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Preliminary Assessment of the Public Finance Management and of the Economic Situation in the Turks & Caicos islands

Final Report

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Preliminary Assessment of the Public Finance Management and of the Economic Situation in the Turks & Caicos islands

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Abbreviations and Acronyms

AGD	Accountant General's Department
CAROSAI	Caribbean Organization of Supreme Audit Institutions
CARTAC	Caribbean Regional Technical Assistance Centre
CDB	Caribbean Development Bank
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CIDA	Canadian International Development Agency
COFOG	Classifications of Functions of Government
CS DRMS	Commonwealth Secretariat Debt Recording and Management System
CD	Customs Department
DEPS	Department of Economic Panning and Statistics
DP	Development Programme (Capital Investment)
DRB	Disaster Relief Board
DSA	Debt Sustainability Analysis
EC	European Commission
EDF	European Development Fund
EU	European Union
GDP	Gross Domestic Product
GFSM	Government Financial Statistics (Manual)
IMF	International Monetary Fund
INTOSAI	International Organization of Supreme Audit Institutions
IPSAS	International Public Sector Accounting Standards
MDA	Ministries, Departments and Agencies
MoF	Ministry of Finance
OPSM	Office of Public Service Management
OECD	Organisation for Economic Co-operation and Development
PAC	Public Accounts Committee
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PFMO	Public Finance Management Ordinance
PFM-PR	PFM Performance Report
PI	Performance Indicator
PSC	Public Service Commission
SFA	Special Facility of Assistance

SIGFIS	Standard Integrated Government Financial Information System
SIGTAS	Standard Integrated Government Tax Administration System
SOA	Statement of Accounts
SS	SmartStream financial management and accounting systems
STABEX	System for the Stabilization of Export Earnings (under the Lome Convention)
TAO	Territorial Authorising Officer
TCI	Turks and Caicos Islands
TCIG	Turks and Caicos Islands Government
TIN	Tax Identification Number
TOR	Terms of Reference
UN	United Nations
UNDP	United Nations Development Programme
VAT	Value added tax
VFM	Value for Money

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Summary Assessment

The European Union was providing the Government of the Turks and Caicos Islands (TCI) with direct budget support grants financed from successive European Development Funds (EDF), STABEX and the European Budget as well as specific programmes of budgetary aid. Payments of this assistance were suspended when the UK Government suspended the Constitution in 2009 in response to the findings of the Auld Commission. Such support cannot be reinstated until a further reassessment of TCI's public financial management systems, using the PEFA performance measurement framework, has shown that effective action has been taken to overcome the problems which led to the suspension of EU assistance. This report provides the required reassessment.

Scope and methodology

2. This assessment is based on the PFM Performance Measurement Framework (PMF), an integrated monitoring framework that allows measurement of country PFM performance over time. The assessment concentrates on central government and also takes into account the government's relationships with, and responsibilities for statutory bodies. TCI does not have local governments. The report encompasses the entire spectrum of PFM activities from the linking of policies to plans, budget formulation and preparation, budget execution, accounting, reporting and control to external oversight and legislative scrutiny. It assesses the current status of PFM in TCI against the internationally agreed indicators. The actual status of PFM in TCI is scored against the 28 high level indicators set out in the PFM PMF and is included in this Summary. The Framework identifies six critical dimensions of performance of an open and orderly PFM system and also assesses donor performance. The overall findings of this assignment are grouped under these criteria.

Background

3. TCI is an upper middle-income territory in the north-eastern Caribbean, adjacent to the Bahamas. Although it has had representative internal self-government since separation from the Bahamas in 1973, it remains dependent on the UK for foreign affairs and defence, and the UK has retained a residual responsibility for the performance of its government. It has undergone very rapid economic development during the last 20 years, mainly concentrated on the island of Providenciales (locally known as "Provo"), whose population increased from less than 1000 in 1970 to well over 20,000 in 2011, largely through immigration from outside TCI to build and staff the major tourist developments there. Average income per head in 2008 was estimated to be in the range of US$15-20,000 a year, although there are no well-based recent economic statistics. With a total population across all the islands currently estimated at somewhat over 30,000, TCI is a small open economy vulnerable to both external shocks and natural disasters as well as to the problems created by its own political mismanagement. Its currency is the US dollar, and there are no controls over payments on either current or capital account. It is completely dependent on tourism (including tourism-related foreign investment), which accounts for well over half of GDP.

4. TCI sustained substantial damage as a result of Hurricane Ike in August 2008, particularly in Grand Turk and South Caicos. Much of the damage to housing, schools and other government buildings remains to be repaired, a process which should be much assisted by the EC's 4.3m

Euro programme of assistance to housing reconstruction in Grand Turk and South Caicos, which has been approved to go ahead shortly under the management of the Disaster Recovery Board (DRB) established by the Governor of TCI to manage the earlier £5m assistance provided by the UK DfID. The DRB is supported by a Disaster Recovery Task Force, which also prepared the plans for the use of the EU assistance. Further EU assistance is in prospect through 11.8m Euro allocated to TCI under the 10th European Development Fund (EDF), once arrangements have been agreed between the EC and TCIG for the progressive release of these funds

5. As well as dealing with the consequences of Hurricane Ike, TCI has encountered a very sharp downturn in economic activity, which only now may be beginning to be reversed. The global recession led to a complete halt to tourism-related construction, a halt to activity in the property market, and a fall in tourist numbers. During the period of rapid growth up to 2008, TCI enjoyed buoyant government revenues from customs duties, stamp duties on property transfers, immigrants' work permit fees and accommodation tax paid by tourists. These revenues were used to finance a rapid increase in public sector employment as well as rapidly growing expenditure on public services, particularly in the health and education sectors. In addition TCIG obtained very substantial receipts from sales of Crown (i.e. public) land, which were used to finance a large development programme. The recession led to a collapse in government revenue, which fell from about $270m in 2007-08 to less than $140m in 2009-10. The resulting crisis in government finance, coupled with evidence of gross financial mismanagement by the then elected government, led the UK government to suspend the Constitution in August 2009 and reassume direct responsibility for and control over TCI..

6. It was already clear in 2006-07 that the growth of expenditure was out-running the growth of revenue. A Fiscal Stabilisation Plan was prepared in response to this, which was also a condition for the receipt of EU budget support under the 9th EDF. However, local capacity constraints and the lack of political will on the part of the then elected government precluded the achievement of any significant progress. Over the last two years the UK-led interim administration, with the assistance of a number of UK-financed advisors, has sought to restore order to TCI public finances. Current expenditure, including transfers to Statutory Boards, was reduced from about $230m in 2007-08 and 2008-09 to about $150m in 2009-10. However, the shortage of cash led to the accumulation of substantial expenditure arrears, most of which have now been paid off out of the proceeds of loans of up to $260m guaranteed by the UK Government. Tourism is currently growing at a healthy rate, although this has not yet been reflected in the starting of any major new development projects which would boost employment and revenues.

7. As was recognised in the 2011-12 Budget, continuing efforts are needed to increase revenues and reduce expenditure if TCI is to meet its objective of achieving an overall fiscal surplus in 2012-13. The Budget accordingly provided for a range of new taxes, and for increases of 35-50 per cent in most licensing fees. The 10 per cent reduction previously applied to public service pay was prolonged, and applied also to housing and other allowances and to the pay of those employed by Statutory Boards. The civil service retirement age is in process of being raised from 55 to 60, and other measures were announced to take account of National Insurance pension entitlements in calculating non-contributory pensions paid to former civil servants, and to prevent civil servants re-employed after reaching retirement age from drawing both salary and pensions. (These measures are set out in more detail in the main report below.) Actual revenue and expenditure are now being closely monitored every month, and further measures will be implemented from 1 December 2011 to increase revenues and reduce expenditure. A new Constitution has been agreed which should afford greater protection from the risks of financial mismanagement by a future elected government; it will be brought into effect as soon as the UK

is satisfied that sufficient progress has been made towards the milestones laid down as the conditions for the restoration of elected government. While significant progress has been made, more remains to be done to reduce the costs and improve the functioning of government departments, to modernise much primary and secondary legislation, including that concerning PFM (EU technical assistance is contributing to this), and to establish the conditions for sustainable economic growth

Integrated assessment of PFM performance

8. The PFM analysis has been carried out for the period 2008-09 to 2010-11 based on a review of a wide range of documentation, reports and many interviews with a number of stakeholders.

The results of the analysis are set out in table 1 below.

Table 1 Summary assessment

PFM Performance Indicator		Scoring Method	Dimension Ratings				Overall Rating
			i.	ii.	iii.	iv.	
A. PFM-OUT-TURNS: Credibility of the budget							
PI-1	Aggregate expenditure out-turn compared to original approved budget	M1	C				**C**
PI-2	Composition of expenditure out-turn compared to original approved budget	M1	D	NR			**D**
PI-3	Aggregate revenue out-turn compared to original approved budget	M1	D				**D**
PI-4	Stock and monitoring of expenditure payment arrears	M1	B	B			**B**
B. KEY CROSS-CUTTING ISSUES: Comprehensiveness and Transparency							
PI-5	Classification of the budget	M1	C				**C**
PI-6	Comprehensiveness of information included in budget documentation	M1	C				**C**
PI-7	Extent of unreported government operations	M1	D	A			**D+**
PI-8	Transparency of inter-governmental fiscal relations	M2	-	-	-		**-**
PI-9	Oversight of aggregate fiscal risk from other public sector entities	M1	D	-			**D**
PI-10	Public access to key fiscal information	M1	B				**B**
C. BUDGET CYCLE							
C(i) Policy-Based Budgeting							
PI-11	Orderliness and participation in the annual budget process	M2	C	D	C		**D+**
PI-12	Multi-year perspective in fiscal planning, expenditure policy and budgeting	M2	D	B	D	D	**D+**
C(ii) Predictability and Control in Budget Execution							
PI-13	Transparency of taxpayer obligations and liabilities	M2	C	C	C		**C**
PI-14	Effectiveness of measures for taxpayer registration and tax assessment	M2	D	C	C		**D+**
PI-15	Effectiveness in collection of tax payments	M1	C	B	C		**C+**
PI-16	Predictability in the availability of funds for commitment of expenditures	M1	A	B	C		**C+**
PI-17	Recording and management of cash balances, debt and guarantees	M2	B	A	B		**B+**
PI-18	Effectiveness of payroll controls	M1	A	A	A	B	**B+**
PI-19	Competition, value for money and controls in procurement	M2	C	A	C	D	**C+**
PI-20	Effectiveness of internal controls for non-salary expenditure	M1	A	B	B		**B+**
PI-21	Effectiveness of internal audit	M1	D	NA	NA		**D**
C(iii) Accounting, Recording and Reporting							
PI-22	Timeliness and regularity of accounts reconciliation	M2	B	C			**C+**
PI-23	Availability of information on resources received by service delivery units	M1	B				**B**

PFM Performance Indicator		Scoring Method	Dimension Ratings				Overall Rating
			i.	ii.	iii.	iv.	
PI-24	Quality and timeliness of in-year budget reports	M1	A	A	B		B+
PI-25	Quality and timeliness of annual financial statements	M1	D	D	C		D+
C(iv) External Scrutiny and Audit							
PI-26	Scope, nature and follow-up of external audit	M1	B	A	B		B+
PI-27	Legislative scrutiny of the annual budget law	M1	D	NA	NA	D	D
PI-28	Legislative scrutiny of external audit reports	M1	D	NA	NA		D
D. DONOR PRACTICES							
D-1	Predictability of Direct Budget Support	M1	D	D			D
D-2	Financial information provided by donors for budgeting and reporting on project and program aid	M1	D	A			D+
D-3	Proportion of aid that is managed by use of national procedures	M1	B				B

A brief summary of the key findings is set out in the following paragraphs.

Credibility of the budget

9. For a number of years prior to 2007-08 the ready availability of revenue (including receipts from the sale of Crown land) allowed a very lax approach to budget discipline. In 2006-07, the most recent year for which there are audited accounts, excess expenditure amounting to $39.2m was incurred on expenditure heads whose original budget was $114.8m; the overall out-turn on current expenditure showed a net increase of $21.1m over the original Estimate of $180.7m. No Supplementary Estimates were ever presented, and no steps have since been taken to regularise this excess expenditure. For 2007-08 the out-turn was only $1.9m net in excess of the original budget of $233.6m, although there were increases in some areas amounting to $20.9m offset by reductions of $19.0m elsewhere. For 2008-09 and 2009-10 the current expenditure net out-turns were close to the original budget, although there were significant reallocations between votes. But capital expenditure fell far short of budget in 2008-09 as cash was already drying up. In 2010-11 upward pressures on current expenditure (partly reflecting bills which should have been paid the previous year) were partially offset by capital expenditure being cut from a budget of $29.8m to an out-turn figure of only $7.2m. As noted in paragraph 5 above, these developments reflected a sharp contraction in available revenue, and were accompanied by an increasing volume of expenditure arrears not immediately reflected in accounts prepared on a cash basis. The bulk of these arrears have now been cleared through a number of substantial commercial loans, guaranteed by the UK Government, or been made the subject of a progressive payment agreement with the creditors in question. But some debts remain outstanding, notably arrears of contributions and rent owed to the National Insurance Board, and upward pressures continue to be felt, particularly in the area of health expenditure, where the outlook is for a significant excess over the original budget provision for 2011-12. .

Comprehensiveness and transparency

10. The budget is presented by main heads (reflecting the responsibilities of the different Ministries) with breakdowns by administrative unit and by economic classification. Revenues are broken down by reference to the nature of the tax or charge and the administrative unit responsible for its collection. The budget documentation, comprising the Budget Speech and the detailed Estimates of Revenue and Expenditure (including the previous year's out-turn and the current year's forecast out-turn), has not in recent years included any forecasts of output or inflation. The presentation of the fiscal deficit has not been in accordance with GFS norms (because debt repayments have been treated as current expenditure), statements of the debt stock have been incomplete and misleading, and no information has been presented about financial

assets. Because of unresolved issues concerning the responsibilities of Statutory Boards, some government operations have been incompletely reported, and financial oversight of Statutory Boards generally needs to be strengthened; action to ensure sufficient oversight should be complete by the end of the current financial year. Public access to information has recently been improved by the publication of in-year budget execution reports. Year-end Financial Statements and audit reports are in principle available to the general public, but no such Statements have been presented since 2006-07. (It is understood that the backlog, together with the reports of the Chief Auditor, should be cleared by the end of 2011-12.) There is full publication of tender invitations and contract awards above a minimum monetary threshold. Full information is published about staff and other resources allocated to individual secondary schools and in aggregate to primary schools and primary health clinics.

