2011/12 Budget Statement
Presented to the Consultative Forum
April 5, 2011

Madam, Chair
Members of the Consultative Forum
Ladies and Gentlemen

A pleasant good morning to all,

It is indeed a privilege for me to make a statement on the 2011/12 Budget for the government of the Turks and Caicos Islands.

The need for change

The Government of the Turks and Caicos Islands faces a financial crisis. It has been running a significant budget deficit since 2007 and has accumulated high levels of debt as a result. It cannot attract further borrowing on the capital markets. Without UK support the TCI public sector would be bankrupt. The Government would have been unable to pay salaries or fund public programs; administration and the rule of law would have collapsed; existing lenders would have foreclosed on their loans; and more people and businesses would have faced hardship.

Bankruptcy has only been avoided so far because the UK Government have provided the financial support needed to keep the public sector afloat and now, through $260 million of loan guarantees, with the time and resources we need to tackle the dire fiscal legacy the interim government inherited.

The previous administration failed to pay many of its creditors, damaging local businesses and the reputation of the islands. We have worked hard, with the support of the UK, to ensure that TCIG is able to meet its obligations once again.

The previous administration also failed to protect taxpayers. It gave away public land and public money, through widespread tax concessions and exemptions, at an increasing and unsustainable rate. We are working hard to recover what we can, and to put in place a more robust system for the future.

Moreover, the previous administration also failed to invest in the future. We have invested $70 million in the development of Providenciales Airport, which will lay the foundations for growth for years to come.

The UK Government-backed financial support package which is now in place buys us the time we need to tackle the fiscal crisis. The package has allowed us to refinance TCIG's high level of debt at much lower cost, and provides enough money for the deficits that will continue into 2012/13 even with new budget measures. As a result, future debt service costs will be reduced considerably and this will provide further resources for us to continue to provide key services.

The UK has also funded the costs of the SIPT and the civil recovery process, as well as police costs incurred to combat the spike in violent crime in the last financial year, providing an extra $10.5 million to TCIG for this purpose. I am glad to report that the UK has now also provided a further one-off $3.2 million grant to support public service reform.

The UK support does not, however, provide money to reverse previous spending cuts or fund significant new expenditure; instead it provides a one-off opportunity to take the fiscal measures needed to bring revenue and spending into line. We have no alternative other than to balance TCIG's budget by raising revenues and cutting spending; like any household or business, the public sector cannot continue to live beyond its means. Achieving this is not only essential to avoid the spectre of default; it will also provide a major boost to the economy by allowing payments to be made to local businesses and restoring confidence that the Turks and Caicos Islands are financially secure and a good place for investment.

Tackling the severe and structural fiscal problems and achieving a fiscal surplus in the financial year ending March 2013 will be tough. We must stabilise the Government's finances now, though, to ensure a quick path out of the current economic difficulties to a more prosperous TCI in future. Being well on course to achieve this is a key milestone towards setting a date for elections.

It's worth reviewing how this crisis came about.

National accounts statistics suggest the economy doubled in size in real terms between 2002 and 2008, but that growth was neither balanced nor sustainable. It was fueled by rapid growth over a short period of time in public administration and construction.

In fact, over this period public sector spending expanded three fold, far exceeding growth in public revenues despite increasing sales of Crown land. This heavy and growing reliance on the public sector and the construction industry for employment and incomes increased the vulnerability of the economy to external shocks. The global financial meltdown and property crash in 2008 brought growth to an abrupt halt.

The tax system was never able to generate sufficient recurring revenues to cover such a high level of public spending. The tax base is too narrow, it is easily avoided by some, and it weighs too heavily on some groups and sectors of the economy, notably lower income groups and the hospitality industry.

In addition the tax base has been eroded by generous exemptions and concessions granted in the past, together with inadequate administration, collection and enforcement. Tax revenues peaked at around of 24% of GDP in 2006, but have since fallen to around 16% of GDP. In dollar terms, the peak was in 2008/09, at $220 million, falling to around $120 million in 2010/11. Yet, due to the commitments made by the previous administration, we have only been able to cut government spending to around $170 million on a recurrent basis, of which more than $70 million is spent on personnel.

The result has been a growing structural deficit which will continue to grow unless there are significant reforms. Expanding the TCI economy is vital, but this will not close the deficit fast enough to avoid defaulting on our debts without the measures set out in this budget.

The US economy remains weak, but modest medium term growth is possible if the TCI economy is able to modernise and diversify. Forecasters suggest the Caribbean could grow at around 4% per year, largely driven by tourism. The major new investment in an extended Providenciales International Airport which is underway is vital for TCI to share in this growth. The airport has already attracted new flight operators, with the prospect of increased competition for airspace and lower fares.

