

The Turks and Caicos Islands

Macro-economy and Public Finances

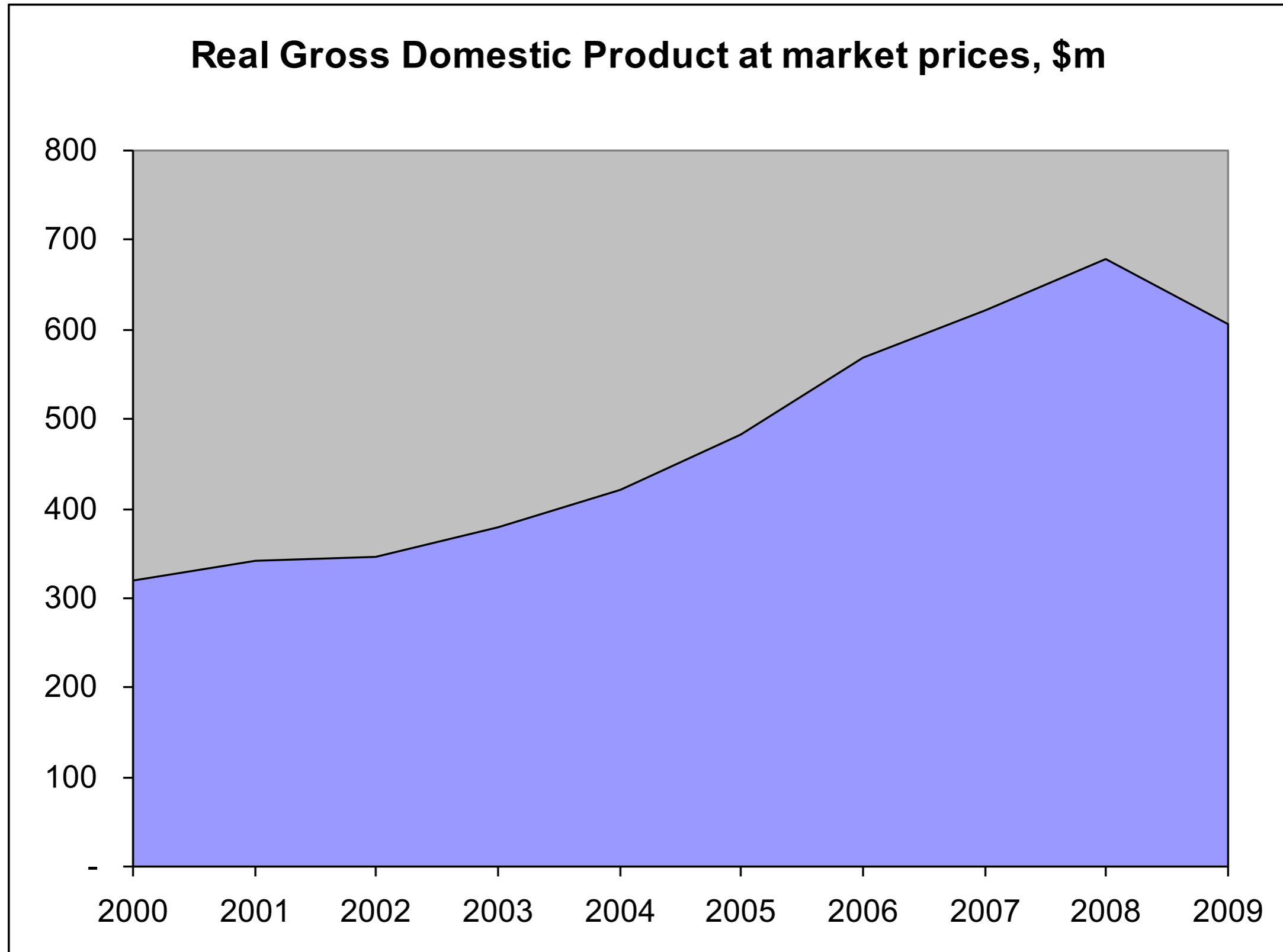


Based on preliminary and unvalidated data from the Ministry of Finance
and Department for Economics, Planning and Statistics

