for the needs of the people.

The breakdown of Personal Emolument Costs is:

Established Staff Basic Salaries (including NIB/NHIB)	$41,057,807
Wages	$ 3,907,125
Allowances	$ 7,648,303
Rewards and Incentives	$ 21,500
Pensions	$ 4,000,000
Gratuities	$ 1,000,000

The budget for 2012/2013 reflects a $1.5m decrease in costs as a result of the Fire Officers being transferred from TCIG's payroll to the Airports Authority and savings of $3.6m resulting from the VS Scheme. The budget for Personal Emoluments includes $1.5m to fund critical vacant posts that are essential to the Government. The wage budget of $3.9m has been reduced by $3.5m from the previous year's expenditure of $7.4m.

Gratuity expenditure has also been reduced by a substantial sum from $3.9m spent in 2011/2012 to $1.0m budgeted in 2012/2013. This results from the revised gratuity policy and the departure under the severance scheme of most of those persons who joined government service prior to 1992 and would have previously been entitled to gratuities in this and future years.

Public Service Reform Programme

A total of $8.5m was spent on the Voluntary Scheme in 2011/2012 to cover the cost of severance payments to all staff that left in both February and March. This amount also included gratuity and leave payments made to staff that left the service at the end of February.

The budget for 2012/2013 includes a further $3.0m, which is being budgeted to cover the additional outstanding leave and gratuity payments that are due to staff that left the service at the end of March. This sum also includes transfer and leave payments due to Fire Officers that were transferred to the Airports Authority.

Transfers to National Health Insurance Board/Treatment Abroad

Transfers to NHIB were a major challenge in 2011/2012 where, against a budget of $12.0m, TCIG actually transferred a total of $25.2m, resulting in over expenditure of $13.2m.

TCIG is normally obligated to transfer $1.0m per month to the National Health Insurance Board to cover those NHIB costs that cannot be met from its members' contributions, such as Treatment Abroad as well as contributions for wards of the state. However, during 2011/2012, due to fiscal challenges being experienced by NHIB, TCIG assisted NHIB by covering in full its Clinical Service payments of $2.0m per month to Inter Health Canada. This was done as a temporary measure allowing NHIB to work on increasing its contribution rate and to build up sufficient cash reserves to cover these costs going forward.

Unfortunately NHIB is still not in a position to resume the full responsibility for these costs in 2012/2013. Therefore TCIG has agreed to transfer $1.5m per month to NHIB in 2012/13 to assist with these and other costs. This increases the budget from the normal transfer of $12.0m to $18.0m instead, but still well below the total transferred last year

In addition to budgeting $18.0m as Transfers to NHIB for FY 2012/2013, TCIG has also budgeted $5.0m for ICL Reconciliation (electricity, operating expenses) and Insurance Costs. While these costs items are also the responsibility of NHIB, they cannot be accommodated in their budget at this time.

In order to resolve this problem TCIG intends to work closely with NHIB during the financial year to help to improve their financial position and also to help in managing all costs in the healthcare sector more effectively.

Hospital Provisional Charges

Under the agreement with Inter Health Canada, TCIG's primary responsibility is to cover the cost of infrastructure and equipment costs. To this end, the TCIG budget includes $18.4m in relation to Hospital Provisional Charges. This covers the monthly unitary and equipment cost payments

Subventions

In the 2012/2013 Budget, Subventions to statutory bodies have been reduced from $8.4m the previous year to $6.6m in 2012/2013. The 2012/2013 Budget reflects the closure of TCInvest and a 25% reduction in all other statutory bodies' budgets from the previous year. As the statutory body reform is just under way the budget has not factored in any major savings from the closure or amalgamation of any further statutory bodies.

The Statutory Bodies Reform Programme is advancing and will involve an in depth review of each statutory body, in order to assess their operations and the necessity of them remaining in place and remaining as statutory bodies instead of being incorporated within government departments.

SIPT/Civil Recovery

SIPT Expenses are included in the budget at $7.0m; while Civil Recovery Expenses are budgeted at $5.0m. This is in line with previous years' expenditures. In addition to this, a provision of $2.5m has also been included in Operating Expenses under the Judiciary Department to cover the legal aid cost of the SIPT Trials, with another $0.1m being included for Civil Recovery Court Costs. As you are aware Legal Aid is a social benefit which is available to all persons being tried before the Supreme Court. To this end the Judiciary Department has already received applications in this regard.

Previous years' SIPT/Civil Recovery costs have been mostly reimbursed by the UK Government or covered by other recoveries. At the end of 2010/2011 the FCO transferred $10.0m to TCIG to assist with the costs of SIPT/Civil Recovery and a further $6.0m was received in April, 2012, in addition to the $1.25m recovered from an individual under investigation in 2011/2012.