At the same time there is increasing interest from external investors keen to develop branded hotels in the islands. Although the cost and availability of significant private finance for real estate investments remain restricted globally, the Government is optimistic that some new projects will be announced over the next year. However, TCI must also seek to grow other sectors including agriculture, fishing, education and medical tourism to provide alternative jobs and incomes, and the government has put a number of measures in place to assist these and other areas of business.

We will continue to invest in affordable economic stimulus measures and in administrative and legal reforms to encourage this growth and diversification, but this needs to be accompanied by wide-ranging public sector reform to improve the openness and competitiveness of the business and economic environment.

Our aim is to restore and firmly embed the principles of sound financial management, sustainable development and good governance. This will help rebuild confidence in TCI and its ability to manage its public finances. We are committed first and foremost to effective police, criminal justice and immigration services, so that people can live, visit and work in the Turks and Caicos Islands in safety. We also need to achieve the milestones set out in last year's Written Ministerial Statement in order to pave the way for elections as soon as possible. And we need to reform our public services to make them fit for the future.

Against this background, any TCI government faces tough choices. It needs to modernise its tax system to improve the efficiency of collection, expand the tax base and increase revenues, and it must cut wasteful public expenditures and implement public sector reforms to improve value for money. The same is true of many other countries, both regionally and globally, that are taking similar action to control their public sector finances and reduce their indebtedness.

Revenue measures

The need to reform TCIG's tax system has been recognised for many years, and last year the Roe Report set out a number of options for change. Since September 2010 we have been working with EU experts to develop these into a feasible set of proposals that will both reform the tax system and help close the budget gap over the next two years.

These proposals have been the subject of widespread consultation, including a series of meetings with members of the business community, the two Chambers of Commerce, the Turks and Caicos Real Estate and Hotels Associations, radio and TV broadcasts, and meetings with the businesses and sectors directly affected. We're grateful to those who took the time to attend the meetings or to comment in other ways.

Government must take decisions that are in the long term interests of the economy and balance the competing needs of families, consumers, employees, different business sectors and the public sector. We have therefore taken stock of the results of the consultation process and, where sensible and feasible, have adjusted the recommendations to produce a package of measures as part of the 2011/12 budget .

First of all, taking account of both practical considerations and the strong views expressed by local businesses and others, we have ruled out the introduction of an income tax. We have also heard the case against a property tax and ruled that out too. The cornerstone of the new, reformed tax system for the medium term is the introduction of a **Value Added Tax**. VAT is a broadly-based consumption tax which has been successfully introduced in countries world-wide, including many smaller economies with a heavy reliance on tourism. In the Caribbean, it has been successfully implemented in Barbados, Jamaica, Trinidad and Tobago, the Dominican Republic, Haiti, Belize, Dominica, Grenada, Guyana, Antigua and Barbuda, and St Kitts and Nevis, and it is in the process of being implemented in St. Lucia, and St. Vincent and the Grenadines. In many instances the revenues raised by VAT have been well ahead of projections, reflecting its efficiency as a tax and its self-policing nature.

VAT will provide a stable source of revenue for TCIG. The current tax system creates distortions and impede economic growth. The proposed VAT will remove many of these distortions by imposing a single rate on domestic and imported goods and services with few exceptions, and will improve competitiveness. The full crediting of VAT on capital investments will also lower the cost of investment for many businesses. This economic boost will help to ease the country's fiscal position.

Introducing VAT will, however, require a significant amount of preparation, especially given the poor state of revenue collection within TCIG, and the lack of readiness within the wider economy. We therefore need to put in place a number of temporary measures to pave the way to VAT, close the budget gap, and avoid a default. We expect that most of these will fall away, together with a number of existing taxes, when VAT is introduced in 2013/14.

Together, these measures will raise revenues to around $160 million in 2011/12, rising to around $190 million by 2013/14. This, along with cuts in expenditure, will put us well on the road to financial sustainability, and allow us to start to repay debt, and build reserves for future investment and to withstand the shocks to which a small island nation is vulnerable.

I will now outline the temporary measures that are required to close the budget gap while we prepare for the introduction of VAT, first those relating to changes to existing revenue streams.

The most important of these is the immediate introduction of a 4% **Customs Processing Fee**, which will apply to all imported goods and importers. This will boost TCIG's revenues by an estimated $12 million in 2011/12, and will have the advantage of including imports that are currently covered by exemptions and concessions, so that the cost is shared as widely and as fairly as possible. The only exception to this will be goods imported by InterHealth Canada; the structure of this contract means that TCIG currently pays for services on a cost-plus basis until a review is carried out in time for financial year 2012/13, and adding the Customs Processing Fee to InterHealth's costs will lock the extra costs into TCIG's budget for the length of the contract.