Policy-based budgeting

11. Until 2008-09 Budgets were prepared including a projection of expenditure for the two years following the year for which Estimates were presented. It does not appear, however, that these projections ever acquired any significant traction in constraining the preparation of the following years' budgets. In any event the fiscal crisis led to the forward projections being discontinued until the situation has been definitively stabilised. Although a calendar for the different stages in the preparation of the Budget had previously been established by custom and practice, it has never been enshrined in primary or secondary legislation, and the two most recent Budgets have been prepared largely by MoF, which received little in the way of constructive responses from spending Departments to its request at an earlier stage of 2011-12 budget preparation for options for reductions of up to 20 per cent. As a result most Departments had only a short time after the issue of the final MoF instructions to prepare their final 2011-12 proposals, which were to include options for reducing their overall expenditure by up to 30 per cent. The 2011-12 Budget was promulgated by the Governor before the beginning of the current financial year, but the Consultative Forum, which currently serves as a sort of substitute for an elected legislature, declined to undertake any discussion of the Budget proposals in public session because it had not been given the full details to study in advance. This year the MoF have already undertaken preparations for the 2012-13 Budget in consultation with spending Ministries, so opening the way to the resumption of a more normal procedure.

12. So far as investment planning is concerned, it is clear that, prior to 2009; there had been inadequate consideration of the consequences of major investments for future current expenditure, notably in the case of the two new hospitals built under a PFI scheme. As and when circumstances permit the resumption of significant public investment activity it will be important to ensure that projects are selected which offer the best prospects of early savings (e.g. through the restoration of government office buildings making it possible to reduce current rental payments), or at any rate the minimisation of inescapable future costs. Meanwhile a debt sustainability analysis conducted by a consultant in 2010 concluded that the current level of government debt should be manageable within the borrowing guidelines agreed in 2002 with the UK government, although it would take some years to rebuild cash reserves to the extent required. Under these guidelines net debt should not exceed 80 per cent of current revenue, and debt service (interest plus capital repayments) should not exceed 8 per cent of current revenue. Given that in the immediate future emphasis is placed on the need to achieve an overall fiscal surplus, which would by definition avoid any increase in net debt, it would be reasonable now to exclude capital repayments from the definition of debt service

Predictability and control in budget execution

13. TCI levies no annual personal or corporate income taxes, or property taxes. The largest contribution to the financing of government expenditure comes from customs duties (including a processing fee levied on all imports) which make up nearly $60 m of total budgeted current revenue in 2011-12 of some $163m. Next in size is the accommodation tax on tourists ($27m), followed by work permits for expatriate workers ($15m). The remaining revenue comes from a wide variety of fees and charges whose collection is fragmented across numerous different Departments or Statutory Boards. Substantial and non-transparent exemptions from customs and other taxes and charges have been granted in the past in negotiations with resort developers; in their absence annual revenue might have been [$30-40m] higher. The rules concerning the different revenue streams seem well enough understood by those responsible for making payments, and there is little in the way of tax assessments which could give rise to appeals. In addition to these taxes and fees there are payroll-based contributions to National Insurance and National Health Insurance which together amount to more than $40m a year.

14. Separate databases are kept for each revenue stream (even for the Insurance and Health contributions), with no automatic linkages between them. Effective enforcement arrangements are in place covering the two largest revenue generators (import and accommodation taxes), while many of the lesser revenue streams are transactions-based and thus at less risk of arrears being incurred. Only limited resources are available for audit or enforcement, which are not co-ordinated. Revenues once collected are paid into the Treasury without delay (although cheques still have to be cleared). Reconciliations are performed between the records of the collectors and those of the Treasury in the cases of revenues which are the responsibility of the Customs and Revenue Control Departments of MoF, but it is not clear that comparable reconciliations are carried out in respect of all the smaller revenue streams. Because in most cases the initiative to make payments rests with the taxpayer, it does not appear that there are substantial recognised arrears (other than in the cases of insurance and health contributions). There were apparently arrears of payments due from developers as conditions for development approvals, but further investigation found that in most cases the planned developments had not been realised.

15 . In the situation of acute cash shortage which has applied since 2008-09,cash flows have been closely monitored by the Treasury, and so far as possible forecast, taking into account known seasonal patterns of revenue and expenditure: in particular customs duty and accommodation tax receipts would normally be higher during the peak tourist season from December to March. The Government Financial Instructions prescribe that approved amounts on each sub-head should be released as cash limits in quarterly instalments which must be observed unless the CFO permits a relaxation. In the period covered by this assessment there has been very little headroom for operational expenditure on goods and services, once inescapable employment costs have been taken into account. Within these limits it appears that Departments have normally been allowed to spend up to quarterly limits, although there have been repeated attempts to identify in-year savings which would reduce expenditure below the level approved in the Budget.

16. Debt recording and reporting has been a major weakness during the period of financial crisis. Until recently no system was in operation to bring together the servicing of outstanding loans and the management of cash and overdraft borrowing. Moreover substantial arrears were also accumulated, which are in fact just another form of debt. As a result the information given in successive Budget presentations has been so incomplete as to be seriously misleading. Arrangements are now in place to keep track of debt of all kinds including overdraft, unpaid

invoices (most of which will not be beyond the normal date for payment), and older arrears. Nevertheless it would probably be a good discipline if TCI were to make use of the Commonwealth Secretariat's Debt Recording and Management System (CS DRMS) so as to ensure that matters are not overlooked after the departure of the present team of UK-sponsored advisors. With the exception of some small deposit accounts, to which special considerations apply, all the Government's cash balances are consolidated in the Treasury's two main accounts at commercial banks. The contracting of loans and the issue of guarantees has been effectively controlled by the MoF, but no clear policy has been in place to guide debt management other than the limits implied by the Borrowing Guidelines agreed with the UK government.

17. The unconstrained expansion of the government payroll, with appointments made through political patronage without any central oversight, was an important contributory factor in increasing current expenditure to unsustainable levels. Unjustified temporary appointments have since been discontinued: some steps towards this were taken even before the suspension of the Constitution. A continuing effort – already under way - will be needed to achieve a "right-sized" public service which is both efficient and affordable. Personnel and payroll records are effectively integrated, with changes to personnel records, which are automatically reflected in the pay of individuals, the exclusive preserve of OPSM. A full payroll audit has been undertaken in the course of the last year to confirm the existence and identity of all persons currently on the government payroll. Finally, both voluntary and compulsory redundancy schemes to substantially reduce the numbers employed in the public service are scheduled to be implemented by the end of March 2012.

18. Procurement is currently regulated by the Financial Instructions issued by MoF under the Finance and Audit Ordinance. All contracts whose value exceeds a certain threshold (currently $75,000, but due to be reduced in the near future to $15,000) must be let through a central Tenders Board chaired by MoF and including people with experience in planning, construction and civil engineering. Open tendering is the default method, with limited tendering or single source procurement requiring the approval of the Cabinet (in current circumstances the approval of the Governor is required). Invitations to tender are published in the local press, and where appropriate in specialised international publications. All contract awards are published in the Official Gazette. TCI-owned companies have a 5 per cent preference margin, and foreign companies can only bid for contracts below the Tenders Board threshold if they hold TCI business licences. Although the Financial Instructions require all tenders to be carefully and transparently administered, they do not provide for any specific machinery to deal with complaints. In the current straitened financial climate relatively few contracts have been let through the Tenders Board: 10 in 2009-10, with no derogations from open tendering, and 40 in 2010-11, two of which (representing less than 5 per cent of the total value of contracts supervised by the Tenders Board) were not let by open tender. The interim administration intends to replace the present Financial Instructions (which are in essence at least 20 years old) with a specific Procurement Ordinance incorporating international best practice. Meanwhile efforts are under way to improve tender documentation, so as to ensure that tender specifications are complete and fully thought through, and to improve contract management during the execution phase, so as to reduce the risks of contractors adding unnecessarily to the specification and costs of contracts.

19. In the period up to the suspension of the Constitution in 2009 there were serious gaps in internal controls which resulted in wasteful expenditure repeatedly criticised by the Chief Auditor. Proper use is now being made of the SmartStream module which records purchase orders, and raises questions if the amount involved exceeds the available provision. However,

some gaps remained in this control, particularly where operative decisions (e.g. about medical treatment for individuals, and the provision of drugs) were made outside the normal framework; action is now being taken to improve controls in the health sector. Other internal controls and procedures now appear to be functioning satisfactorily, and payments are being correctly processed. (It will be important to ensure, once there has been a return to elected government, that controls in this area are not again subject to political over-ride.)

20. There is currently no internal audit function in TCI.

Accounting, recording and reporting

21. There remain some unreconciled differences between Treasury and bank account records which have led to previous years' accounts being qualified. These differences have now been isolated so that the General Ledger as from 1 April 2011 is in balance. Reconciliations of the main Treasury accounts are carried out monthly, but there may be delays before full details are available concerning the posting of some less important revenue streams to the General Ledger Progress is being made in reconciling some minor accounts and clearing advances, although this process will take some time to complete.

22. Information about the resources provided to individual secondary schools is provided in the budget, together with aggregate information about the relatively small numbers of primary schools and health clinics. All construction projects at schools and health facilities are separately identified in the Development section of the Budget. In a very small community such as TCI information about resources for individual service delivery units cannot readily be suppressed.

23. Monthly reports of revenue and expenditure are prepared before the end of the following month, and allow detailed comparison with each item in the Budget. Although a separate report on commitments is not produced, the current requirement for the specific approval of the CFO for all payments of $5,000 or more is largely preventing any commitments from being made outside budget provision, and enables MoF to update their cash flow and full year expenditure forecasts. With the exception of the situation in the health sector (see paragraph 19 above) the information provided can be relied on as correct and complete.

24. The latest audited annual financial statements are those for 2006-07. During the financial crisis beginning in 2008 no financial statements were produced. In recent months a major effort has been made to bring the production of financial statements up to date, and those for the three years to 2009-10 had been submitted to the Chief Auditor by November 2011. Those for 2010-11 should follow shortly. In the past the statements have not been in conformity with GFS or IPSAS, although they have been produced in a consistent format over time, with explanations of the accounting standards used.. A new format is being introduced for 2009-10, with statements produced on both the former and new basis, which will be in conformity with GFS and represent a substantial step towards full conformity with IPSAS

External scrutiny and audit

25. External audit under the responsibility of the Chief Auditor covers the whole activity of government. Under section 52 of the current Finance and Audit Ordinance the Chief Auditor's remit covers all Statutory Bodies, although he may allow the audit of Statutory Bodies to be carried out by private sector auditors under his supervision. The audit covers the whole range of revenue, expenditure, financial assets and liabilities. A range of performance audits is carried

out, and significant and systemic issues are addressed. That the report on 2006-07 was not produced until September 2010 is the fault of the administration, not the Auditor. To the extent that the resources available to the Auditor have been constrained, preventing his staff from undertaking work on the spot, that is again not his fault. His reports, once completed, have been submitted without delay to the Governor (in the absence of an elected legislature), and made available to the public. Professional standards are adhered to and responses sought from auditees before audits are finalised. Following the suspension of the Constitution there is evidence that his recommendations, for example in the field of effective staff management, are being acted on by the Departments concerned.

26. There has been no scrutiny by the legislature of the two most recent Budgets. The Consultative Forum currently in operation declined to discuss the 2011-12 Budget in public because it was given so little time to do this. No Supplementary Estimates have been presented to the legislature in recent years, or more recently notified to the Consultative Forum, although there have been substantial increases each year in the amounts spent on some programmes as compared with original budgets. In 2006-07 excess expenditure of $39.2m was incurred on programmes for which the original budget was $114.8m. This has never been regularised. With the legislature suspended, there has been no Public Accounts Committee to consider the Chief Auditor's reports, and thus no question of hearings being held, or recommendations addressed to the administration.

Donor Practices

27 TCI as a relatively high income country has not been much dependent on grants from donors or soft loans from International Financial Institutions (IFIs). Public investment has generally been financed by current surpluses, receipts from land sales, and market borrowing. CDB has provided small amounts of grant aid under its Basic Needs Trust Fund Project (a poverty alleviation programme) as well as loan funds for on-lending by TCInvest to local businesses. The EU has provided modest amounts of budget support under successive EDFs, although payments have been suspended since the suspension of the Constitution in 2009. Moreover previously scheduled payments would not have been made even if the Constitution had not been suspended, since TCI was in breach of the conditions for the receipt of budget support. UK DFID provided $7.5m towards reconstruction following Hurricane Ike in 2008, and more recently UK FCO has provided funding to offset some of the costs of the criminal and civil investigations into wrong-doing by the former elected Government, which were initiated in response to the recommendations of the Auld Commission in 2009. The timing of the receipts of donor funds has generally been rather uncertain, but they have all been expended under TCI management, using TCI procedures for procurement, payment/accounting and reporting. Where funds have been advanced for post-hurricane repairs managed by the TCI Disaster Recovery Board (chaired by the Governor), a separate audit has been required by DFID, and the same arrangements are intended for an EU grant of 4.3m Euro for the same purpose, with payments expected to begin shortly (November 2011).

Assessment of the current strengths and weaknesses and their impact on PFM

(a) Aggregate fiscal discipline

28. TCI would in any event have faced serious difficulties in the management of its budget through the impact of the global recession in curtailing construction activity and tourist arrivals, and thus substantially reducing current revenues. But these difficulties were compounded by

previous fiscal mismanagement and a general lack of budgetary discipline. The failure to make transparent in-year adjustments to previously established budgets, combined with failure to enforce controls over commitments led to a situation in which TCI did not have an accurate measure of its budgetary situation and the extent of its debts. The inability over an extended period to present any annual financial statements illustrates the extent of the problem. The interim administration, with the assistance of UK-sponsored advisors has now largely brought the situation under control; steps are currently being taken in the health sector to ensure that there is a sufficient measure of control, particularly over access to publicly funded medical treatment abroad.

(b) Strategic allocation of resources

29. During the period up to 2007-08 there was an unsustainable expansion of public service employment and a very high level of public investment, as well as instances of wasteful expenditure of no benefit to the public. Current budgetary stringency, combined with efforts to reshape public service employment should in future ensure a more efficient allocation of resources. It will be important going forward to implement a much more participatory approach to budget preparation, so that spending Departments can control their own priorities within available resources, and informed decisions be taken about the impact of budget allocations on the delivery of particular public services. Room will need to be made for some increases in investment and maintenance expenditures, which have had to be cut to the bone in the situation of extreme cash shortage. EU aid towards post-hurricane reconstruction, which is now in prospect, given that the budgetary situation is in process of stabilisation, should make a useful contribution in this context. It will be important to plan the future allocation of resources over a period longer than the budget year immediately ahead, and to ensure that the consequences of decisions on public investment for ongoing current expenditure are fully recognised and taken into account.

(c) Efficient service delivery

30. Efficient service delivery has been held back by wasteful use of manpower, inadequate management of the execution of some contracts, and perverse incentives in the delivery of health services. Hurricane damage has had an adverse impact on service delivery, as well as adding to costs through the need to rent office space to replace government buildings rendered unusable through hurricane damage. While arrangements for collection and enforcement of import and accommodation taxes are effective, much scope remains to improve the efficiency of collection and enforcement of other revenue streams, including national insurance and health contributions where unification of the collection machinery offers the prospect of both efficiency savings and higher revenues. The planned introduction of VAT in April 2013 should represent a major step towards greater efficiency in this area. Work is currently in progress to address all these problems: it will be important to establish a timetable for effective action in each case.