Grants and Contributions

Grants and Contributions of $3.4m, have been substantially reduced from the previous year's expenditure of $4.8m. This is primarily due to the expenditures on scholarships being reduced from the previous year's expenditure of $3.8m to $2.65m. As the large number of students granted scholarships in previous years have come to the end of their courses, the number of new scholarships being granted is expected to be maintained at previous levels within this reduced budget

The budget presented for scholarships includes not only the continuing cost of all students currently on scholarship, but also includes funding for new local Community College Associate Degree and Bachelor Degree scholarships as well as new international scholarships based on priority and performance.

Social Development Costs

Paying particular attention to the area of social development, the Department of Social Development's budget has been increased from $1.3m spent in 2011/2012 to $1.7m for 2012/2013. This includes a Home Help Services budget of $0.3m, $0.2m for Care of Juveniles, $0.1m for Welfare Benefits, $0.1m for Continuous Education, $0.125m for the new Juvenile Center Operating Costs and $0.1m for Electronic Monitors as an alternative to prison sentencing.

The Social Development Department has been reformed and has done some impressive work with the Courts in the past few months with Welfare Officers filling the role of probation officers to the courts.

Maintenance Costs

A significant increase in expenditure has also been recorded in Maintenance Expenses. This has been increased from $3.7m spent in 2011/2012 to a budget of $5.3m for 2012/2013. This deliberate increase includes a budget of $1.0m for road maintenance, $0.25m for maintenance to school buildings; $0.2m for maintenance to other government buildings; $0.65m for street lighting; $0.2m for reinstatement costs to leased office buildings and $1.8m in relation to the Solid Waste Management Scheme. This demonstrates the Government's commitment to working towards improving infrastructure around the islands and also to improving the standards of government owned and operated properties.

Other Expenditure

Included under Other Expenditures are significant increases in expenditure regarding Computer Licence, Software and Maintenance fees which have increased as a result of TCIG's commitment towards becoming fully compliant with our software licence agreements.

Other Expenditures also includes Insurance Costs of $0.5m. This covers Police Accidental Death Insurance of $0.1m, Third Party Insurance for government vehicles of $0.1m and the Caribbean Catastrophic Risk Insurance Facility of $0.3m. The Catastrophic Risk Insurance facility is a pooled facility with other Caribbean islands and is quite important as, once a category 3 or above hurricane is experienced in TCI, an automatic cash payout is generated.

Hosting and Entertainment Expenses of $0.1m actually includes the cost of hosting meetings and conferences and the Training budget of $0.4m includes training for all government departments including the Police of $0.1m.

Advertising and Promotions expenses have increased to $0.2m as a result of the Investment Unit advertising and promotion costs of $0.15m.

Captured under Sundry Expenses are Repatriation and Exportation Expenses of $1.0m and Central Purchasing Unit Unallocated Stores Adjustments of $0.1m.

Travel Expenses, Professional and Consultancy and numerous other expenditure accounts have been kept in line with expenditures for the previous financial year.

New Expenditure Accounts

A number of new expenditure heads have been added to the 2012/2013 Budget. These include: the Director of Public Prosecutions Office ($1.0m); Crown Land Unit ($0.5m); Investment Unit ($0.5m); National Audit Office ($0.2m); Chief Internal Audit Office ($0.1m); Juvenile Center ($0.1m) and Radar Operations ($1.0m). These costs have been distributed among all expenditure codes and have largely impacted office expenses, salaries, operating expenses and other expenditure accounts.

Provisions Accounts

To safeguard against potential unplanned and undecided expenditures, the budget also includes various provisions accounts, including: $3.0m for Investment in Milestones which can be used to fund the additional costs of investments needed in the Elections and other departments; $1.5m is budgeted as a part year Provision for the possible funding for Elected Government (elected members' salaries, etc) and a budget of $6.2m has been included for Historic Liabilities that were quite a challenge in the last few years.

Contingency Fund

In addition to the provisions accounts, a prudent Contingency Fund of 3% of total expenditure ($5.0m) has been included in the revenue budget to accommodate unforeseen and extraordinary costs.

On top of this, a Special Contingency Fund of $6.0m has also been included below the revenue account surplus to account for any other unexpected budget variances that may occur during the financial year. The Special Contingency Fund will only be used to cover adverse budget variances in extreme circumstances and will be done with the prior approval of the UK Government. If the financial outcomes for 2012/13 remain in line with budget, it may be possible with UK Government approval to release some or all of this special contingency provision for additional infrastructure improvement works.