Introducing a Customs Processing Fee also preserves the changes to the import duty tariff that were introduced last year to simplify the tariff structure and improve administration, and to provide some help to lower income families and small businesses. It is important to note that, even with the new Customs Processing Fee, import duties on a wide range of essential goods will still be lower than they were in 2009/10. We strongly urge those who have not yet done so to pass on the benefit of this overall reduction to their customers.

The system of import duties has been undermined by wide-ranging concessions and exemptions that were granted in the past, which reduce the effective duty rate significantly. We will carry out a thorough review of these during 2011/12 with the aim of ensuring that they are being properly exercised, and where possible we will remove them unless they contribute materially to improved social and economic welfare that would otherwise not occur, in line with the new Encouragement of Development Ordinance.

We will also make changes to the system of **work permits** to raise revenue and to make it fairer and more effective. Work permit fees are complex, with the list of different occupational categories running to 35 printed pages. They are therefore open to significant error and manipulation. In addition, the fees themselves have not been increased since 2001. It is clear that there is still much work to be done to create a system that is more transparent and simpler to operate, delivers the skills the economy needs, and allows skilled labour to move freely between the available jobs. In the meantime there is scope to improve the working of the current system.

We will continue to investigate the feasibility of moving to a percentage-based fee system, collected monthly, as recommended by the consultants; this would raise an additional $15 million in a full year. In the meantime, we are proposing to radically simplify the employment categories under which work permits are issued and to raise the fees with effect from 1 September 2011, leading to part year revenues of $5.2 million in 2011/12.

Most other **fees and charges** have not been increased since 1996. In real terms they have been eroded by around 35%, and this has also contributed to the widening gap between spending and revenues. We will therefore restore this loss of revenue by increasing fees and charges broadly in line with inflation, but at the same time simplifying and improving administrative efficiency to reduce unnecessary burdens on business.

The largest category of fees relates to **business licensing**. Responsibility for administering these will move to TCInvest from 1 July 2011, in line with our aim of developing a system of one-stop-shop advice for those who want to invest and do business in TCI. This will enable us to bring together business licensing with the provision of business advice and support and, in due course, the administration of other Government services such as work permits and other regulatory requirements.

As with work permits, the structure of business licences will be reviewed and simplified by TCInvest as part of our objective to simplify processes and regulation; in the meantime all business licence fees have increased by an average of 35% from 1 April 2011, and all renewals for 2011/12 must be completed by 30 June in order to allow a smooth handover of responsibility from TCIG to TCInvest. This will raise additional revenue of $1.9m this financial year.

A range of other fees and charges will also be increased, including **vehicle licences and driver's licences,** which will increase by 50% from 1 May 2011; this increase alone will raise revenue of $0.8 million in 2011/12.

In addition to these increases in existing revenue streams, we will also introduce new revenue measures that will help to close the budget gap and bridge the way to the introduction of VAT by covering sectors of the economy that are currently not subject to taxation. We propose to introduce these measures from 1 September 2011; this will allow the time needed to consult fully with the sectors affected and to put in place proper systems for collection and enforcement.

The first of these new measures is a tax on **electricity**. We have listened to the strong views that were expressed about the original proposal to introduce a 10% sales tax on electricity usage. We have concluded that a carbon tax on electricity generators is a better option, to encourage the generating companies to review their generating efficiency and mix of sources, including from renewable technologies, over time. This also has the advantage that it cannot be passed directly on to consumers, and we will continue to use the regulatory framework to apply downward pressure on electricity costs. This measure will be introduced by 1 September 2011, and is forecast to raise $1.6 million in 2011/12, rising to $3.4 million in 2012/13, and will pay for the new waste management programme.

We will also introduce a **water sales tax**. Again, we have listened to the concerns that were raised in consultation, and we have modified the proposal to include a threshold so that most households will not pay this tax. Instead it will be levied only on commercial customers and the largest residential customers, where it will have the effect of encouraging conservation of this scarce resource. This measure will be introduced by 1 September 2011 and will raise an estimated $0.7 million in 2011/12, rising to $1.4 million in 2012/13.

Finally, we propose to introduce a **sales tax on financial services and insurance premiums**. The bank tax will be levied on all non interest-bearing services provided by banks at a rate of 10%; it will replace money transfer fees and stamp duty (miscellaneous). The insurance tax will be levied on gross premiums for general insurance with a rate of 2.5%. Life and health insurance premiums will be exempt from this tax. These taxes will be introduced by 1 September 2011, and they will raise an estimated $2.7 million in 2011/12, rising to $ 5.7 million in 2012/13.