Prospects for reform planning and implementation

31. Progress in a number of areas of PFM was previously set as benchmarks for the release of EU funds under EDF9, but in the then political climate was not achieved. Since suspension of the Constitution in August 2009, the interim administration has sought to address many of the problems, as described above. A new Constitution has been prepared which should provide a more effective foundation than hitherto for responsible fiscal management; this will be brought

into force once the UK government is satisfied that sufficient progress has been made towards the milestones established for the restoration of elected government. Work is under way, with EU and UK technical assistance, to modernise and strengthen legislation in key areas, including PFM. Preliminary drafts have been prepared of new Ordinances governing Public Financial Management, Procurement and Audit, which will need to be promulgated before the new Constitution is brought into force.

32. Substantial steps have already been taken to increase revenue and broaden the tax base. As a result revenue for 2011-12 is forecast to increase by 25 per cent as compared with 2010-11.. The implementation of these measures was aided by EU technical assistance as well as that of UK-sponsored advisors. Work is well advanced, including necessary legal drafting, in preparation for the introduction of Value Added Tax currently planned for April 2013. This should make possible a considerable simplification of the present range of different taxes and charges, as well as providing for a larger and more certain revenue stream to support the future provision of public services. Meanwhile it will be very important to maintain the improvement achieved in cash and debt management, accounting and reporting. Much remains to be done to bring all these initiatives to fruition, but the interim administration is making every effort to ensure success. The challenge for the future will be to ensure the availability of sufficient people with the requisite managerial and technical skills and experience to achieve this.

1. INTRODUCTION

1.1. *Objective of the Public Financial Management Performance Report (PFM-PR)*

1. The purpose of this PEFA evaluation is to assess the current performance of the Public Financial Management (PFM) system in the Turks and Caicos Islands (TCI), in order to identify priorities for further PFM reform, and to provide a common information base for dialogue between the government and its development partners. It has been sponsored by the European Commission (EC) as part of the analysis undertaken to determine the future eligibility of TCI for direct EU budget support. Such support was suspended when the TCI Constitution was suspended by the UK government in August 2009. .

2, The PEFA Public Financial Management (PFM) Performance Measurement Framework (PMF) is one of the elements of the Strengthened Approach to supporting PFM reforms developed by the World Bank, the European Commission and other development partners. The Strengthened Approach has three components: (i) a country led PFM reform strategy and action plan, (ii) a coordinated programme of activities financed by development partners which supports and is aligned with the government's PFM reform strategy, and (iii) a shared information pool. The PEFA PMF is a tool for achieving the third objective. .

3. It should be stressed that the PEFA PMF does not seek to assess fiscal or expenditure policy. The framework rather focuses on assessing the capacity of the elements of the system to facilitate the achievement of desired enable policy outcomes. Thus, this report does not articulate specific recommendations for PFM reform or an action plan. It is hoped, however, that the analysis presented will assist the government to define and articulate its PFM reform priorities and action plan. The intention is to assess the performance of the PFM system not that of individual officials engaged in it.

1.2. *Process of preparing the PFM-PR*

4. Following an initial half day workshop at which the main elements of the PEFA analysis were presented to Ministry of Finance (MoF) officials and others concerned, detailed discussions were held during the period 30 September-2 November 2011 with many stakeholders. These included the government's Chief Financial Officer (CFO), the Permanent Secretary, Finance, the Heads of the Budget and Economic Planning and Statistics Departments, the Acting Accountant-General, the Collector of Customs, the Head of the Revenue Control Unit and the Chairperson of the Tender Board. Others with whom discussions were held included the Chief Auditor, the Permanent Secretaries of the Ministries of Health, Education and Works, the Chairman of the National Health Insurance Board, the Directors of the National Insurance Board and the Financial Services Commission, officials of TCInvest and the President and representatives of the Chamber of Commerce. Issues were also explored with a number of the advisors currently sponsored by the UK government to assist TCIG in overcoming its financial and governance difficulties. Finally a meeting was held with H.E. the Governor and a member of his staff. The author of this report is very grateful for the open and constructive spirit in which the discussions were conducted, and for the provision of much detailed information which he has sought to reflect in the report. A first draft of much of the report was presented to MoF and other stakeholders at a workshop on 31 October 2011.

5. Following this discussion the main findings were presented orally to the EU Delegation in Jamaica on 3 November 2011, together with the consultant's preliminary conclusions on the eligibility of TCI for EU General Budget Support (GBS) and his suggestions for the conditions which might be attached to the payment of EU assistance under the 9th EDF. A complete first draft of the PEFA report was then circulated to the principal stakeholders in the TCI Government, the EU Delegation and the UK FCO and DFID. At the same time a note was submitted to the EU Delegation setting out the consultant's conclusions on the eligibility of TCI for EU GBS. A substantially revised version of the draft PEFA report was submitted to the main stakeholders in mid-December, following two rounds of detailed comments from the TCI Government (and a week's delay caused by a breakdown in telecommunications). Initial comments on this draft were received from the EU Delegation and DFID, together with approval for the consultant's request that the draft be submitted for peer review by the PEFA Secretariat. A further version of the report was then prepared, which incorporated the consultant's preliminary responses to a series of detailed comments received from the EU Delegation. That version was accordingly submitted to the PEFA Secretariat, whose comments have been taken into consideration in this text (prepared on 25 January 2012).

1.3. The methodology for the preparation of the report

6.. The assessment was prepared on the basis of the PFM Performance Measurement Framework issued by the PEFA multi-donor programme in June 2005, and takes into account the adjustments made to some of the Indicators in 2011. The PFM Performance Measurement Framework is an integrated monitoring framework that was developed as a tool to provide reliable information on the performance of PFM systems, processes and institutions. The framework relies on a set of high level Performance Indicators. Thus, the approach has been to assess the current status of TCI PFM system based on the PEFA Indicators, which comprise a set of 28 **I**ndicators that measure different aspects of the central government's PFM systems and 3 Indicators that assess the involvement of donors in the government's budgetary processes. While the main focus of the assessment is on government Ministries; the report also takes into consideration the activities of statutory bodies, some of which have important implications for government finance. The Performance Indicators, which are scored on a rating system from A to D, are presented along with a narrative to provide a brief description of the different PFM processes and procedures adopted by the government, and also to support and explain the ratings. Before presenting the Performance Indicator ratings, the report gives information about the country's economic situation, recent budgetary outcomes and the administrative structure in which PFM takes place.

1.4. The scope of the assessment as provided by the PFM-PR

7. In conformity with PEFA guidelines, the assessment of TCI's PFM concentrates on the operations of the Government as set out in successive annual Budget documents The central Government includes the Office of the Governor, the Judiciary, the Attorney-General , the Chief Auditor, and 8 ministries. The Budget also includes provision for transfers to a number of Statutory Bodies, some of which also have their own revenue streams.

8. A number of the PEFA indicators require data for the three most recent financial years as the basis for the assessment. Thus, the PEFA assessment for TCI is based, where relevant, on the experience of the financial years 2008-09, 2009-10, and 2010-11 (ending in each case on 31

March). The structure of the rest of the evaluation report is as follows. Section 2 provides background information on the economic, fiscal, legal and institutional context for the evaluation. Section 3 explains the scores for the 31 individual Performance Indicators. Section 4 describes the Government's PFM reform efforts up to November 2011, and the prospects for further progress. A series of annexes provide more detailed reference information, including the list of people consulted (Annex 1), the list of documents consulted (Annex 2), [and the TOR for the evaluation (Annex 3)].[Not attached to this draft]

2. COUNTRY BACKGROUND INFORMATION

2.1. DESCRIPTION OF THE COUNTRY ECONOMIC SITUATION, INCLUDING ECONOMIC PROSPECTS AND RISKS

9. The UK Dependent Territory of TCI consists of an archipelago of islands situated between the Caribbean Sea and the Atlantic Ocean, to the South-East of the Bahamas. Nearly three quarters of the population is on the island of Providenciales (Provo), and about one sixth is on Grand Turk, which remains the capital. Other inhabited islands are North, Middle and South Caicos and Salt Cay..

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Table 2.1 Selected Macroeconomic Indicators

	2006-07	2007-08	2008-09	2009-10	2010-11
Population statistics					
Population (Thousands)	33.2		36.6		32.2
Size of insured (NI) population (thousands)	19.1	21.6	22.4	21.2	19.7
Non-residents as % of contributors	65.5	69.6	70.7	69.2	67.0
External sector					
Imports (US$millions)	518.1	602.6	549.5	350.0	<300
Exports	14.9	18.3	24.5	18.7	17.3
Fiscal Balance (deficit -) (US$m)	-22.1	-33.5	-27.8	-23.9	-61.4
Net government debt (US$m at 31 March)	28.7	62.2	90.0	113.9	175.3

Sources: Ministry of Finance, National Insurance Board; and author's calculations (2010-11 population figure assumes population fell in line with fall in numbers of NI contributors.)

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10. TCI is a relatively high income country with a small open economy. Its GDP per capita was estimated to exceed $30,000 (at current market prices) in 2008, although no precise recent statistics are available for population, prices or GDP. (A census is due to be undertaken in the first quarter of 2012, which is expected to supply much of the currently missing data.) The economy depends primarily on receipts from tourism and externally-financed construction to offset the large trade deficit resulting from the fact that almost everything used in TCI has to be imported, while exports account for less than 2 per cent of GDP. The currency is the US dollar, and there are no controls over trade or payments. Rapid economic growth in recent years has been almost entirely concentrated on Providenciales, whose population was only a few hundred in 1970. Overall the population is estimated to have trebled over the last twenty years, although that of Grand Turk was apparently static at about 4,000 and is estimated to have declined recently to around 3,500.

11. Rapid economic growth continued until brought to a halt in 2008-09 by the combined effects of the global recession, the Government's emerging fiscal crisis and the impact of Hurricane Ike. Evidence for this is provided by the rising numbers of non-permanent resident contributors to national insurance (NI) until that time (see Table 2.1). Trade statistics show imports of most construction materials and furniture growing rapidly up to 2008, and then falling back by more than 50 per cent in 2009. This fall in imports was paralleled by a fall in non-permanent resident contributors to NI of about 17 per cent between 2008-09 and 2010-11. This suggests an overall

contraction in the population of at least 5,000 during the same period, and tends to confirm the view of business opinion that the economy has contracted by some 30 per cent or more since the pre-recession peak

12. There are now some signs – in late 2011 – of a resumption of economic growth. Tourist numbers have been rising sharply, and so has the yield of Accommodation Tax. Although customs duty receipts have continued to fall short of earlier unrealistic estimates of an 11 per cent increase, the yield from stamp duty on property transfers has been rising, which should clear the way for some resumption of construction activity. Indeed a number of large agreements with developers for new tourist facilities are currently actively under discussion and their execution can expected to be reflected in increases in the yield from customs duties (including the current processing fee), work permit fees, and road fuel duties, and thus offer the prospect of an improvement in the fiscal balance.

13. It should be recognised that TCI remains very dependent on economic developments elsewhere. Its growth since 1990 has been entirely the result of tourist developments concentrated on Providenciales. There is relatively little scope for diversifying the economy: the soil is too poor to support any significant agricultural development, there is no prospect of any major expansion of fishing, there is strong competition from neighbouring countries inhibiting the development of financial services (and OECD countries are now much more hostile to such activity than they were 20 years ago), and neither the location nor the population is conducive to any development of manufacturing. The experience of recent years has made clear that TCI cannot in the long term rely on revenue from land sales and on taxes paid by foreigners to support the provision of adequate public services. Successful development will rely on the one hand on maintaining a sufficiently attractive environment for inward investment, and at the same time having a sufficiently broad tax base to enable public services to be financed through any down-turns in tourism and tourism-related investment activity. This situation is clearly recognised by the Government, which is concentrating its efforts on developing the tax system, notably through preparations for the introduction of VAT, and on reorganising its arrangements for attracting inward investment where the statutory body TCInvest has in recent years proved expensive and ineffective. A new National Economic Development Plan is being prepared which takes full account of these requirements and constraints.

2.2. DESCRIPTION OF BUDGETARY OUTCOMES

2.2.1. Fiscal performance (see Table 2.2)

14. Current revenue was broadly stable at about $200m in the three years to 2008-09.
Receipts from land sales were at a very high level in 2006-07 and 2007-08, and remained substantial in 2008-09, although well below the amounts in the two previous years. But in 2009-10 current revenue fell by 35 per cent, while receipts from land sales largely disappeared. With the economy in deep recession, revenue did not recover in 2010-11. Only in 2011-12 is revenue projected to increase to about $160m, reflecting the introduction of new taxes, increases in existing taxes and fees, and increases in the yields of Stamp Duty on property transfers and of Accommodation Tax paid by tourists.

15. On the expenditure side there was a 50 per cent increase in employment costs between 2006-07 and 2007-08, reflecting both higher numbers and substantial pay increases. Current

expenditure then had to be reduced very sharply in 2009-10, and capital expenditure almost halted, reflecting the lack of available revenue. About two thirds of the increase in employment-related costs has been reversed in the two subsequent years. Expenditure on education was cut by about 20 per cent (from $41m in 2008-09 to $33m in 2009-10), mainly through reduced expenditure on scholarships for study abroad, while health expenditure fell from $70m in 2008-09 to less than $30m in 2009-10, the year in which the new contribution-financed National Health Insurance Plan (NHIP) was introduced to take over a substantial part of the expenditure previously falling on the Budget (see paragraph 15 below). In practice some of the reduction in cash expenditure was achieved by building up expenditure arrears, particularly in relation to the costs of treatment abroad and other non-NHIP health service costs, which have had to be cleared in the two subsequent years.

16. Overall the picture until recently has been one of steady deterioration in the Government's fiscal balance. Both current and capital expenditure were expanded unsustainably, and when receipts from land sales dried up, and current revenues fell sharply in line with the contraction of the economy, capital expenditure had to be largely halted, together with much expenditure on essential maintenance. The difficulty of cutting current expenditure in response to the fall in revenue was compounded by the fact that the government had committed itself to a major restructuring of health service provision, including the construction of two new hospitals under a PFI scheme, and the introduction of a National Health Insurance Plan under which the current costs of medical treatment for the insured population were to be borne by a new Statutory Board financed in part by contributions by employers and employees (2.5 per cent of earnings paid by both employers and employees up to a ceiling three times higher than that used for National Insurance contributions). But the Government would still have to finance through the Budget the infrastructure costs of the new hospitals, the costs of treating uninsured and indigent patients, and the continuing costs of treatment abroad for patients whose treatment was considered to be beyond the capacities of the new hospitals. The difficulty of predicting what these different costs would be in the new health service environment, and then bringing them under control, for example by preventing unnecessary referrals abroad, has represented a major challenge, and lies at the root of much of the substantial fiscal deficits incurred up to the end of 2010-11. A major review of the current arrangements is currently under way and can be expected to realise savings in FY 2012-13. The size of the overall 2010-11 deficit is not a reflection of renewed profligacy on the part of the Government, but rather the consequence of the postponement of payments which should have been made in earlier years, together with difficulty of getting a grip on the costs inherent in the new health service arrangements.