Overall:

An achievable revenue target of $200.6m has been set. There are a number of possible revenues that at present are not sufficiently certain to include in the budget, such as the Emerald Cay judgment of $9.3m and other potential revenue upsides.

It has been agreed that should there be any additional windfall revenues outside of the budget during 2012/2013, these sums would be paid into the Sinking Fund in order to build up capacity to pay down the national debt which is a key priority.

In regards to expenditure, various provisions have been built into the budget to safeguard against external and other shocks, where in addition to the normal Contingency Fund of $5.0m and the provision for historic liabilities of $6.2m; a Special Contingency Provision of $6.0m has been created 'below the line', with the intention that this will only be released for discretionary capital or revenue expenditure purposes with the approval of the UK Government. This contingency fund will also be used to pay into the sinking fund if revenue and expenditure perform in line with the budget and it has not been used for any other purpose; otherwise it will be available to protect against unbudgeted adverse events.

It should be noted that a $7.0m contribution to the Capital Programme must be funded from the Revenue Account. Bond repayments of $5.9m must also be met from the Revenue Account, so the proposed 2012/13 TCIG Budget shows a net overall cash surplus of $3.8m which is considered realistic and achievable.

Capital Programme

The Capital Programme expenditure budget has been increased from $5.5m actual expenditure in 2011/2012 to $16.2m in 2012/2013; $14.4m is in relation to TCIG funded expenditure and $1.8m is in relation to Grant funded expenditure. It has been agreed with the loan guarantor that capital expenditure commitments will not be made until the income to pay for them is received or certain to be received.

TCIG funded capital expenditure is budgeted to be funded by a transfer from the consolidated fund of $7.0m and proceeds from sale of land of $7.4m. As the Crown Land Bill has been passed and the Crown Land Unit put in place, activity on crown land will shortly be reopened and based on the new Crown Land Ordinance will see certain transactions moving straight to freehold title, thus resulting in sale of land revenues to the government.

We have applied strict prioritization criteria to TCIG funded expenditures which it has been decided are: education, health, infrastructure and improvements to government owned facilities. Although these expenditures are critical, we also need to ensure that our finances do not deteriorate further. Thus we will only go forward with each expenditure item once the money to pay for them has either been received or is certain to be received.

Capital Projects in the four critical areas are as follows:

Education

With regards to the education sector, the budget includes $0.9m for the construction of buildings at the Ona Glinton Primary School, $0.5m for the new administration block at the HJ Robinson High School, $0.3m for additional toilet blocks at the Clement Howell High School; $0.1 for a Canteen at the Clement Howell High School and $0.2m for the construction of a bathroom block at the Ianthe Pratt Primary School

Health

In the health sector, the capital budget includes: $0.1m for upgrades to the Salt Cay Clinic and $0.1m for furniture and equipment for the Middle Caicos Clinic.

Infrastructure

In terms of infrastructure, the budget includes $1.35m for repairs to the causeway that connects North and Middle Caicos and $1.0m has been included for a new water RO plant and Equipment for Grand Turk, along with a further $0.3m for repairs to the water catchment facilities in both Grand Turk and South Caicos. This will result in a much needed improvement in water facilities for the residents of Grand Turk and South Caicos.

Government Properties

With regards to government owned properties: $0.3m is being budgeted for the refurbishment of the former Immigration Office at South Base in Grand Turk, with another $0.3m being budgeted for refurbishment works at the former Chief Secretary's Office in Grand Turk.

The budget also includes: $0.3m for the construction of a Customs Warehouse and Office in Grand Turk; $0.3m for the construction of a Remand/Detention Center in Providenciales; $0.1m for a Home for Juveniles; $0.4m for the renovation of the Providenciales Magistrates Court and a further $0.1m for the South Caicos Community Center.

Other Capital Expenditure

Included in other capital expenditure is $0.3m for TCIG's contribution to the EU Housing Initiative and $0.3m for TCIG's contribution to the Carnival Infrastructure projects; $0.3m for the Radar System; $0.2m for new Police Patrol Vessels and $4.5m for Providenciales Airport Land Acquisition Costs.

Grant Funded Expenditure

Grant Funded Expenditure of $1.7m will include $1.0m for the EU Housing Initiative which will seek to aid in the repair of homes damaged during Hurricane Ike; while $0.1m will be spent on the Strengthening of the Public Health Delivery System in the TCI, $0.65m on the Bight Community Park, $0.3m for the Contribution to the Basic Needs Trust Fund and $0.04m on repairs to the South Caicos Disable Center.