Together with forecast annual growth of around 4% in the economy over the same period, these measures will raise an estimated $33.4 million in 2011/12, helping to close the Government's fiscal deficit and starting the much-needed process of reforming the national revenue system. They will spread the burden of new taxation more widely among the people who live and work in TCI and those who visit these islands, they will protect the most vulnerable, and they will pave the way towards the introduction of a Value Added Tax from 1 April 2013.

At that point, subject to successful implementation of VAT, it should be possible to greatly simplify the entire tax system and reverse the temporary measures being introduced this year. It should be possible to reduce many import tariffs and eliminate a range of other taxes including accommodation tax, telecommunications tax, vehicle hire tax, carbon tax, water sales tax, and bank services/insurance premium tax. This will be a huge leap forward for TCI in developing a modern, stable and efficient tax system which supports economic growth and stabilises government finances.

It is always difficult to predict the performance of new revenue measures in practice. The tax reforms have been modelled as thoroughly as possible by experts, using the best available data from a range of sources, but there is a degree of unavoidable uncertainty about the performance of the economy, particularly given the poor state of information in TCI. We have therefore developed a contingency plan under which we will respond to any shortfall in forecast revenues by increasing the Customs Processing Fee from the initial rate of 4%. Each 1% increase in CPF would raise approximately $3 million in revenue. We hope that this will not be necessary, but it is vital that TCIG is able to raise enough revenue to produce a fiscal surplus in the year ending March 2013.

We are forecasting growth in some existing taxes such as accommodation tax and import duties due to increases in tourism. The collection of import duties should also increase due to the introduction of ASYCUDA World. This will revolutionize the way in which the Customs Department and the trading community conduct their business by using the latest information and communication technology. Greater reliance will be placed on enhanced techniques for risk analysis, compliance, trade facilitation and post clearance audit. This will speed up the clearance process, simplify procedures, strengthen the enforcement capability, reduce administrative costs and, most importantly, increase revenue.

Prospects for increases in stamp duty are limited due to a continuing decline in real estate activities, but plans to introduce legislation to facilitate fractional ownership of assets in the TCI are intended to increase transactions in the sector as well as visitor arrivals.

Finally, in line with the decision taken as part of the 2010/11 budget, fuel tax will increase by 25c per gallon with immediate effect.

In addition to these measures, we are continuing to explore **new revenue streams**. This year's budget includes $2 million from new sand mining contracts which are currently being tendered; this is likely to rise to $3 million in 2012/13, with the potential for more in future years. Sand mining will not be permitted in protected areas, and will be preceded by environmental impact assessments.

On the grounds of prudence we have not included any provision for other new income that may come on stream during the year.

As well as reforming the revenue system and increasing revenues, it's also critical that we improve our **revenue administration**. Arrears have increased significantly over the last few years, compounded by poor monitoring and enforcement. This situation was made worse by the Government's inability to pay its creditors on time, leading to a vicious circle of non-payment and a lack of capacity to enforce debts due to Government. We are now able to pay our bills as they fall due, thanks to the UK-backed financing package, and we will use the opportunity this provides to ensure that all monies due to Government are paid on time and in full.

We will invest in our revenue collection capacity and systems, especially as we implement VAT in 2013. We aim to introduce a single Revenue Authority for TCI, bringing together responsibility for all revenue collection and enforcement activity to reduce costs and increase effectiveness. With this in mind we have requested assistance from the IMF's regional centre of expertise, CARTAC, who are undertaking a fact-finding mission to TCI this week. We hope that this will provide the opportunity to learn from other Caribbean nations who have faced similar challenges, and to share experience, skills and expertise. This initiative has the potential to develop new, highly skilled jobs for the right people, in line with the wider civil service reform objectives.

Expenditure measures

As well as reversing the steep decline in TCIG's revenues and reforming the revenue system to make it more stable and efficient, we also need to tackle the rapid and unsustainable growth in public expenditure that has occurred since 2002. Some success has been achieved, but the crisis in the public finances means that much of this has been done on an ad hoc basis, making the savings that are easy to achieve rather than those that will lead to more effective, efficient and sustainable public services for the future.

Staff costs are by far the biggest element of TCIG's expenditure, at around $70 million in 2010/11. These costs have fallen from $88 million in 2008/09, due to controls on recruitment and the 10% pay cut imposed in May 2010, which helped to keep the public sector from collapse. We now need to start the hard work of reforming the civil service to ensure that it's fit for purpose, that it's able to deliver the services needed by a modernising economy and expected by residents and those who visit and work here, and that it offers rewarding jobs and career opportunities for public servants.

We have recently started a process to reform the public service by reviewing the way in which Ministries do their work and the resources they use, and making adjustments to improve the structure of the organisation and the jobs people do. We aim to build a public service that is smaller and stronger, with high standards and greater accountability to the people of TCI, with the right incentives for staff to do their jobs well and greater opportunities for fulfilling work and career progression.