17. The 2011-12 Budget included a series of measures to increase revenues and contain expenditure. The revenue measures included:

a. imposition of a 4 per cent customs processing fee on all imports (including those by businesses entitled to customs duty exemption);
b. increase in road fuel tax from 50 to 75 cents a gallon;
c. increase in minimum business licensing fee from $150 to $300 a year, together with increases in higher rates averaging 35 per cent;
d. increases of 35-50 per cent in vehicle and driver licence fees:
e. increases of 35-50 per cent in most other fees and charges;
f. increase in royalty at duty free shops from 7 to 10 per cent:
g. higher penalties for non-compliance with accommodation and telecommunications taxes;
h. imposition of a 10 per cent tax on fees for services provided by financial institutions; and
j. imposition of a 2.5 per cent tax on insurance premiums.

The overall objective of these measures is to increase total revenues (net of grants) from about $125m in 2010-11 to more than $160m in 2011-12.

18. On the expenditure side the measures included maintenance of the 10 per cent reduction previously imposed on public service pay, together with extension to pay in statutory bodies and to housing, transport and other allowances paid to civil servants. The civil service retirement age was raised from 55 to 60, and steps were taken to adjust non-contributory public service pensions to reflect pension entitlements under the National Insurance scheme. Civil servants re-employed after reaching retirement age were no longer to be allowed to draw both salary and pension. A general review has been initiated to “right-size” the civil service, with the objective of achieving overall savings in public service pay of 25 per cent by 2013-14. Substantial progress towards this is expected to be achieved by a combination of voluntary and compulsory redundancy schemes, within the context of a restructured civil service, by March 2012.

19. Both revenue and expenditure remain under close review through the year. It is only in 2011-12 that the full cost implications of the new National Health Insurance Plan introduced in 2009 are being recognised. The Government pays through the budget $14m a year for the new hospital facilities, together with $2m a month to meet the costs of medical treatment for non-contributors to the Plan and the costs of treatment abroad for patients who cannot be treated in the new hospitals. Payments to the health service provider, InterHealth Canada Ltd during the first two years are on a cost plus basis, and fees now need to be determined for different procedures on the basis of actual experience. Referrals abroad have continued at a higher level than expected, and new arrangements have now been introduced to subject these to more effective scrutiny, while increasing the range of treatments available in the TCI hospitals. The finances of the NHIP are to be further strengthened by raising total contributions from 5 to 6 per cent of salaries, and by introducing minimum contribution amounts. At the same time the previous perverse incentive to seek treatment at the hospital Accident and Emergency facilities rather than at primary healthcare facilities is to be removed by making access free to primary health care.

Table 2.2 Out-turn of Government operations (US$ millions)

	2006-07	2007-08	2008-09	2009-10	2010-11
Total revenues and grants	**262.1**	**277.4**	**244.6**	**144.6**	**138.1**
Current revenue	206.4	209.6	200.3	133.6	122.8
Land Sales	50.5	60.9	35.4	4.6	1.2
Grants	5.2	6.9	8.9	6.4	14.1
Total expenditure	**284.1**	**310.9**	**272.3**	**168.3**	**208.6**
Current expenditure	203.0	234.2	234.4	157.4	200.5
Staff-related expenditure	63.0	90.2	88.0	82.7	69.9
Goods and services	101.8	88.5	104.9	46.4	69.1
Transfers and subventions	33.5	51.3	38.0	22.2	45.9
Capital expenditure	81.1	76.7	37.9	10.9	8.1
Interest payments	4.7	4.2	3.6	6.1	11.4
Prior year adjustment					4.2
Overall Balance (Deficit -)	**-22.0**	**-33.5**	**-27.7**	**-23.8**	**-70.5**

Sources: Financial Statements 2006-07, draft Financial Statements for later years.

2.2.2. Allocation of budgetary resources

Because of administrative reorganisations it is difficult to construct a satisfactory Table. It is intended in future to include a simple functional presentation of expenditure in Budgets and Financial Statements. The Accountant-General is considering whether the same breakdown of expenditure can be provided for recent past years. Meanwhile information about the allocation of funds to different Ministries is presented in the discussion of PI-2 below.

2.3. LEGAL AND ISTITUTIONAL FRAMEWORK FOR PUBLIC FINANCIAL MANAGEMENT

2.3.1. Legal Framework

(a)The Constitution

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20. The 2006 Constitution, which was suspended in 2009, contained no specific provisions relating to PFM, and thus did not in itself restrict the powers of the elected government in this field. Nor did it give any particular protection or authority to the Chief Auditor. The new Constitution, which will be brought into force once the UK considers sufficient progress has been made under its Milestones for the restoration of elected government, contains provisions intended to ensure that future elected governments will manage public finance in a prudent way. Section 109 requires an incoming elected government to commit itself to work within general principles for fiscal policy agreed with the UK government which will ensure affordability and Value for Money (VFM) in expenditure programmes, and support long-term financial stability for TCI.

(b)The Finance and Audit Ordinance (FAO) 1980

21. This Ordinance provides generally for financial management and audit, including preparation of the Budget, operation of the Consolidated Fund, payment and accounting procedures, financial reporting, authority to contract debt, functions of Accounting Officers, etc. It requires revision in order to provide for effective and transparent financial management and reporting in the current IT environment. Much of the necessary work has already been completed.

(c) *Public Procurement*

22. Public procurement is currently regulated by provisions in the Financial Instructions issued from time to time by MoF under the currently applicable FAO. A new Ordinance is in course of preparation.

(d) Audit

23. The authority, powers and remit of the Chief Auditor derive from FAO 1980. For budgetary purposes the Audit Office is treated as part of MoF. Under the new Constitution the budget of the National Audit Office, alongside those of the other Institutions protecting good governance, will be determined by the Appropriations Committee of the House of Assembly separately from the rest of the Budget as submitted by MoF.

(e) Revenue Generation

24. Each revenue stream (Customs Duties, Customs Processing Charge, Accommodation Tax, excise duties on road fuel, alcohol and tobacco, taxes on bank services and insurance policies, Stamp Duties on property transfers, fees for annual vehicle and drivers' licences, business licence fees, fees for work permits, etc) is determined by a separate Ordinance. The introduction of VAT planned for 1 April 2013 should make possible a considerable simplification of the tax system.

2.3.2. The Institutional Framework for PFM

25. As a UK Dependent Territory TCI has been governed in recent years by an elected government under the supervision of a UK-appointed Governor. The 2006 Constitution previously in force was suspended following the 2009 Report of the Auld Commission which found indications of serious corruption in government activities. Once the UK government is satisfied that sufficient progress has been made in relation to eight "Milestones" related to the restoration of good governance and sound public finance, and full civil and criminal investigation s of the indications of corruption, a new Constitution which has already been approved will be brought into force, followed quickly by a return to elected government. In the interim period the Governor is exercising full powers, supported by an Advisory Council, and with the advice of a Consultative Forum.

(a) The Governor.

26. In "normal" times the Governor is directly responsible for external affairs, the police, the judiciary and public appointments. He has the power to block legislation enacted by the House of Assembly, but would not normally do so unless he considered it incompatible with good governance and was supported by the UK government in his view. The Governor similarly has to approve the annual budget, consulting the UK government in the process. It is likely for the foreseeable future that the UK government will want to be satisfied about the prudence with which public finances are being managed. Article 109 of the new Constitution requires the TCI government to commit itself to managing public finance within a framework of principles agreed with the UK which will ensure full transparency and prevent any unsustainable build-up of public debt.
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(b) The Legislature

27. The Constitution provides for a House of Assembly with 15 elected members and four members appointed by the Governor in consultation with the political parties. There are to be an Appropriations Committee with the duty of reviewing the government's Budget proposals and proposing the amounts of provision for the Institutions of Good Governance (National Audit Office, Complaints Commission, Integrity Commission, Human Rights Commission, Director of Public Prosecutions), and a Public Accounts Committee to work with the Auditor-General.

(c) The Executive

28. The Governor appoints as Premier the leader of the party which commands a majority in the House of Assembly. The Constitution provides for six Ministries, which will require some reorganization of the present eight Ministries. Each Ministry is headed by a Minister who is a

member of the House of Assembly, who is responsible for setting policy. The officials responsible for executing policy in each Ministry are headed by a Permanent Secretary appointed by the Governor, who is Accounting Officer for the Ministry's revenue and expenditure. The new Constitution provides for six Ministries (to replace the current eight). It is intended that these should be: Finance; Education and Employment (including Culture, Youth and Sport); Health and Social Welfare (including Environmental Protection, Food Safety, Agriculture and Fishing); Home Affairs (including Border Control, Immigration, Citizenship, Prisons); Trade (including Tourism, Communications, Commerce, Gaming); and Public Service Management (under the CEO, with responsibility for Strategic Policy and Monitoring, Organisational Performance and Internal Audit. The Attorney-General would be responsible for the Judiciary, Crown Land Policy, and land use and planning controls over building and other development.

(d) Statutory Boards

29. In addition to the Ministries some of the functions of government are carried out by Statutory Boards which may receive funding through the Budget, but whose operations fall outside it. The most important are the National Insurance Board and the National Health Insurance Board, each of which collects compulsory earnings-related contributions from employers and employees; the current yield of contributions, at about $40m, corresponds to about 25 per cent of the government's current revenues from taxes and charges. Some Boards (Airports Authority, Ports Authority, Financial Services Commission) cover their costs in full from charges for their services, and pay over excess revenues into the Budget. TCInvest borrows from International Financial Institutions to on-lend to TCI businesses, and has a government guarantee; but it is doubtful whether sufficient provision has been made in its accounts for non-performing loans, with the consequence that the Government is at some significant financial risk. Each Board has been responsible for determining its own expenditure, and there is evidence of unnecessarily high costs being incurred. For example, it is hard to justify separate machinery to collect National Insurance and National Health contributions which use essentially the same tax base, but at present do not even exchange information about their registers of employers through whom the vast majority of receipts are collected. The interim administration has begun a review of the operations of Statutory Boards, with a view to improving financial discipline, reducing costs and maintaining effective control over the financial risks they could pose to the government. Early attention is being devoted to the merging of the procedures for the collection of National Insurance and National Health Insurance collections and to reviewing the operations of TCInvest, the effectiveness of the latter being critical to the stimulation of foreign investment in tourist facilities which will in turn impact Government revenues. In this report the Airports and Ports Authorities are treated as public enterprises, since they are in effect part of the market economy, while the other statutory boards (which include a number of bodies responsible for cultural, sporting and regulatory activities as well as the National Insurance and National Health Insurance Boards) are treated as part of general government.

3. ASSESSMENT OF THE PFM SYSTEMS, PROCESSES AND INSTITUTIONS

The purpose of the PEFA-based PFM assessment is to evaluate public financial management with focus on the central government and its functional performance through a set of 31 high-level performance indicators. These include 3 performance indicators assessing donor practices. In the case of TCI, the analysis covers all activities of government ministries and their subsidiary departments and other agencies (MDAs) currently operating in the country. The assessment also has regard to the implications of the activities of Statutory Boards under the government, some of which receive income in the form of transfers from the Budget. All SBs are required to submit annual financial statements to the Chief Auditor, who may audit them himself, or permit them to be audited by a private sector auditor under his supervision.

For the period in study, the government includes the Office of the Governor, the Judiciary, the Attorney-General, the Office of Public Service Management (OPSM), the Police, the Chief Auditor, and the 8 current Ministries.

A number of PEFA indicators require data for three years as the basis for the assessment. Data should cover the most recent completed fiscal year for which data is available and the two immediately preceding years. Thus, the PEFA assessment for TCI is based on the experience of the fiscal years 2008-09, 2009-10, and 2010-11 (the fiscal year starts on April 1 and closes on March 31). Actual expenditures and revenues referred to in this report generally relate to cash transactions only; in the context of TCI's recent experience the way Budgets and financial statements are presented requires careful analysis, given that at times during this period substantial payment arrears were incurred, which were not immediately recognised or reported. .

3.1 BUDGET CREDIBILITY

PI-1 Aggregate expenditure out-turn compared to original approved budget

Score C: Actual primary expenditure deviated from the originally approved budgeted primary expenditure by more than 15% in only one of the past three years. It deviated by 15.8% in 2008-09, by 5.0% in 2009-10 and 5.6% in 2010-11.

The ability to implement the budgeted expenditure is an important factor in supporting the government's ability to deliver the public services for the year as expressed in policy statements. Budget credibility requires actual budgetary releases to be similar to voted budgets and requires appropriate fiscal discipline to be in place. In aggregate, actual total primary expenditure deviated from the budgeted primary expenditure by 15.8% in 2008-09, by 5.0% in 2009-10 and by 5.6% in 2010-11.(Table 3.1). As the Table shows, the current expenditure out-turn fell short of Budget by 0.1 per cent in 2008-09 and by 2.9 per cent in 2009-10, but exceeded it by 8.4 per cent in 2010-11. This excess seems to have been due to arrears incurred in earlier years being partially paid off subsequently. Meanwhile capital expenditure fell far short of original budget each year: by 56.8 per cent in 2008-09, by 26.5 per cent in 2009-10 and by 75.7 per cent in 2010-11. For 2011-12 the interim administration is confident that the initial forecasts presented in the Budget will prove substantially more accurate.

Table 3.1 Comparison of Original Budgeted and Actual Expenditures: 2008-09 – 2010-11 (In millions of US Dollars, unless otherwise indicated)

	2008-09		2009-10		2010-11 (Prel.)	
Description	**Budget**	**Actual**	**Budget**	**Actual**	**Budget**	**Actual**
Primary recurrent	229.3	229.0	157.5	152.9	171.6	189.1
Capital expenditure	87.7	37.9	14.8	10.9	14..8	7.7
Primary expenditure 1/	317.0	266.9	172.4	163.8	186.4	196.8
Difference as % of budgeted primary expenditure		15.8%		5.0%		5.6%

Source: Calculations based on draft financial statements for 2008-09, 2009-10 and 2010-11..
1/Excludes debt service payments .

PI-2 Composition of expenditure out-turn compared to original approved budget (Method M1)

Score D: (i) The overall variance in expenditure composition exceeded the overall deviation in primary expenditure by more than 10% in two of the past three years. Additional variances observed were11.3% in 2008-09, 8.5% in 2009-10, and 29.7% in 2010-11. (D)
(ii) No provision was voted to the formally established Contingency Fund during the period of this report, and there were no reallocations from it. (Not Rated)

(i) Additional variance over net deviation from budgeted expenditure

This indicator measures the extent to which reallocations between budget lines have contributed to variance in expenditure composition beyond the variance resulting from changes in the overall level of expenditure. To this end, it is necessary to estimate the total variance in the expenditure composition and compare it to the overall deviation in primary expenditure for each of the last three years. Variance is measured as the sum of the absolute deviations between actual and originally budgeted expenditure for each main area of expenditure calculated as a percentage of total budgeted expenditure. In order to be compatible with the assessment in PI-1, the calculation excluded debt service.