Public Debt

At the end of March 31st, 2012, total debt stood at $228.7m. This included loans held by TCIG ($214.6m) and also those held by statutory bodies (TCInvest), but guaranteed by TCIG ($14.1m); $185m of that debt balance is guaranteed by the UK Government, which was necessary to finance the deficits from 2007 onwards and to repay all outstanding creditors. The remainder of the debt that is not guaranteed by the UK Government consists of bonds ($29.6m) and the TCInvest loans (14.1m).

Principal repayments of bonds due during 2012/2013 total $5.9m and interest payments total $7.7m. The very low interest rate facilities secured via Scotia Bank as a result of the UK Government guarantee has led to a saving of more than $10.0m a year in debt servicing costs, compared with levels paid in 2009/2010.

Moving forward it is a key priority for TCIG to be able to pay down its national debt. This can only be done by of course generating fiscal surpluses, which will allow reductions of debt stock, which is much preferable instead of having to borrow funds on a continuous basis to fund revenue account deficits and other capital costs.

It is the intention of the Government to create a Sinking Fund that will be used to accumulate funds towards the paying down of the national debt. At present, interest on debt is low due the UK Government guarantee and there is no repayment due for most of the debt until 2016. However, in future years interest charges will increase and large principal payments will become due. Thus we need to ensure that these are both affordable.

Context of the Budget in relation to the Wider Economy

The Turks and Caicos Government has clearly benefited from significant gains during 2011/2012. This is despite not being able to implement $4.3m of its proposed revenue measures, including, but not limited to: Water Consumption Tax which was budgeted at $1.6m; Water Consumption Tax which was budgeted at $0.7m and Sand Mining Fees which were budgeted at $2.0m. Despite all these revenue shortfalls TCIG was still able to exceed its revenue budget.

Revenue collection during 2011/12 in both the Tourism and Real Estate sectors showed a substantial increase in economic activity in those areas and the start of a rebound in the Turks and Caicos Islands economy.

Revenue collection in business licence renewals and applications show that businesses still want to do business in the Turks and Caicos and collection from the Tourism Sector including Accommodation Tax which exceeded $33m, Seaport Departure Tax of $1.4m and Vehicle Stamp Duty of $0.8m, show that tourists still love to visit our shores and we are still well placed in the tourism market.

2011/2012 saw the arrival for the first time, of the Turks and Caicos Islands one millionth visitor, which was a historic occasion and all indications show that 2012/2013 will be an even more economically successful year.

With the new Investment Unit having already been put in place, there are over 20 major development projects currently under consideration. This added to the Government's Capital budget of $16m means that much needed extra cash will begin to circulate through the Turks and Caicos economy which will help to jump start other economic activity and employment, particularly in the construction industry

Improved Business Practices

Much has been done in the past year to improve the way that TCIG conducts its business. As mentioned, in addition to putting in place a new Investment Unit, TCIG is also improving and streamlining the offering of concessions and the drafting of development agreements to reflect more equitable practices.

In addition to reforming the way that TCIG conducts business, TCIG has also sought to protect and preserve the rights of its citizens by conducting a major legislative reform project which will see the completion/revision of over 80 pieces of legislation, included, but not limited to a new: Crown Land Ordinance; Elections Ordinance; Employment Ordinance; Juvenile Justice Bill; TCI Domestic Violence Bill and Health Regulation and Health Professions Bill. These are all vital instruments that will help to protect the rights of the citizens and belongers of the Turks and Caicos Islands and will help to make our country a better place to live.

Financial Management

In the area of financial management, as of April 1st a new Public Financial Management Ordinance came into being which will ensure the safeguarding and protection of the Government's finances and will hold Accounting Officers and Statutory Bodies to a higher level of accountability.

The new National Audit Office Ordinance will also see the Audit Department as of September 1st, 2012 split into two critical bodies: the National Audit Office which will be set up as an independent statutory body and the Internal Audit Office, which will be required to ensure internal compliance within government; while the Chief Financial Officer Ordinance will set out the CFO's executive position in TCI's government for the period of the UK Government's loan guarantee.

During 2011/2012 I am happy to report that the Treasury was able to produce 4 years of back logged financial statements from 2007 onwards that are now with the Audit Department to be audited within the approved timeframe.

During the year TCIG also worked to improve its relationship with the public by trying to keep the public more informed of the operations and finances of the government. This was done through the publication of quarterly reports on government finances. These reports detail the fiscal position of the government at the end of each quarter and are posted on the governments' official website.