This will mean staffing changes, and some staff may need to move between Ministries and Departments to ensure that essential posts are filled. Some jobs will have to go, in line with the widely-accepted target to reduce the cost of the public service, but we will work to find alternative employment opportunities for staff, and we will provide assistance for the people affected by these changes.

We are very grateful for the offers of support we have received from our partners in the private sector as we begin this process, and we will work with them to manage the transition as well as possible by sharing expertise, information and resources. This has the potential to provide a further boost to the economy by releasing resources to more productive uses and providing alternative career paths that are both challenging and worthwhile for public servants.

Achieving this won't be easy, especially against a background of very tight financial resources, but it is essential. Last year's budget included a target to reduce the cost of the public service by 25% by 2013/14, and we need to continue to make progress towards that target if we are going to remove the spectre of default and keep the burden of taxation as low as practical.

In the meantime the budget for 2011/12 contains measures which will reduce costs by around 10%, an important step toward achieving the 25% target. Much of this will be achieved by applying proper controls over the TCIG payroll.

The Interim Government is committed to ensuring that all public servants receive the pay and allowances to which they are entitled. At the same time we must safeguard the interests of the people of TCI and be equally sure that no public servants receive payments to which they are not properly entitled. We are in discussion with the recently formed Civil Service Association on a number of related issues as well as on the broader reform programme.

The TCIG payroll has been thoroughly reviewed to ensure that all payments are properly made and accounted for. The exercise identified a disturbing number of significant anomalies which have cost the hard working taxpayers of TCI many millions of dollars in unwarranted payments, and caused real unfairness between public servants. These can be resolved by applying existing laws properly and removing inconsistencies. We recognise that many public servants have not benefited from these payments, and we hope that by applying the rules properly we can give public servants confidence that they are being treated fairly in future, while generating significant savings that will help to reduce the need for cuts in the size of the public service.

The most significant anomalies relate to pensions. Some people have been receiving both Government and NIB pensions in full, in spite of the provisions of the existing legislation. In future, people receiving both government and NIB pensions will have their government pensions reduced by the amount of the NIB pension, in line with existing legislation, rather than receiving both pensions in full.

In spite of past practice, people employed by the government on or after 6 April 1992 have no entitlement to a gratuity; the legislation will be properly enforced in future.

Finally, people who retire from the government will no longer be able to draw both a pension and a salary on being re-employed by government.

Other anomalies relate to leave and allowances. Existing provisions in General Orders will be applied to cap the level of accumulated leave at 30 days, and no more than 30 days accumulated leave will be paid when an employee leaves the service. We will put in place a transitional scheme which will allow payment for up to 60 days leave where this is supported by proper records. This will be reduced by 2½ days each month until March 2012, when the 30 day rule will be fully enforced. Contract workers will no longer be able to accumulate annual leave to be paid upon completion of their contracts. The 10% reduction in allowances other than housing that was agreed last year will be properly applied, and the arrangements for housing, transport and other allowances will be tightened to ensure greater consistency and transparency.

All of these measures reflect the proper and consistent application of existing legislation and General Orders, and the changes will be implemented as soon as possible.

We are also proposing some changes to the TCIG pension scheme, which is closed to people who joined TCIG after 6 April 1992, in order to increase fairness and affordability. In line with normal practice for non-contributory pension schemes, and on actuarial advice, people employed by the government before 6 April 1992 will no longer be able to convert part of their government pension into a lump sum. We have listened carefully to views from public servants and from the CSA on this measure. We recognise that some have made financial plans based on past practice, so we are proposing transitional protection for those who are already nearing retirement age.

We will legislate to close the gap between the Government retirement age, at 55, and the NIB retirement age, which is 60. To eliminate that gap, the government retirement age will increase from 55 to 60, with transitional protection for those who are already aged over 50. We are seeking to create new legislation to provide a temporary reduced pension to those people employed after 5 April 1992 until they reach the age of 60. This will provide a source of income to those people until their NIB pension becomes payable. Finally, in keeping with actuarial advice, housing and other allowances will no longer be included in the calculation of government pensions.

We fully understand that these are difficult times and so we are making transitional arrangements in a number of cases to ensure that the people affected are treated as fairly as possible. Nor will we seek to recover overpayments, unless there is clear evidence that individuals receiving such payments acted improperly or were clearly aware that they were in receipt of payments to which they were not entitled.

These measures are essential to bring about a more equitable situation and to release scarce funds for use in other areas of government such as education and primary healthcare.