Table 3.2 below shows the differences between budgeted and actual expenditure for each main area. The main elements of variation were a large increase in current expenditure on health services in 2008-09, balanced by reductions elsewhere. But capital expenditure fell more than 50 per cent below the large amount budgeted (see Table 3.1). In 2009-10 expenditure charged to the Health Vote fell short of budget, but the MoF made substantial payments under block 14 (Statutory Charges: Provision and Funds Contribution) which were in effect a contingency vired to specific purposes, but not provided for in the original budget. A much lower budget was set for capital expenditure, but there was nonetheless a significant shortfall in the out-turn. In 2010-11 there was a significant overall net excess of current expenditure, again driven by developments in the health sector, while only half the capital budget was spent. Only in 2010-11 did the additional variance exceed 15 per cent of the original budget, as net overall increases in current expenditure were substantially but not completely offset by reductions in capital spending. The way in which uncertain matters are treated in block 14 appears rather unsatisfactory. This section has been used to present possible additional expenditure, what are in effect arrears of expenditure from previous years, and even unallocated reductions in expenditure elsewhere in the Budget. It would be better to provide an overall sum to be placed in the Contingency Fund, and then to present Supplementary Estimates to move elements of this to where they were needed. Where provision is used to meet previous years' expenditure, it would seem better to treat this as a financing item, and adjust the expenditure recorded for earlier years. Rating for this dimension: C

Table 3.2 Composition of Budget Execution by Administrative Unit: 2008-09 – 2010-11 (In millions of US dollars + indicates excess over initial provision)

	2008-09			2009-10			2010-11		
	Budget	Out-turn	Difference	Budget	Out-turn	Difference	Budget	Out-turn	Difference
Governor	1.2	0.8	0.4	1.6	0.9	0.6	12.4	13.4	+1.0
OPSM	2.8	2.3	0.5	4.0	2.7	1.3	5.1	3.9	1.2
Police	18.4	16.5	1.9	16.0	15.2	0.8	18.6	15.8	2.8
Attorney-General	2.0	1.5	0.5	1.9	1.6	0.2	2.0	2.0	-
Judiciary	2.5	1.9	0.6	2.2	2.1	0.1	2.3	2.1	0.2
Audit	1.0	0.6	0.4	0.6	0.5	0.1	0.6	0.5	0.1
Tourism, Trade	31.2	31.1	0.1	-	-	-	-	-	-
Tourism	-	-	-	6.9	7.9	+1.0	-	-	-
Finance (inc Statutory charges)	30.0	33.1	+3.1	-	-	-	-	-	-
Finance (excl. Statutory charges)	-	-	-	10.3	10.9	+0.6	8.4	14.6	+6.2
Environment	6.1	4.5	1.6	5.2	4.1	1.0	5.5	4.9	0.6
Works	23.2	17.9	5.3	12.6	12.3	0.3	10.9	10.5	0.4
Education	45.0	41,3	3.7	32.7	33.2	+0.5	30.9	29.0	1.9
Home Affairs	17.8	14.7	3.1	11.3	11.0	0.3	9.7	8.6	1.1
Health	55.0	70.4	+15.4	35.9	29.8	6.1	44.0	52.0	+8.0
Trade, Communications	-	-	-	3.0	2.3	0.7	7.9	13.4	+5.5
Border Control, Labour	-	-	-	3.3	2.6	0.7	6.1	6.3	+0.2
MoF Statutory Charges	-	-	-	14.6	22.3	+7.7	17.4	23.5	+6.1
less debt service	7.0	7.6		4.5	6.6		10.2	11.4	
Adjusted current expenditure	229.3	229.0	0.3	157.5	152.9	4.6	171.6	189.1	+17.5
Capital Expenditure	87.7	37.9	49.8	14.8	10.9	3.9	14.8	7.7	7.1
Adjusted Total expenditure	317.0	266.9	50.1	172.3	163.8	8.5	186.4	196.8	+10.4
Overall difference (net %)			15.8			5.0			5.6
Overall variance (% based on sum of absolute variances)			27.1			13.5			35.3
Difference (%)			11.3			8.5			29.7

Source: Ministry of Finance, draft Financial Statements.

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(ii) Proportion of expenditure charged to the contingency fund

No formal use was made of the established Contingency Fund, although some apparent contingency items were included in section 14 of the Estimates alongside provision for payment arrears and unallocated reductions in expenditure. Fluctuations in amounts shown under "Provision and Funds Contribution" have been included in the calculations of variance in dimension (i) above. Given the lack of clarity and consistency in this aspect of TCI's budgeting and accounting, it seems preferable not to rate this dimension.

PI-3 Aggregate revenue out-turn compared to original approved budget

Score D: Actual domestic revenue as a percentage of originally budgeted revenue) was 76.1% in 2008-09, 69.3% in 2009-10, and 80.1% in 2010-11.

Table 3.3 Comparison of Original Budgeted and Actual Revenues: 2008-09 – 2010-11 (In US Dollars millions unless otherwise indicated)

Budget item	2008-09 Budget	Actual	2009-10 Budget	Actual	2010-11 Budget	Actual
Current revenue	247.9	200.3	159,5	133.6	159.3	126.5
Land Sales	62.0	35.4	40.0	4.6	-	1.2
Total revenue	309.9	235.7	195.6	138.2	159.3	127.7
% difference		-23.9		-30.7		-19.9

Source: Draft Financial Statements for each year.

Apart from shortfalls on receipts from land sales (see Table 3.3) the revenue shortfalls reflected lower than budgeted customs receipts in all years, markedly lower receipts from Stamp Duty on land sales in 2010-11, and widely distributed shortfalls on most of the numerous other smaller revenues from taxes and charges.

PI-4 Stock and monitoring of expenditure payment arrears

Overall score: (scoring method M1): B

(i) Stock of expenditure payment arrears (as a percentage of actual total expenditure for the corresponding fiscal year) and any recent change in the stock

Score: B. The stock of expenditure payment arrears, which may have exceeded 20 per cent of annual expenditure in 2009-10, has now been reduced to 5 per cent or less, and arrangements are in hand to pay these off once the exact amounts have been determined.

The Accounts Payable are reported through the Standard Integrated Government Financial Information System (SIGFIS) which compiles all outstanding balances due from Government bodies to banks, suppliers and contractors. Those balances represent invoices and other accounts for payment presented to the Treasury, and only become arrears if left unpaid for more than 30 days. The rating for this dimension is based on the actual position at August 2011 rather than on the figures for arrears at the end of the two previous financial years. The cash reporting conventions used for financial statements for years up to 2009-10 do not provide for the inclusion of any information about expenditure arrears.

Precise information is now available each month about unpaid invoices, with their ages in each case. At the end of August 2011 records showed total unpaid invoices at $5.2m, of which only $1.2m were more than 30 days old. In a number of cases where substantial arrears were incurred, formal agreements have been made with creditors to pay off arrears over a period of time: these are excluded from the arrears figure above, as are arrears of rent and contributions to the National Insurance Board. Arrears owed by the government to the NHIB to meet excess costs of treatment abroad, and the costs of treating patients who are “wards of the state”, have not yet been determined precisely, but are unlikely to significantly exceed $10m. In total, arrears owed outside general government have been reduced very substantially, and are now less than 10 per cent of annual expenditure. Rating for this dimension: B

(ii) Availability of data for monitoring the stock payment arrears

Score: B. Substantially complete data on the stock of arrears is available monthly and annually,

although not all amounts are yet precisely known..

A record of payments arrears can be generated at any time from the accounting system, which tracks invoices outstanding for payment through the SIGFIS General Ledger/Accounts Payable system, including the age of each unpaid invoice But there are residual uncertainties about amounts payable in the health sector, and there may still be some bills outstanding from 2009, which the suppliers concerned have not presented to the Ministries concerned because they were aware of the government's lack of cash. The accounting system cannot absolutely prevent Ministries from taking on commitments without notifying the Treasury, and in fact this happened frequently in the years before the suspension of the Constitution in 2009. MoF have now made very clear the need for all Ministries to enter their purchase orders into the system, and have warned suppliers/contractors that they should not accept orders other than in the approved purchase order format. Rating for this dimension: B

3.2. COMPREHENSIVENESS AND TRANSPARENCY

PI-5 Budget classification

Score C: The budget system is based on consistent administrative and economic classifications that broadly reflect COFOG/GFS 1986 standards, but a functional classification of expenditure is lacking, and some expenditures are not treated consistently from one year to the next.

The formulation and execution of budget revenues and expenditures are based on administrative and economic classifications which enable consistent comparisons to be made over most of the range between budgets and out-turns, and between one year and the next. They are broadly consistent with the standards set out in the IMF *Government Finance Statistical Manual* published in 1986 (economic classification) and in the United Nations *Classification of Functions of Government Manual* (COFOG) (administrative classification). However, some current revenues (fuel tax) and current expenditures are classified as capital (notably on maintenance of buildings and civil engineering assets), while Ministerial reorganisations get in the way of straightforward year-to-year comparisons, and the treatment is inconsistent from one year to the next of some elements included in MoF section 14 of the Budget for "Provisions and Funds Contribution"

PI-6 Comprehensiveness of information included in budget documentation

Score C. Budget documentation fulfils 4 of the 9 benchmarks.

The budget documentation presented (to the Advisory Council and the Consultative Forum) for financial years 2010-11 and 2011-12 covers only four of the nine benchmarks, as explained in Table 3.5 below. Nor is there any indication of medium term macro-economic prospects.

Table 3.4 Summary of Budget Documentation

Elements of budget documentation	Availability	Notes
Macro-economic assumptions, including at least estimates of aggregate growth, inflation and	No	No information is available about aggregate GDP, and there are currently

exchange rate		no TCI price statistics.
Fiscal deficit, defined according to GFS or other internationally recognized standard	No	Information about the GFS fiscal balance has not been provided. The picture has been confused by debt repayments being treated as current expenditure.
Deficit financing, describing anticipated composition	No	
Debt stock, including details of at least for the beginning of the current year	No	Details given in successive Budget Books of outstanding debt have been seriously incomplete .
Financial assets, including details of at least for the beginning of the current year	No	Information is included in financial statements when presented, but not in Budget documentation.
Prior year's budget out-turn, presented in the same format as the budget proposal	Yes	The detailed estimates provide actual expenditure for the prior year.
Current year's budget (revised budget or estimated out-turn) , presented in the same format as the budget proposal	Yes	The detailed estimates provide original budget estimates and projected expenditures for the current year.
Summarized budget data for both revenue and expenditure according to the main budget heads of the classification used, including data for current and previous year	Yes	Revenue and Expenditure are summarized by economic classification for prior year actual, current year approved.
Explanation of budget implications of new policy initiatives, with estimates of the budgetary impact of all major revenue policy changes and/or some major changes to expenditure programs	Yes	Budget statements have included indications of the expected impact of new revenue measures, etc

PI-7 Extent of Unreported Government Operations

Overall score D+ (scoring method 1**):** All domestically financed expenditure by government departments should be provided for in annual Budgets, should pass through the Treasury system, and should be included in financial reports. But in 2008-09 and 2009-10 significant arrears were incurred, not all of which were in respect of expenditure included in the relevant Budgets or have subsequently been fully reported. Expenditure by statutory bodies has generally been reported at out-turn stage, but not at budget stage. All donor-funded expenditure (loans as well as grants) is included in the Estimates as well as in out-turn reports (although the out-turns often bear little relation to the Estimates).

(i) Level of unreported extra-budgetary expenditure

Score D: Unreported extra-budgetary expenditure has been a problem in recent years as a result of the uncontrolled incurring of arrears, in many cases without provision having been included in annual budgets. Most of these have now been identified and paid off, although there are still (October 2011) some outstanding amounts, particularly where the government is liable to make payments to the National Health Insurance Board in respect of people whose treatment is outside the National Health Insurance Plan.. Budgets for the intended expenditure by Statutory Boards (including the National Insurance and National Health Insurance Boards whose expenditure and contribution income correspond to about 20 per cent of current total Budget expenditure) have not generally been published, and many of the smaller bodies are several years behind in presenting end-year financial statements. There is no sign of any "quasi-fiscal" expenditure (e.g. concealed subsidies paid through state-owned enterprises, or directed bank lending at lower than market interest rates).

(ii) Income/expenditure information on donor-funded projects, which is included in fiscal reports

Score A: Economic and financial information on projects funded by external loans and grants is included in the Estimates and Financial Statements , although the out-turn figures often bear little relation to the Budget Estimates

PI-8 Transparency of Inter-Governmental Fiscal Relations

Overall Score: NA. There are no sub-national governments in TCI.

PI-9 Oversight of aggregate fiscal risk from other public sector entities

Score D: Section 62 of the Finance and Audit Ordinance requires that all Statutory Boards receiving public funds should have their annual financial statements audited by the Chief Auditor or by a private sector auditor under his direction. Repeated questions have been raised about the accounting arrangements, employment policies and cost controls of many of these bodies, some of whose operations (notably TCInvest) represent a significant fiscal risk to the Government. No steps have yet been taken to establish consistent monitoring of these bodies, a number of which are several years late in presenting annual financial statements. But it has been agreed that the CEO's Office should take on this responsibility and recruit appropriately qualified staff to meet it.

The Government is at significant risk as a result of loan guarantees to enable TCInvest to borrow from CDB and EIB for on-lending to TCI businesses. It is also at risk through its obligation to meet certain of the costs of treatment under the National Health Insurance Plan under the management of the hospitals service provider, InterHealth Canada. Although MoF representatives sit on a number of the Boards, they have not been in a position to ensure that the bodies concerned have been run in a prudent, effective and efficient way. The CEO needs to make pro-active arrangements to ensure that all the Boards serve the public interest and avoid unnecessary costs. A review is currently being undertaken of the costs and staffing of the Statutory Boards, with a view to ensuring that a sufficient measure of control will be exerted in future over their operations, and that the contingent fiscal risks they pose are minimised. The only government shareholding in a company is a minority holding in the Providenciales water utility.

(ii) Extent of central government monitoring of sub-national governments' fiscal position

Score N/A.

PI-10 Public Access to Fiscal Information

Score B: The government makes available to the public (in a complete form) 3 of the 6 listed types of information, namely, the annual budget documentation, external audit reports and contract awards. In addition some information is available about annual financial statements and resources for primary service units (see Table 3.6).

Table 3.5 Summary of Fiscal Information

Elements of fiscal documentation	Availability	Notes
Annual budget documentation: A complete[1] set of documents can be obtained by the public through appropriate means when it is submitted to the legislature.	Yes	See explanatory notes in PI-6 above. Such information as is available is published in the Government Gazette, on the Government web-site and freely released to the press.
In-year budget execution reports: The reports are routinely made available to the public through appropriate means within one month of their completion.	No	Detailed monthly reports on revenue and expenditure out-turns are available within a few days of the end of each month, although the format needs to be adjusted to make them more readily understandable. These have apparently not yet been published, although there is an intention to do so.
Year-end financial statements: The statements are made available to the public through appropriate means within six months of completed audit.	Partially	Annual financial statements of the central government are in principle released to the public when they are presented to the Governor with the Auditor's Opinion on them. But the most recent financial statements were for 2006-07, published in September 2010.
External audit reports: All reports on central government consolidated operations are made available to the public through appropriate means within six months of completed audit.	Yes	The Chief Auditor publishes his external audit reports when they are presented to Governor.
Contract awards: Awards of all contracts with value equivalent above approx. US$100,000 are published at least quarterly through appropriate means.	Yes	Contract awards in excess of [$15,000] are published.
Resources available to primary service units: Information is publicized through appropriate means at least annually, or available upon request, for primary service units with national coverage in at least two sectors (such as elementary schools or primary health clinics).	Partially	Resources for individual secondary schools are published in full, but those for primary schools and health clinics only in aggregate. However information can be obtained on request to the relevant departments.