The new PFM Ordinance dictates that this practice will continue with not only the Ministry of Finance having to update the public on a quarterly basis, but also requires that once ministerial government is back in place, it will also be the responsibility of the Minister to ensure that the House of Assembly and the public is kept informed of the finances of government on a continuous basis.

Future Outlook

The Turks and Caicos Islands Government is in the process of drafting a new Development Strategy for 2013 through 2017. This Strategy aims to respond to new economic circumstances.

The new Development Strategy updates the earlier development plans, making adjustments for the national and global recession, focusing on further reforms to be considered for adoption by the next elected government of the Turks and Caicos Islands (TCI).

It is our intention to make the Turks and Caicos a well-governed country where balanced, sustained and increasingly diversified growth and development will lead to equal opportunity, security and empowerment for all members of society.

Much has been done in terms of putting in place a modern Public Finance Ordinance that speaks to the roles of the Minister, the House of Assembly and Accounting Officers, budget execution and reporting, and the management of public funds.

TCIG has also been able to develop proper reporting systems through the development of monthly departmental and stakeholder financial reports, quarterly financial reports published on the government website and in local media, and internal forecast documents which project revenue and expenditure for the remaining quarters of the financial year.

The 2012/2013 Budget demonstrates marked improvements in terms of increased revenue collection while reducing the levels of discretionary and other expenditure. During the financial year, we will continue to focus on revenue collection, monitoring and enforcement, and on prioritizing our expenditure and controlling costs to ensure adherence to the budget.

New Taxes and Protecting Vulnerable Persons

In last year's budget it was announced that a new 'Value Added Tax' (VAT) would be implemented from 1 April 2013. The implementation process for VAT is now well under way, with the public consultation on how it will be implemented in the course of being conducted. Many comments have already been made about VAT by businesses and members of the public, much of it adverse and based on misunderstandings.

I should like to take this opportunity to explain that whilst VAT is a new tax, it is really a replacement for existing taxes. It is not intended that VAT will raise additional tax, other than the opportunities it will provide for improved collection rates in some business sectors. I should also make it clear that VAT will be implemented in the simplest possible way for a small country like TCI, so additional costs imposed on businesses and on Government will be minimal.

The main reason for implementing VAT is to spread the tax burden more fairly across all business sectors and to reduce the tax losses occurring due to the past concessions offered to certain businesses under development agreements, which are no longer justifiable and result in unfair competition against those businesses that have not received such generous, or any concessions.

I can give an assurance that no other new taxes are under consideration and I do not expect any increases in existing taxes will be necessary now that a financial surplus is being projected in this year's budget.

It is very important for TCIG's future financial stability that VAT is implemented; as it will provide a sustainable source of government revenue that is fair across all sectors of the economy and does not discourage external investment in TCI as an income or property tax almost certainly would. These two taxes were recommended in previous consultancy studies as the alternatives to VAT that could provide a fair and sustainable source of government revenue in the longer term. However they were discounted in favor of VAT, for the reason of being discouraging to external investors.

I recognize that lower income and other vulnerable individuals need to be protected from the effects of tax on their living costs, so I intend to ensure VAT is implemented in a way that ensures this.

In the same way as import duties on basic food items and other essential healthcare products, etc are set at zero rate, so will such items also be exempted under the new VAT arrangements.

Once the VAT consultation period ends on 19 June, decisions will be made on exactly what exemptions will be included in the VAT legislation which will be approved in mid July. Adjustments in or removal of existing taxes will also form part of the implementation arrangements for VAT, so consideration will be given at the same time to how these can best be set in a way that also protects vulnerable individuals in a reasonable way, without undue loss of revenue to government.

Conclusion

It has been a very difficult period over the past few years for the Turks and Caicos Government in the management of its finances. TCIG has required the assistance of not only the UK Government, but also the efforts of the individual ministries and departments within the Turks and Caicos Islands, most particularly the Ministry of Finance to be able to reform TCIG's finances.

The production of this budget has involved input, advice and support from all sectors of government who are all thanked for their contribution; most especially the Permanent Secretaries, Heads of Department and Budget Team within the Ministry of Finance who worked so diligently over the past 4 months to prepare this document. Profound thanks is also extended to the Governor, Chief Financial Officer, Chief Executive Officer and all TCIG Advisors for their assistance in carrying out this and other initiatives.

The reforms implemented over the past few years have been hard and have been faced by strong opposition, but were necessary to ensure that the Turks and Caicos Islands Government restores its international credibility through ensuring financial stability and clear intent to continuing on a sound financial footing.

Much has been done in the past few years and there is still much more to do. Producing and presenting this budget is my first monumental step; the difficult task at hand will now be to deliver the objectives that have been set out in the budget; to this I pledge my full commitment!