In addition we will further strengthen controls over recruitment, to save money and to lay the groundwork for civil service reform, by eliminating all unnecessary appointments and promotions. We are working across Government to identify the functions and posts that relate to essential public services, and we will freeze recruitment to all other posts until the rightsizing exercise is complete. We will also apply existing controls to the appointment of waged staff to reduce the number of staff and look for efficiencies in the way public services are provided, and we will apply strict controls to overtime payments, which continue to be excessive in some Ministries and Departments.

Finally, the budgetary pressures mean that we are unable to increase salaries through increments in the next financial year; we intend to review both this and the base level of salaries once TCIG's finances are well on track to achieving a surplus.

We expect that these measures will be sufficient to achieve the necessary savings during the coming financial year. However, we will monitor payroll expenditure closely and, if the necessary savings are not made we will need to take further measures during the year.

Healthcare is the next biggest element of TCIG's budget, but there is limited scope to reduce this expenditure in the short term. A new PFI contract with InterHealth Canada, signed by the previous administration, came into effect in April 2010, providing new medical centres on Providenciales and Grand Turk. The contract currently operates on a cost-plus basis; this is due for review later this year, when data on activity and costs will enable us to move to funding based on the number of people entitled to treatment.

In the medium term there is scope to reduce costs through better articulation of healthcare needs by the Ministry of Health in dialogue with InterHealth, using the management information gathered from the two medical centres by the National Health Insurance Board. There is also scope to make better use of the new facilities, for example by bringing in doctors to treat groups of patients here, rather than transporting patients to hospitals elsewhere in the Caribbean or the US for treatment, and by expanding the opportunities to raise third party revenue where TCIG receives 50% of the net profits. The development and implementation of a national Strategic Health Plan and an effective Healthcare Regulatory Authority will be essential in bringing about these changes.

In addition to the cost of the InterHealth contract, TCIG is responsible, through NHIB, for the cost of medical treatment overseas for those patients who cannot be treated within TCI. This is an area of high cost and risk, since one serious road traffic accident victim can cost more than a million dollars to treat. These costs are the subject of a reinsurance scheme negotiated by the NHIB which limits the risk to TCIG, but this area needs to be kept under close review and reserves need to be built up over time to mitigate the risks inherent in an insurance-based healthcare system, especially with the significant increase in the qualifying population since contributions began in November 2009. The NHIB is reviewing how these pressures can be managed, and we have asked them to keep TCIG informed of developments.

I will now turn to TCIG's **statutory bodies.** Subventions to statutory bodies account for almost $11 million of TCIG direct expenditure in 2010/11, and their total expenditure amounts to substantially more. Although some statutory bodies carry out important functions of government, their number and cost is high for a country the size of TCIG, and their current configuration and governance represent significant risks.

TCIG currently has insufficient oversight and control of the finances of its statutory bodies. It's important that they apply the same standards of financial discipline expected of TCIG itself, and exercise proper control over their revenues and expenditures, but this isn't always the case. For example, statutory bodies were asked to reduce their expenditure and salaries by 10% in 2010/11 but only three did so - TCInvest, the Cultural and Arts Commission and the Community College - while the Tourist Board carried out a major downsizing exercise which reduced its staffing by over 50%. The remainder appear to have continued spending at or above their original budgets, in many cases overspending their subventions and building up significant liabilities which ultimately fall to TCIG if they cannot be met from other funding sources.

In addition, some statutory bodies collect significant revenue on behalf of TCIG, but we do not have sufficient oversight to be sure that these funds are being managed in the best interests of Government as a whole, or that the appropriate amount is being collected and returned to TCIG for investment in other public services. This has a significant impact on TCIG's ability to set and meet priorities for public services and economic stimulus. Finally, there is a real concern about the strength and quality of governance in some areas, especially since some statutory bodies are responsible for significant investment in major areas of public policy.

We will therefore carry out a fundamental review to reduce the number of bodies and ensure that they are properly aligned with TCIG's overall objectives. We will also put in place a series of immediate measures to monitor and manage their finances to ensure that they remain within their budgets and do not accumulate liabilities that will ultimately fall to TCIG. Together, these measures will generate savings of 25% in 2011/12.

We are also proposing a fundamental review of **scholarships** to support students undertaking higher education. The Interim Government fully recognises the social and economic importance of providing opportunities for higher education to the young people of the Turks and Caicos Islands. But it is vital to ensure that this money is properly and effectively spent. TCI public expenditure on scholarships was $17 million in 2008/9, and it is expected to be around half this amount in the current financial year. Around 170 students studying overseas were enrolled in the scholarship programme at November 2010.

The Ministry of Finance recently carried out a thorough review of the administration of scholarship funds, with a view to ensuring maximum efficiency in the way public funds are applied to the programme. The review quickly uncovered a range of major failings in the way the scheme was operated, with serious abuses dating back many years.