3.3 POLICY-BASED BUDGETING

PI-11 Orderliness and participation in the annual budget process

Overall score D+ (score method 2)**:** The Budgets for the last three years (i.e. 2009-10, 2010-11 and 2011-12) have essentially been prepared by MoF with relatively limited consultation with spending Ministries

(i) Existence of, and adherence to, a fixed budget calendar

[1] 'Complete' means that the documents made publicly available contains all the information listed under indicator PI-6, to the extent this information exists.

Score C: Before the recent fiscal crisis an understanding about the normal budget calendar had been established through custom and practice, but it was never enshrined in primary or secondary legislation. No Budget was prepared for 2009-10 until after the Constitution had been suspended in August 2009. For 2011-12 the earlier stages of budget preparation failed to establish a sufficient understanding of the constraints of the situation, with the result that MoF's final Budget Memorandum gave spending Ministries only a very short time to prepare submissions including scenarios providing for reductions in expenditure of up to 30 per cent..

(ii) Guidance on the preparation of budget submissions.

Score D; Recent Budgets have been essentially the work of MoF, with only limited consultation with the spending Ministries. This is in part a reflection of their very limited capacity to undertake financial planning and thus respond constructively to MoF requests. The final MoF Circular issued in the context of the preparation of the 2011-12 Budget did not include ceilings for the expenditure of each Department.

(iii) Timely budget approval by the legislature within the last three years

Score C: The Governor has approved the annual budget estimates within two months of the start of the last two financial years, but in the previous year the budget was not settled until nearly half the year had passed. (see Table 3.7)

Table 3.6 Dates of budget presentations and budget approvals by the Governor

Fiscal year	Presentation by PS/Finance	Consideration by Consultative Forum	Approval by the Governor
2009-10	17 September 2009	17 September 2009	9 October 2009
2010-11	21 April 2010	21 April 2010	26 April 2010
2011-12	Prepared but not presented	No consideration	5 April 2011

Source: MoF.

PI-12 Multi-year perspective in fiscal planning, expenditure policy and budgeting

Overall score (scoring method 2)**: D+**

The currently applicable Finance and Audit Ordinance (FAO) does not include any explicit provisions about fiscal policy in the medium term. However, projections of revenue and expenditure for two years beyond the year in respect of which Estimates were presented were included in Budget presentations in the years up to and including 2008-09. In the crisis situation of recent years no attempt has been made to provide information for any period beyond the year immediately ahead, although the intention to again present fiscal policy in a medium term context once circumstances permit has been repeatedly restated. The new FAO currently being prepared will include a requirement to present at regular intervals the medium term outlook for the economy and the government's fiscal balance; the government of the day will need to show that the projections of revenue and expenditure are consistent with the continued observance of the limits on government debt enshrined in the Principles of Public Financial Management adopted in accordance with Article 105 of the (new) Constitution.

(i) Multi-year fiscal forecast and functional allocations

Score D: No multi-year fiscal forecasts and functional allocations have been produced since 2008-09.

(ii) Scope and frequency of debt sustainability analysis

Score B: A debt sustainability analysis was undertaken in 2010 by consultants on behalf of the Government.

As a dependent territory without its own currency, TCI is not a member of the International Monetary Fund (IMF) and so has not been subject to the periodic reviews of debt sustainability which IMF staff members carry out in the course of regular consultations with all member states. TCI is formally subject to borrowing guidelines agreed with the UK government, under which total debt should not exceed 80 per cent of annual revenue, and debt service (interest and capital repayments) should not exceed 8 per cent of annual revenue. In present circumstances of deep recession, TCI is in breach of the debt limit. Nevertheless TCI's overall debt level is much lower in relation to national income than those of almost all independent countries in the region, and could be expected to return to conformity with the current guidelines if and when the economy recovers.

(iii) Existence of sector strategies with multi-year costing of recurrent and investment expenditure

Score D: No sector strategies with multi-year costings of current and investment expenditure have been prepared since the suspension of the Constitution in 2009. The government's Medium Term Socio-economic Development Framework published in 2008 contains statements of objectives for the development of public services, but no quantitative indications how these would be achieved.

(iv) Linkages between investment budgets and forward expenditure estimates

Score D: Budgeting for investment and recurrent expenditure remain separate processes without the recurrent cost implications of newly completed capital projects being taken into consideration in a medium term horizon.

Public service investment has been planned separately from current expenditure under the leadership of MOF Department of Economic Planning and Statistics (DEPS). Each year's Budget contains a detailed statement of that year's expenditure on all investment projects in process of execution. But the total costs of each project are not shown, and there has been no analysis of the impact of completed investments on future current expenditure. Thus two new hospitals have been built under a PFI scheme, which have substantial surplus capacity and require a very substantial ongoing commitment by the government outside the National Health Insurance Plan which is expected to meet most of the current costs of publicly provided medical treatment..

3.4. PREDICTABILITY AND CONTROL IN BUDGET EXECUTION

PI-13 Transparency of Taxpayer Obligations and Liabilities

Overall score (scoring method 2)**: C**

(i) Clarity and comprehensiveness of tax liabilities

Score C: Legislation and procedures for the numerous different taxes, fees and charges are reasonably clear, but very extensive non-transparent tax concessions and incentives are in operation, which undermine the comprehensiveness and fairness of the system.

TCI has no annual corporate or personal income taxes, nor any annual property tax. The total budgeted revenue for 2011-12 of $163m is expected to come from customs duty receipts (expected yield in 2011-12 about $60m, including the proceeds a 4 per cent processing fee charged on all imports), accommodation tax ($27m in 2011-12), stamp duty on land transactions ($9m in 2011-12) and charges for work permits ($15m budgeted for 2011-12), with the remainder coming from communications and gambling taxes, fees for business and telecommunications licences, excess revenues from airport and port operations and from the regulation of financial services and numerous other fees and charges. In the years up to 2008-09 sales of land were a very important source of revenue, but not one which could be relied on indefinitely to support the current provision of public services. It is estimated that the value of the non-transparent concessions previously granted to tourism development and other investment projects (including the electricity utility on Providenciales) is equivalent to about half the yield of customs duties. In addition there may be scope for argument about the rates to be charged, e.g. for work permits and business licences. Plans are now in hand for the introduction of Value Added Tax (VAT) as from 1 April 2013, which would represent a considerable widening of the tax base, and would offer the opportunity to simplify and/or reduce a number of present taxes, fees and charges.

(ii) Taxpayers' access to information on tax liabilities and administrative procedures

Score C. Revenue collection is very fragmented, and the user-friendliness towards the taxpayer performance of the different collecting authorities varies. The number of different taxes and charges, some of which have to be paid monthly, is such as to represent a considerable challenge to the taxpayer to comply with all of them.

(iii) Existence and functioning of a tax appeal mechanism

Score C. Arrangements exist for administrative appeals (ultimately to the Permanent Secretary Finance, advised by the Attorney-General) against customs and some other tax assessments, but little use is apparently made of them. Further appeals could then follow to the Magistrate's Court, but again there is no recent experience. Most revenues depend on the taxpayer approaching the collecting authorities to pay amounts which are clearly established. Plans for the introduction of VAT include provision for an independent appeals machinery.

PI-14 Effectiveness of measures for taxpayer registration and tax assessment

Overall Score (scoring method 2): **D+**

(i) Controls in the taxpayer registration system

Score D: Separate databases are maintained for each of the different taxes and charges, with no links between them. Very few resources are available for enforcement**.**

An EU-financed consultancy on development of the tax system in early 2011 made substantial recommendations for consolidating tax registration, collection and enforcement. However, priority has hitherto been given to possible new sources of revenue, and to increases in tax rates and charges. The first step would be to bring together the collection machinery for National Insurance and National Health Insurance schemes, which presently maintain entirely separate administrations to make collections charged on what is in principle the same tax base. Useful costs savings and improvements in administrative efficiency should be possible for both schemes, while more effective compliance should substantially increase revenues and thereby reduce the risks from the Budget having to underwrite the costs of NHIP.

(ii) Effectiveness of penalties for non-compliance with registration and declaration obligations

Score C: There are penalties in some areas (e.g. customs, accommodation and telecommunications taxes) for non-compliance, but there are very few resources for enforcement e.g. of the requirements for business licences, and arrangements do not appear very effective across the wide range of different fees and charges.

Any steps towards consolidating enforcement activity as between different revenue-collecting authorities, including linkages between databases and eventually the introduction of a unique Taxpayer Identification Number applicable to all taxes and charges, would pay dividends. The introduction of VAT in 2013 will need to be backed by effective arrangements to enforce registration and regular declaration.

(iii) Planning and monitoring of tax audit and fraud investigation programs

Score C: Customs devote some effort to risk-based inspection, and the MoF Revenue Control Unit addresses some target areas, notably Accommodation Tax but also including payments due from developers to support the costs of scholarships. But few resources are available for audit and investigation across the whole range of fees and charges**.**

PI-15 Effectiveness in collection of tax payments

Score (scoring method 1)**: C+**

(i) Collection ratio for gross tax arrears

Score C: There are no significant identified arrears in TCI's main budget revenue streams (taxes on imports, accommodation tax and stamp duty on land transfers).which together account for

about two-thirds of budget revenues. Other revenue streams (e.g. vehicle and business licences) depend on annual payments at the initiative of the taxpayer, where there is no question of the authorities identifying arrears without investigation of the reasons for non-renewal. It appears that there are arrears of national insurance and national health insurance contributions, which are outside the Budget; in the case of health contributions failure to collect amounts due results in the need for additional expenditure impacting directly on the Budget.

Comprehensive information about tax arrears is not available in a form matching the PEFA criteria. If the assessment were based strictly on flows directly affecting the Budget, there would be a case for an A rating, reflecting the fact that identified arrears are less than 2 per cent of collections. The PEFA Secretariat consider that the available information is insufficient to permit any rating. Apart from earnings-related national insurance and national health insurance contributions (where it appear that there may be significant arrears but which affect the budget only indirectly) there are no taxes in TCI assessed by the authorities where arrears are likely to be identified. TCI as yet has no personal or corporate income taxes, and VAT has not yet been brought in. There is no significant risk of arrears in respect of taxes on imports, where either goods are only released when taxes have been paid, or the goods are covered by a bond lodged by the importer. Land transfers cannot be executed without payment of tax, while in the case of accommodation tax, arrangements are already in place to enforce collection. Many other taxes and fees (e.g. business licences and vehicle licences) require the taxpayer to approach the authorities to make an annual payment. Reminders are not sent out, and few resources are available to investigate non-renewals. A special effort by MoF Revenue Control Unit in 2010-11 yielded about half the $2.5m budgeted from arrears of developers' contributions and accommodation tax. In a number of the cases concerned, it was found that the development had not gone ahead, or that the developer had gone out of business This assessment proposes a C rating, to reflect the significant risk to the Budget from uncollected arrears of NHIP contributions..

(ii) Effectiveness of transfer of tax collections to the Treasury by the revenue administration authority

Score B: All revenue is banked daily by its collectors for the credit of the Treasury. But where cheques are involved, it may take up to 3 days before they are cleared and the funds reach the Treasury accounts.

All tax and other revenue payments are made directly by cheque or in cash at the collectors' offices, and immediately paid into the Treasury account. Where cheques are involved, it may take 3 days to clear them through the banking system; no arrangements are currently in place for taxpayers to pay electronically directly into the Treasury account.

(iii) Frequency of complete accounts reconciliation between tax assessments, collections, arrears records and receipts by the Treasury

Score C: Reconciliations are carried out quarterly by MoF Revenue Control Unit and Customs in respect of the individual payments which make up the two thirds of total revenues for which they are responsible. As explained above there are no situations in which assessments are made by the authorities which could serve as a basis for the identification of arrears. These arrangements for reconciliations in respect of the main revenue streams would arguably support a B rating, but since it has not been possible to obtain assurance that other revenue streams are similarly reconciled a C rating is proposed.

PI-16 Predictability in the availability of funds for commitment of expenditures

Overall score (score method 1)**: C+**

(i) Extent to which cash flows are forecast and monitored

Score A: Cash flow planning and monitoring are the responsibility of MoF Treasury and Budget Departments. A cash flow forecast is prepared for the fiscal year and updated and reported monthly on the basis of actual cash inflows and outflows.

In the present very difficult fiscal situation MoF Budget and Treasury Departments monitor very closely the revenue inflows and expenditure outflows. Unlike countries with their own currencies, TCI, which uses the US dollar, has no access to a lender of last resort. In these circumstances the government has to satisfy its cash requirements through tax revenue, bank or other market borrowing, or through the mobilisation of external grant or loan finance. If, as happened after 2008, revenues fall sharply and funds cannot be secured from the market, the result is the accumulation of payment arrears. The initiative for cash flow monitoring rests with MoF Departments, but it reflects very close consultation with those responsible for different revenue streams and for certain key expenditures.

(ii) Reliability and horizon of periodic in-year information to MDAs on ceilings for expenditure commitment

Score B: MDAs are permitted to make forward commitments within the limits set by the expenditure provision on each budget line, but must plan on the basis that total payments in any given quarter should not exceed the amount released to them for that quarter.

Once the Budget has been approved by the Governor, MDAs are free to enter into commitments for the purchase of goods and services up to the limits of the relevant budget lines. The Purchase Orders should be entered into the commitments module of the SmartStream financial management system, and would be rejected if they exceeded the amounts available on the relevant budget lines. However, in accordance with the Financial Instructions issued under FAO, cash is released by MoF in quarterly instalments, and spending Ministries know that their payments during the next quarter should not be permitted to exceed these allocations.

(iii) Frequency and transparency of adjustments to budget allocations, which are decided above the level of management of MDAs

Score C: During the situation of fiscal crisis MDAs have repeatedly been asked by MoF during the course of the year to reduce their expenditure below previously approved levels. The need for these adjustments has generally been well understood within the Government, although the resulting reductions have not been published.

PI-17 Recording and management of cash balances, debt and guarantees

Overall score (scoring method 2): **B+.** Public debt, which was out of control at the beginning of the fiscal crisis is now fully recognised and closely tracked**.**

(i) Quality of debt data recording and reporting

Score B: Records of government debt are complete, updated and reconciled on a monthly basis. But the monitoring of contingent liabilities has been inadequate.

There was a rapid and uncontrolled increase in government debt from 2007-08 (see Table 2.1 above). TCI then found itself in a situation in which bills could not be met, and substantial payment arrears were incurred. Debt figures included in annual Budget documents were restricted to the amounts of bond issues, and excluded overdraft borrowing and other current liabilities. The interim administration has brought the situation under control, most arrears have been identified and either paid off or made the subject of agreed progressive payment plans. With the assistance of a $260m loan guarantee, the bulk of TCIG debt has been refinanced on much more favourable terms. Government cash flow and debt are now closely monitored each month, although improvements remain to be made in monitoring the contingent liabilities of Statutory Boards, and a clear account of the overall debt position has yet to be given to the general public. Control of the situation has been achieved through the work of UK-sponsored advisors: there is now a need to ensure that a sufficient continuing debt management capability is established within MoF to ensure that debt tracking and management does not again become a problem.

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(ii) Extent of consolidation of the government's cash balances

Score A: All TCIG cash balances, including those in respect of which separate accounts are maintained, are consolidated in the Treasury's main accounts at Scotia Bank and FCIB.

The Treasury has control of all TCIG cash balances which are consolidated in its two main bank accounts. All government revenues are paid directly into these accounts. Cash balances held by the National Insurance Fund and other statutory bodies are entirely separate from the Consolidated Fund, and MoF has no direct role in monitoring or managing them.

(iii) Systems for contracting loans and issuance of guarantees

Score B: The Borrowing Guidelines agreed with the UK government serve as a framework within which debt management should be conducted and loans and guarantees contracted.. Loans and guarantees are effectively controlled by MoF. But debt management policy has not been clearly specified in terms of targets for the government's overall fiscal balance.

PI-18 Effectiveness of payroll controls

Overall Score (score method 1): B+

(i) Degree of integration and reconciliation between personnel records and payroll data

Score A: A centralised personnel database is maintained for all established staff by the Office of Public Services Management OPSM), which is integrated with the MoF payroll database which underpins all wage and salary payments, including those to unestablished and casual staff.

Establishing control over public service pay, numbers and grading has been a key task of the interim administration. Numerous unjustified appointments to temporary positions have been ended, and rigorous central control of pay, numbers and grading has been established. OPSM now has exclusive control over the staff records which underlie the operation of the government payroll..

(ii) Timeliness of changes to personnel records and the payroll

Score: A: Only OPSM can make changes to individuals' records which in turn govern their pay. The large bulk of any changes are made in time for the next operation of the payroll, so that only a few retrospective adjustments need to be made**.**

iii) Internal control of changes to personnel records and the payroll

Score A Changes to the personnel records of all staff have to be justified and documented in order to receive approval from OPSM. .

Internal controls in OPSM are designed to prevent unauthorised and unjustified changes from being made to personnel records. OPSM procedures ensure that there is always an audit trail justifying whatever changes are made by reference to the relevant decisions on appointments, promotions and allowances.

(iv) Existence of payroll audits to identify control weaknesses and/or ghost workers

Score _B A full audit has been carried out of the entire government payroll, designed to test the reality of individual's appointments and ensure that there are no ghost workers. But ongoing arrangements have yet to be made to ensure that the present satisfactory situation is maintained in the years ahead.

PI-19 Competition, value for money, and controls in procurement

Overall score (score method 2)**: C+**

(i) Transparency, comprehensiveness and competition in the legal and regulatory framework for procurement

The statutory basis for government procurement is clear, and the texts of the relevant principal and subordinate legislation have been published. The Financial Instructions issued by MoF under the Finance and Audit Ordinance 1980 require all contracts above a threshold value (currently $75,000, but due to be reduced to $15,000) to be let through an interdepartmental Tenders Board, with open tendering the default method. Restricted tendering or single source procurement is permitted when circumstances require and subject to the approval of the Executive

Council/Governor. Invitations to tender are published in the press, and contract awards are published in the Official Gazette. But the regulations do not apply to procurement by Statutory Boards, there is no publication of government procurement plans, and there is no specific provision for any independent review of procurement complaints. Since three of the six benchmarks are satisfied, the rating is C.

Score _C:.

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(ii) Evidence of the use of competitive procurement methods

Score A: During the recent period of financial stringency there has been little scope for letting of contracts. All 10 contracts above the threshold let in 2009-10 (with a total value of about $790,000) were let by open tender. 38 of the 40 contracts (total value about $2,850,000) let in 2010-11 were let by open tender; the remaining two, representing less than 5 per cent of the total value of the contracts, related to specialised technical assistance for the installation of the ASYCUDA World Customs system which could not have been procured elsewhere.

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(iii) Public access to complete, reliable and timely information about government procurement

Score C Full information is provided about bidding opportunities and contract awards, but there is no advance publication of procurement plans or of any information about the results of procurement complaints..

(iv) Existence of an independent administrative procurement complaints machinery

Score: D In order to score higher than D, there must be a procurement complaints machinery involving both independent professionals and representatives of civil society, who are independent of the contract awarding process. No formal arrangements have been made for dealing with procurement complaints which cannot be resolved administratively. There being no body established to consider procurement complaints, whether or not independent of the authorities responsible for procurement, neither of the first two benchmarks is satisfied. MoF stated that if a complaint arose which required some independent adjudication, it would be referred by the Attorney- General to the UK lawyer with experience of TCI affairs who is retained by the TCI government. But there had been no recent experience of this procedure, which is informal rather than statutory. Although this procedure could be seen as professional and independent, and as not requiring complainants to pay heavy fees, there is no local involvement of people from outside government. Moreover no rules have been specified to determine the procedures to be followed, the timeframe within which the work would be done, or the authority of any decisions or recommendations by the adjudicator.

PI-20 Effectiveness of internal controls for non-salary expenditure

Score (score method 1)**: B**+

Internal control procedures for non-salary expenditure now appear to work reasonably well, having previously broken down during the period up to 2008-09.

(i) Effectiveness of expenditure commitment controls

Score: A: The Smartstream commitments control module is now (as of April 2011) fully operational, and both spending Ministries and suppliers should understand that government orders should only be accepted if the approved Purchase Order form is used, which shows that the commitment has been registered with MoF and is not inconsistent with approved budgetary provision. Orders would be rejected if the amounts involved exceeded the funds available on the relevant budget line. No commitment control system can be entirely proof against suppliers accepting orders which have not been registered with MoF and which are not provided for in budget Estimates. But the personal responsibility of Accounting Officers for preventing such irregularities, and the risks suppliers face of delay or non-payment of their eventual invoices should ensure that most commitments are captured.

(ii) Comprehensiveness, relevance and understanding of other internal control rules/procedures

Score B: Basic internal control rules and procedures exist for initiating, processing and recording transactions, which are currently generally understood and respected by those involved. But there remain risks that activities and intentions may be held back by administrative inefficiency and delays. The authority of the finance function could usefully be strengthened when detailed regulations are made about the way in which the new FAO currently being prepared should be applied.

The current Financial Instructions which prescribe, inter alia, that officers responsible for placing orders should not be responsible for authorising the subsequent payments, also lay down arrangements for safeguarding and accounting for stores, cash and other assets. These appear now to be reasonably well observed, although there are indications of administrative inefficiency and delay. It will be important to ensure that the new FAO currently being prepared is accompanied by a revision to the Financial Instructions to bring them up to date in the present electronic environment, and to provide, so far as possible, for the automated enforcement of appropriate financial controls and procedures..

(iii) Degree of compliance with rules for processing and recording transactions

Score B: Compliance with existing rules for processing and recording transactions appears now to be satisfactory. But the experience up to 2008-09 illustrates the risk that rules may be flouted by decision of those in authority. Although the payments process is operating satisfactorily, it is not yet clear that the culture of accepting non-observance of the rules, e.g. in the making of transparent arrangements for in-year budget changes and reallocations, has been completely eliminated.

Once commitments have been made, there is no current evidence of MDAs failing to observe the rules for processing and recording transactions. The Treasury checks the documentation attached to all payment requests, and further tests of such transactions are undertaken in the course of the annual financial audit carried out by the Chief Auditor.

PI-21 Effectiveness of internal audit

Overall score (score method 1)**: D** The Internal audit function currently does not exist in the TCI government**.**

(i) Coverage and quality of the internal audit function

Score D: No internal audit work is currently carried out as a regular activity in the TCI public service.

It should be noted here that much of the work currently being done by UK-sponsored advisors in restoring the integrity of operating systems has some of the quality of internal audit. But they have been in a position to exercise a degree of de facto authority which would not normally be the preserve of an internal auditor. As the advisors' work comes to an end, it will be important to build an element of internal audit capacity to support management both in MoF and in spending Ministries. .

(ii) Frequency and distribution of reports

Score NA: In the absence of the function there are no reports to be considered.

(iii) Extent of management response to internal audit function

Score NA: There is no question of a management response where the function does not exist.

3.5. ACCOUNTING, RECORDING AND REPORTING

PI-22 Timeliness and regularity of accounts reconciliation

Overall score (score method 2)**: C+**

(i) Regularity of bank reconciliation

Score B: Bank reconciliation for the main Treasury-managed bank accounts takes place at least monthly, at aggregate and detailed levels, usually within four weeks of end of period. .

The restoration of discipline in this aspect of Treasury activity has been an important task of the interim administration, with the assistance of UK-sponsored advisers. Bringing reconciliations up to date has been an essential precondition for producing the financial statements for the years since 2006-07. A line has been drawn under the unreconciled differences between Treasury and bank account records which led to the qualification of the accounts in the years up to 2006-07.

Draft financial statements for the years 2007-08 to 2009-10 have just been completed and submitted to the Chief Auditor, and those for 2010-11 should follow shortly.

(ii) Regularity of reconciliation and clearance of suspense accounts and advances

Score C: Reconciliation and clearance of suspense accounts and advances take place at least annually, but there may be delays in clearing suspense accounts, and some minor advances remain uncleared.

Reconciliation and clearance of suspense accounts and advances have been carried out at least annually in all cases, with suspense accounts cleared more frequently, although sometimes subject to some delays as revenue items are posted correctly to the General Ledger. Information about advances is included in the Financial Statements, which show the total outstanding increasing from $4.7m in March 2008 to $5.4m in March 2010 and $5.5m in March 2011 It is understood that further efforts will be devoted to clearing the accounts of advances to public officers, although movements in the amounts in question will not have had a significant impact on government finance overall.

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PI-23 Availability of information on resources received by service delivery units

Score B (score method 1**):** Full information is given in the Budget about resources for individual secondary schools. Aggregate data is presented about primary schools and health clinics. In a very small community such as is TCI information about the resourcing of primary schools and health clinics can always be obtained through direct enquiry from the responsible departments**.**

PI-24 Quality and timeliness of in-year budget reports

Overall score (score method 1)**: B+**

(i) Scope of reports in terms of coverage and compatibility with budget estimates

Score A: Comparison between budget estimates and actual out-turns of revenue and expenditure is possible by administrative unit and economic classification. The reports include full information also on capital receipts and development expenditure. Information is presented in terms of cash receipts and payments, but the current requirement for the CFO's specific authorisation for all payments of $5,000 or more, coupled with the capture in SmartStream of all Purchase Orders, makes it possible to track commitments and thus provides an important element in the detailed monthly forecasts of payments on each budget line up to the end of the current financial year..

(ii) Timeliness of the issue of reports

Score A: In-year budget reports covering all items of revenue and expenditure, are prepared on a monthly basis, and generally issued before the end of the following month.

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(iii) Quality of information

Score B: There are no major concerns about accuracy and consistency of financial data amongst the various fiscal reports.

The reports generated through SIGTAS comprise most of the information required for reconciling any differences and performing a complete fiscal analysis on a timely basis.

PI-25 Quality and timeliness of annual financial statements

Overall score (score method 1)**: D+** This Indicator is difficult to rate at present (November 2011) because no government Financial Statements have yet been published for any year subsequent to 2006-07, for which the Statements were issued in July 2010.

(i) Completeness of the financial statements

Score D: Although the FAO currently in force requires a consolidated set of government Financial Statements to be prepared annually for TCI, this has not yet (November 2011) been done for any year later than 2006-07. The Statements should cover revenue, expenditure, bank account balances and the stock of other assets and liabilities.

The Financial Statements cover government entities only, including transfers to Statutory Boards (SBs). The transactions of SBs (including the National Insurance Scheme and the National Health Insurance Plan) are excluded. Expenditure on donor-funded projects is included. The format of the Statements is currently in process of revision. When this is complete the Statements will include:

- Consolidated Statement of Assets and Liabilities
- All Funds: summary Statement of Receipts, Payments, Overall Surplus/Deficit (GFS basis) and Financing, with separate Statements for Consolidated Fund and Development Fund
- All Funds : payments and receipts by function (COFOG)
- Detailed Statements of Current Revenue and Expenditure by administrative unit responsible
- Capital Expenditure by project and source of finance
- Statements of Advances, Deposits and Investments
- Statement of Public Debt
- Statement of Contingent Liabilities

(ii) Timeliness of submissions of the financial statements

Score D: The Financial Statements for 2009-10 have only very recently (November 2011) been submitted for audit. Audit of the Statements 2007-08 and 2008-09 Statements, which were submitted in September 2011 is not yet complete.

The current FAO requires the draft the annual Financial Statements to be submitted for audit within 6 months of the end of the financial year to which they relate, and for the audit to be completed within 3 months thereafter. The new FAO will give the Treasury 4 months to prepare the Statements and the Auditor 3 months for his audit. At end-November 2011 audit was in process of the Statements for the three years to 2009-10, with those for 2010-11 expected to be submitted for audit in the near future. It is expected that the audit of all the years up to 2010-11 will be complete by the end of 2011-12.

(iii) Accounting standards used

Score C: International accounting standards have not yet been fully applied. The financial statements have in the past been presented in a consistent format, with some disclosure of the standards used..

When the Financial Statements have been presented in the proposed new format, they will be substantially in conformity with the International Public Sector Accounting Standards (IPSAS) for cash-based accounting

3.6. EXTERNAL SCRUTINY AND AUDIT

PI-26 Scope, nature and follow-up of external audits

Overall score (using methodology M1): B+__

(i) Scope/nature of audit performed (including adherence to auditing standards)

Score B: A comprehensive audit of the government's Financial Statements is carried out every year, together with a range of specific audits which include some Value for Money (VFM) examinations. These include supervision, and in some cases performance, of the audit of Statutory Boards. Auditing standards are adhered to. But the extent of detailed audit is currently constrained by the reduction in the resources allocated in the Budget for this purpose.

The reports made by the then Chief Auditor were an important starting point for the enquiries of the Auld Commission into corruption and financial mismanagement in the period before the suspension of the Constitution in 2009. Audit work has generally been of a good standard, and systemic issues have been addressed in special reports. The new Constitution will strengthen the position and authority of the Chief Auditor, and provide greater assurance that he/she will have access to the necessary resources.

(ii) Timeliness of submission of audit reports to legislature

Score A: Audit reports have recently been submitted to the Governor within 3 months of the receipt of the financial statements from MoF. This was the case in respect of 2006-07, the most recent year for which audited statements have been published. It has not been the fault of the auditor that recent Financial Statements have been produced so long after the event.