Among many problems, the review found that over 35% of students were paid more than they were entitled to in their scholarship or bond agreements. There were several examples of students receiving scholarship benefits in excess of $250,000, when the maximum amounts set out in their agreements were no more than $50,000 to $90,000. Almost two thirds of students had been studying, or completed their studies, beyond the scholarship period specified in their agreements. Several students continued to receive scholarship payments for 6 years or more when the periods stipulated in their agreements ranged from 3 to 5 years, and some students continued to receive scholarship benefits for some years after they had completed their studies. Grades were typically provided by students themselves rather than by their educational institution, and some 82% of students had incomplete grade records on file.

We are therefore putting in place immediate measures to improve the management of the programme, and to terminate payments to students who are no longer entitled to them. This will have the effect of reducing expenditure to around $3.5 million in 2011/12.

For future years, we will prepare proposals to replace the existing programme with a new scheme that will focus support on the brightest and best students who would otherwise be unable to access higher education. This will be accompanied by a wider review of higher education to ensure that best use is made of the educational opportunities provided by the Turks and Caicos Islands Community College, and that educational support is more closely tied to the needs of TCIG and the wider TCI economy.

During 2010/11 the Ministries of Works and Finance undertook a **rent review** exercise. The actions arising from this review include the cancellation of some leases, negotiated reductions in others, and consolidation of government offices together with relocation to lower cost landlords. This should result in cost reductions of at least 10% during the year, with a target rent reduction cost of 25% by 2013/14.

A review of **welfare programs** has been undertaken to eliminate abuses and ensure that the criteria for these programs are met. This should result in reduced costs. We will, however, continue to monitor welfare programs to ensure that vulnerable people have access to assistance.

We are also carrying out a series of good housekeeping measures to cut TCIG's operational costs and protect essential spending in other areas. Expenditure on **utilities** and **communications** has been out of control in recent years. Bills have not been entered onto the financial system by Ministries and Departments, there has been no proper reconciliation of bills received and payments made by the Ministry of Finance, and significant arrears have built up. In the case of communications, the situation has been further complicated by a failure to properly account for telecommunications taxes and licences due from the telecoms providers. Resolving this has required a great deal of time and effort, and has resulted in the payment of arrears to utility providers amounting to $4 million during 2010/11. We now have a clear picture of expenditure going forward, which is factored into the 2011/12 budget. In addition, we will carry out spending reviews of both utilities and communications, to ensure that we are only paying for necessary services and that we are negotiating the best possible deals for TCIG and its taxpayers.

We are also continuing to reduce the costs of local and international **travel**, through applying rigorous controls to ensure that only essential travel is undertaken, and through a new subsistence policy to reimburse only reasonable costs incurred.

Finally, we will undertake a wide-ranging review of TCIG's **procurement** practices. Our initial investigations suggest that there is scope to make significant savings through better planning, aggregation and tendering of purchases.

Investing in the future

All of the measures outlined so far will have the effect of reducing TCIG's expenditure to bring it in line with likely revenues, stabilise the financial position, and allow us to start to build reserves for the future. It is clear, however, that we will also need to find funding to allow us to develop capacity in some areas of the public service, to meet the costs of civil service reform, to provide some economic stimulus, and to invest in achieving the milestones that will allow a date to be set for elections.

The budget therefore contains a provision of $8.6 million that can be made available for these priorities, subject to satisfactory growth in revenues and to the submission and approval of a robust business case. Provision has already been made within the budget to strengthen the judiciary, the Integrity Commission, and the AG's Chambers. This investment will enable us to reach the milestones by supporting the introduction of the new constitution; strengthening the criminal justice system; and investing in economic activity in under-developed sectors such as agriculture and fishing. It will also provide some funding to strengthen critical public services while the rightsizing exercise is underway, and to help civil servants to make a successful transition into new forms of employment where that is the best option for them and for TCIG.

The budget also includes a contingency of $5m to help cushion the effect of the shocks that a small island economy is prone to. It's essential to have such a cushion, to avoid the Government's finances being blown off course once more; if it is unused then it will be available to start to build reserves for the future, an opportunity that has been squandered over the last few years.

Building reserves in this way will be essential to allow TCIG to start to repay its debt and to invest in the development of infrastructure and strong public services.

Capital programme

The gravity of TCIG's financial situation means that the scope for capital expenditure will be extremely limited for the next three years. Existing commitments for 2011/12 already total $6.4 million. Of this, $3.1 million will be met by funding from the Caribbean Development Bank, the European Union and the Department for International Development, while $3.3 million remains to be met from TCIG's resources.

Some high priority projects do not yet have funding, including the rebuilding of Ona Glinton Primary School, the repair of the causeway between North and Middle Caicos, and improvements to the airport at South Caicos. Capital spending, if carefully prioritised and well managed, can also provide much needed stimulus to the economy of the Turks and Caicos Islands.