(iii) Evidence of follow up on audit recommendations

Score B: Evidence from the Audit Office indicates that many recommendations, especially in the context of VFM work, receive a positive response from the bodies audited, and that the situation has improved since the suspension of the Constitution in 2009.

It would be helpful if the responses of audited bodies to recommendations in the Chief Auditor's reports were always clearly documented on the public record, as they would be if the responses were required to be published alongside the auditor's conclusions and recommendations. Recent Special Reports (e.g. the May 2011 Report on the Road Safety Department which is responsible for the issue of vehicle and driver licences) have included the Management's responses to each recommendation, including the timescale within which action would be taken.

PI-27 Legislative scrutiny of the annual budget law

Overall score (using methodology M1): **D**

(i) Scope of the legislature's scrutiny

Score D: There is currently no functioning Legislature..

The new FAO currently being prepared will provide for the Legislature, once the new Constitution has been brought into force, to be given regular reports about the macro-economic background against which the government's fiscal policies are being pursued, and will require the Budget Estimates for the following year to be submitted to the Legislature at least 6 weeks before the beginning of the year to which they relate.

(ii) Extent to which the legislature's procedures are well-established and respected

Score NA: No such procedures are currently in operation. The Consultative Forum which currently fulfils some of the functions of a legislature declined to consider the 2011-12 Budget because it was given so little time to do this.

The new FAO will lay down some essential procedures for consideration of the Budget by the Legislature. It may be desirable to supplement these in secondary legislation issued under the new Ordinance.

(iii) Adequacy of time for the legislature to provide a response to budget proposals both the detailed estimates and, where applicable, for proposals on macro-fiscal aggregates earlier in the budget preparation cycle (time allowed in practice for all stages combined)

Score NA: In present circumstances, when there is no legislature, this dimension is not applicable..

(iv) Rules for in-year amendments to the budget without ex-ante approval by the legislature

Score D: The currently applicable FAO requires Supplementary Estimates to be submitted for approval by the legislature (in present circumstances this means the Governor) when provision on any subhead in the Budget proves inadequate The Permanent Secretary, Finance is authorised to allow funds to be moved from one line to another within a subhead, but such virements are required to be reported without delay to the Legislature/ Governor and thereby published. These requirements were ignored by the elected government in the period up to 2009, and the interim administration has not yet taken any steps to formalise and make transparent in-year changes in budgetary allocations..

It is desirable that the interim administration should comply with the discipline of transparent publication and approval of in-year changes to budget allocations. This would reintroduce good habits in advance of the enactment of the new FAO, which will similarly insist on transparent arrangements for the proper authorisation of in-year changes.

PI-28 Legislative scrutiny of external audit reports

Overall score (scoring methodology M1): **D**

(i) Timeliness of examination of audit reports by the legislature (for reports received within the last three years)

Score D: No such examination currently takes place. No reports were considered by the Public Accounts Committee of the House of Assembly during the 18 months before suspension of the Constitution, and no reports were made by the PAC to the House in recent years.

The new Constitution and FAO will impose responsibilities on the PAC which should prove more difficult to ignore.

(ii) Extent of hearings on key findings undertaken by the legislature

Score NA: There was no functioning Legislature during the reference period.

(iii) Issuance of recommended actions by the legislature and implementation by the executive

Score NA: There was no functioning Legislature during the reference period.

3.7. DONOR PRACTICES

This section uses three high-level performance indicators to measure the performance of donors involved in the government's budgetary processes.

D-1 Predictability of Direct Budget Support

Score: D (scoring method 1):

(i) Annual deviation of actual budget support from the forecast provided by donor agencies at least six weeks prior to the Government submitting its budget proposals to the legislature (or equivalent approving body)

Score D Actual receipts fell more than 50% short of Budget Estimates in two of the last three years .

Direct budget support consists of all aid provided to the government in support of the overall budget (general budget support) or for specific sectors (sector budget support). When received the funds will be used in accordance with the procedures applying to all other general revenue. Identified budget support may be channelled through a transit account before being released to the Treasury.

Funding provided by direct budget support from the EU, UK (DFID and FCO) and CDB has constituted a significant source of financing for the government of TCI, although it has never exceeded 7 per cent of total current and capital expenditure. The timing of EU budget support payments should in principle be predictable, given that it is agreed well in advance and is conditional upon the achievement of specified objectives agreed between EU and TCI. However, during the period covered by this report, EU budget support payments have been suspended in response to the events which led to the imposition of UK direct rule. UK assistance during this period has been provided either as a response to the need to repair damage caused by Hurricane Ike, or to reimburse TCI costs incurred in investigating possible corruption. The latter payment was notified to TCI only towards the end of 2010-11.

Table 3.7 Total Direct Budget Support: Budget versus Actual in US$m

	2008-09	2009-10	2010-11
CDB			
Budgeted	1.4	0.7	1.0
Disbursed	0.3	0.1	0.6
UK (DFID and FCO)			
Budgeted	.0.5	7.5	3.6
Disbursed	0	3.4	13.2
EU			
Budgeted	0	0	8.7
Disbursed	0	0	0
Total Deviation	-1.6	-4.7	+0.5

Source: Budget Books.

(ii) In-year timeliness of donor disbursements (compliance with aggregate quarterly estimates)

Score D:[There is no schedule of donor disbursements by quarters. DfID assistance to post-hurricane reconstruction was paid in instalments as work under TCI control was executed.

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D-2 Financial information provided by donors for budgeting and reporting on project and programme aid

Score: D+ (scoring method 1): No projects in TCI have been executed under the control of the donors concerned. Where TCI has had donor assistance, mainly for post-hurricane reconstruction, work has been carried out under the management of the TCI Government, in some cases with an element of pre-financing by the donor (EU and DFID) and in others (CDB) with TCI financing the work initially and then claiming reimbursement from the donor. The timing of payments has not generally been planned in advance consistently with the requirements of an annual Budget calendar.

(i) Completeness and timeliness of budget estimates by donors for project support

Score:D Project aid has generally been a response to hurricane disasters, and decisions have not had regard to the timing of Budget preparations**.** Prospective payments have been the subject of prior agreement between the donors and TCI, but the amounts have not been determined up to 15 months in advance as would be required to meet the Budget calendar**.** TCI has controlled the actual timing of project execution and thus the timing of claims for reimbursement or further advances...

(ii) Frequency and coverage of reporting by donors on actual flows for project support.

Score: A : The direction of reporting is from TCI to the donors. The actual payments by the donors serve as the disbursement reports.

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D-3 Proportion of aid that is managed by use of national procedures

Score: B All activity in TCI financed by external grants or IFI loans is fully accounted for through the Budget, and uses TCI procurement, payment and reporting procedures. In the cases of EU and DFID assistance directed towards a specific purpose (the repair of hurricane damage), a separate audit has been required. The overall average use of TCI procedures is therefore at least 75 per cent. However, since the amounts of project aid subject to this requirement have recently been large relative to payments of budget support, the overall average use of national systems will not have reached the 90 per cent required for an A rating.

4. GOVERNMENT REFORM PROCESS

4.1 Recent and On-going Reforms

1. As has been noted widely elsewhere in this report, TCI has been undergoing an intensive programme of PFM and other administrative reforms since the Constitution was suspended in August 2009. Much of the work has been done by a team of advisors sponsored by the UK government working closely with local staff. In addition to this the EU has provided technical assistance in producing plans to improve the generation and control of revenues, and to the improvement and modernisation of a wide range of legislation applicable in TCI. The main elements of PFM reform have been as follows:

(i) Preparation of a new Constitution which will better ensure the maintenance of fiscal discipline and transparency; The new Constitution has been approved, and will be brought into force when the Governor determines that enough progress has been made against the "milestones" specified by the UK government for the restoration of elected government in TCI.

(ii) Preparation of new PFM legislation consistent with the new constitutional provisions governing financial management, audit and procurement. Working drafts of these Ordinances have been prepared, which are now being refined by UK and EU consultants.

(iii) Measures to bring public expenditure under better control, and into line with prospectively available resources. These have included work to identify and pay off expenditure arrears incurred when revenue collapsed under the combined impact of the global recession and local financial mismanagement; measures to reduce pay and casual employment in the public sector; measures to reorganise government Ministries with a view to greater economy and efficiency, including steps to "right size" public service employment in relation to the rest of the economy; measures to reduce wasteful expenditure by Statutory Boards; and measures to improve funding and reduce costs in the publicly provided health service. While much has already been achieved in each of these areas, work is ongoing to bring them to fruition.

(iv) Measures to increase revenues by raising the rates of existing taxes and charges, by introducing new taxes, and by improving the collection and enforcement arrangements. Efforts so far have concentrated on raising more revenue through new taxes (e.g. on communications, banking services and insurance premiums) and on improving collection and enforcement arrangements where responsibility rests with the MoF Revenue Control Unit. Preparations are on track for a further widening of the tax base through the introduction of VAT in April 2013, which should also make possible the simplification of the overall revenue system through the substitution of VAT for a number of existing taxes.

(v) Measures to improvement cash and debt management and reporting, so as to prevent a recurrence of the disorderly situation which led to substantial expenditure arrears being incurred between 2008 and 2010, which were not effectively recognised and tracked. Treasury records and reconciliations are now up to date, and the backlog of audited government Financial Statements since 2006-07 is well on the way to being cleared Meanwhile substantial debts incurred in recent years have been refinanced on favourable terms with the benefit of a loan guarantee of up to $260m by the UK government. It will be important now to ensure that the

Treasury has sufficient resources and capability to ensure that track is not again lost of the government's underlying financial position..

2. Emphasis has so far necessarily been placed on what may be seen to be the "negative" aspects of action to improve PFM performance, i.e. measures to cut expenditure and raise revenue, notwithstanding the fact that the TCI economy remains in deep recession. It would be helpful if the interim administration were able to take some initiatives to raise the level of economic activity. The attraction of one or more major new tourism-related investment projects through the offer of transparent incentives, particularly if it were on Grand Turk which will feel the main brunt of any reduction in public service employment, would be an important step. It could also be useful if the Government were able to identify a limited number of investment projects which have been suspended or held back, where the resumption of work could generate a very rapid cost saving, either by enabling the asset in question to be sold, or by avoiding subsequent increases in inescapable costs which would result if work were further delayed.

3. The assistance in prospect from the EU could be very significant both in permitting some relaxation of fiscal stringency, and in generating much needed activity on Grand Turk and South Caicos which suffered most from Hurricane Ike in 2008, and which are in most need of the diversification of employment opportunities. If the EU were satisfied that sufficient progress has been made in turning round public finances, the unblocking of 3.8m Euro outstanding from the 9^{th} EDF would immediately help the fiscal balance, while the provision of 4.3m Euro already agreed for post-Ike reconstruction through the Disaster Recovery Board (DRB) should provide an early boost for activity and employment. The 9.8m Euro remaining after the allocation of 2m Euro of the 10^{th} EDF allocation to technical assistance, once released will have an impact on the economy of TCI similar to that of the funds spent through the DRB

4. In the longer run the challenge to TCI will be to maintain the improvement of PFM performance when the short-term advisors who have contributed greatly to its achievement, working closely with local staff, have concluded their assignments. The "right-sizing" initiative has drawn attention again to the situation in the TCI public service which has relatively numerous positions for lower-skilled employees, but needs reinforcement at the professional and managerial level, not least in the Ministry of Finance, in order to overcome future challenges. The need to restructure some departments of MoF so as to fill skill gaps of importance in providing the services needed by a dynamic economy is expressly recognised. More generally continuing efforts will be needed to strengthen the professional skills and experience of the public service. Some outside assistance will almost certainly be needed for at least several years ahead.

Annex 1 to TCI PEFA Report

List of persons consulted

H.E. Mr Ric Todd, Governor of the Turks and Caicos Islands
Mr Philip Rushbrook, Director, Governor's Office
Mr Garth Armstrong, Economic Adviser to the Governor

Ministry of Finance
Mr Hugh McGarel-Groves, Chief Financial Officer
Mr Delton Jones, Permanent Secretary, EU Territorial Authorising Officer
Ms Anya Williams, Budget Director
Ms Kathleen Forbes, Head of Department of Economic Planning and Statistics
Mrs Desiree Lewis, Under Secretary, Chair of Tenders Board
Mr Henry Saunders, Revenue Controller
Mr Stuart Taylor, Collector of Customs
Ms Linda Malcolm, Deputy Collector of Customs
Ms Athenee Harvey, Acting Accountant-General
Mr Shirlin Forbes, Senior Statistician, DEPS
Mr Sheldon Wilson, Debt management, DEPS
Ms Shatel Williams, Finance Manager, Treasury
Mr Horatio Tuitt, Secretary Disaster Recovery Task Force

UK-sponsored advisors
Mr John Murphy, Revenue
Mr Stephen Turnbull, Payroll and Statutory Bodies
Mr Stephen Catchpole, Government Organisation and Civil Service Restructuring
Mr Robert Hawkins, Accounting and Reporting
Ms Jennifer Sinclair, Treasury management and organisation
Mr Nigel Hearnden, Procurement

Other Ministries
Mrs Judith Campbell, PS/ Ministry of Health
Mr Derek Taylor, Adviser on Health Policy, Member of NHIP Contract Management Committee
Ms Linda Williams, Undersecretary/OPSM
Ms Cynara John, OPSM
Mrs. Cherlyann Jones, Director of Training/OPMS
Dr Beatrice Fulford, PS/Ministry of Education
Mr Edgar Howell, Director of Education
Mrs Brenda Robinson, Administration Officer, Ministry of Education
Mr Desmond Wilson, PS/Ministry of Works
Mr Xavier Malcolm, Ministry of Works
Mr Norman Watts, Adviser, Engineering Management Services

Mr Albert Edwards, Chief Auditor

Statutory Boards
Mr John Smith, Chairman, National Health Insurance Board and CEO TCI Airport Authority
Mr Colin Heartwell, CEO, National Insurance Board
Mr Kevin Higgins, Managing Director, Financial Services Commission

Mr Clayton Been, Investment Manager, TCInvest
Ms Lilian Misick, Ms Sophia Thomas, Ms Helena Clinton, Small Firms Division, TCInvest

Providenciales Chamber of Commerce
Mrs Tina Fenimore, President
Ms Wendy Hill, Office Administrator
Mr Jay Saunders
Mr Justin Misick

UK Government
Mr Russell Phillips, EU/OCT Co-ordinator, Overseas Territories Dept, FCO
Ms Caroline Rowett, Head, TCI Unit, Overseas Territories Dept, FCO
Mr Alex Harper, Economic Adviser, DfID

European Commission
Mr Jose Valente, DEVCO
Mr Marco Fromentini, Budget Support, DEVCO
Mr Frans Jonkheer, Overseas Territories Task Force, DEVCO
Ms Helen Jenkinson, Head of Economic and Social Development Section, EU Delegation, Jamaica
Mr Koenraad Burie, Economic and Social Development Section EU Delegation, Jamaica

Annex 2 to TCI PEFA Report

List of Documents consulted

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