It is likely that some further capital expenditure will be needed in order to continue to provide essential services. Fuel tax receipts, which have been used to fund capital expenditure in the past, are forecast to raise $6.24 million in 2011/12, taking account of the increase from 25c to 50c which was agreed last year. At this stage we are seeking to appropriate $7.2 million for capital expenditure, which includes a provision of $0.8m for new projects. We will seek approval for new commitments against the provision during the year, on the basis of full business cases. If fuel tax receipts meet the forecast we will have a further contingency of $2.1 million; in this event we will come back with a further appropriation request.

We will continue to seek additional funding from our partners, including the Caribbean Development Bank and the European Union, and we will look for other sources of funding including private and voluntary donations to particular projects.

Government debt

Because of the financial mismanagement of the last few years, TCIG debt has soared. Formal debt rose from near zero in 2000/01 to around $115 million at the start of 2010/11; much of this was at very high interest rates, including the Consolidated Loan, negotiated last year, at 5% above LIBOR. In addition around $40 million was owed to TCIG's creditors, many of whom were local businesses who suffered hardship as a result of long overdue payments. Total borrowing will peak at around $260 million, allowing us to refinance TCIG's debt at much lower cost, and providing enough money to cover the deficits that will continue into 2012/13 even with new budget measures.

With the support of the UK Government guarantee, TCIG's debt has now been refinanced at much lower rates, providing significant savings in debt service costs for the duration of the guarantee. This provides an immediate boost to TCIG's finances, releasing money for other, more productive purposes. The level of Government debt is, however, extremely high for an economy the size of TCI, and it is essential that we manage our finances so that we can not only achieve a surplus in 2012/13, but also start to build reserves that will allow us to start to pay down debt, establish a contingency for unexpected events, and invest in infrastructure and other services for the future.

Financial management

Setting a budget is, of course, only the first step in restoring financial stability to the Government of the Turks and Caicos Islands. We also need to exercise proper financial management in order to exercise control over revenue and expenditure, monitor performance against the budget, and report the results clearly, openly and regularly. We have already made progress with this, and we intend to report financial performance to the Advisory Council and Consultative Forum on a monthly basis from the end of the first quarter of the financial year. This information will be publicly available, as a basis for greater accountability to the people of the Turks and Caicos Islands.

We are also making preparations to bring the backlog of financial accounts since 2006/07 up to date, so that we can produce audited financial statements and fulfill our obligations to be accountable to the people of the Turks and Caicos Islands.

Ladies and gentlemen, I hope this statement has given you a clear picture of the most significant elements in the budget of the Turks and Caicos Islands Government for 2011/12, and of our commitment to achieving a fiscal surplus by the end of 2012/13 as set out in the milestones. These essential corrective measures will be difficult to achieve. But the previous administration left us no alternative, and we have worked hard to ensure that the impact of the fiscal measures is spread fairly and that we can look forward to a sustainable future for the Turks and Caicos Islands.

In concluding on behalf of colleagues and advisers within the Ministry of Finance I would like to record our appreciation to HE The Governor, the Chief Executive Officer, Members of the Advisory Council and the Consultative Forum, Permanent Secretaries, Heads of Department, staff from Statutory Bodies, advisers and consultants, members of the business community and others in the private sector, and people throughout the TCI for all of their inputs to refining the proposals that form part of the 2011/12 budget.

We would also like to record our thanks to the United Kingdom Government and other members of the donor community such as the Caribbean Development Bank, the European Union, PAHO, CEDEMA, and other regional development agencies for the support they continue to provide the TCI during these challenging times.

Finally, Madam Chair, the following Bills and amendments to regulations form part of the budget documents for consideration as part of the Budget debate:

- Appropriations Bill 2011
- Business Licensing (Amendment) (No.2) Regulations 2011
- Customs (Customs Processing Fee) Bill 2011
- Casinos (Amendment) Bill 2011
- Motor Vehicles (Driving License) (Amendment) Regulations 2011
- Road Traffic (Amendment Regulations 2011

I have already provided introductory information on these Bills, including information on commencement date and fee change proposals. I hope this will suffice without the need to separately introduce each Bill. I would be happy to clarify any issues related to each Bill that arise during the debate.

Madam Chair, ladies and gentlemen I therefore commend following Bills to Consultative Forum for debate and passage:

- Appropriations Bill 2011
- Business Licensing (Amendment) (N0.2) Regulations 2011
- Customs (Customs Processing Fee) Bill 2011
- Casinos (Amendment) Bill 2011
- Motor Vehicles (Driving License) (Amendment) Regulations 2011
- Road Traffic (Amendment Regulations 2011

Thank you.