Rapid economic growth in national output

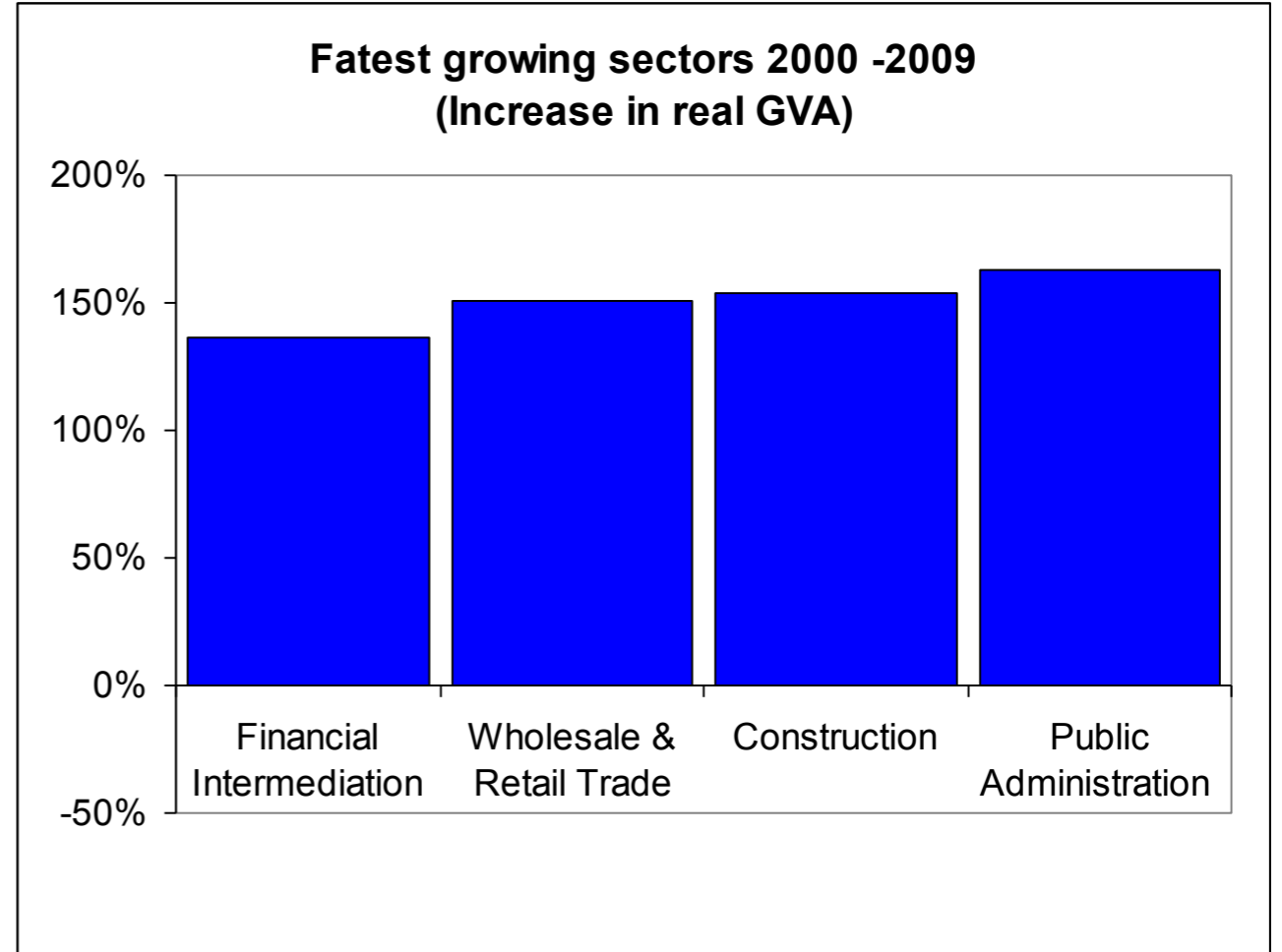
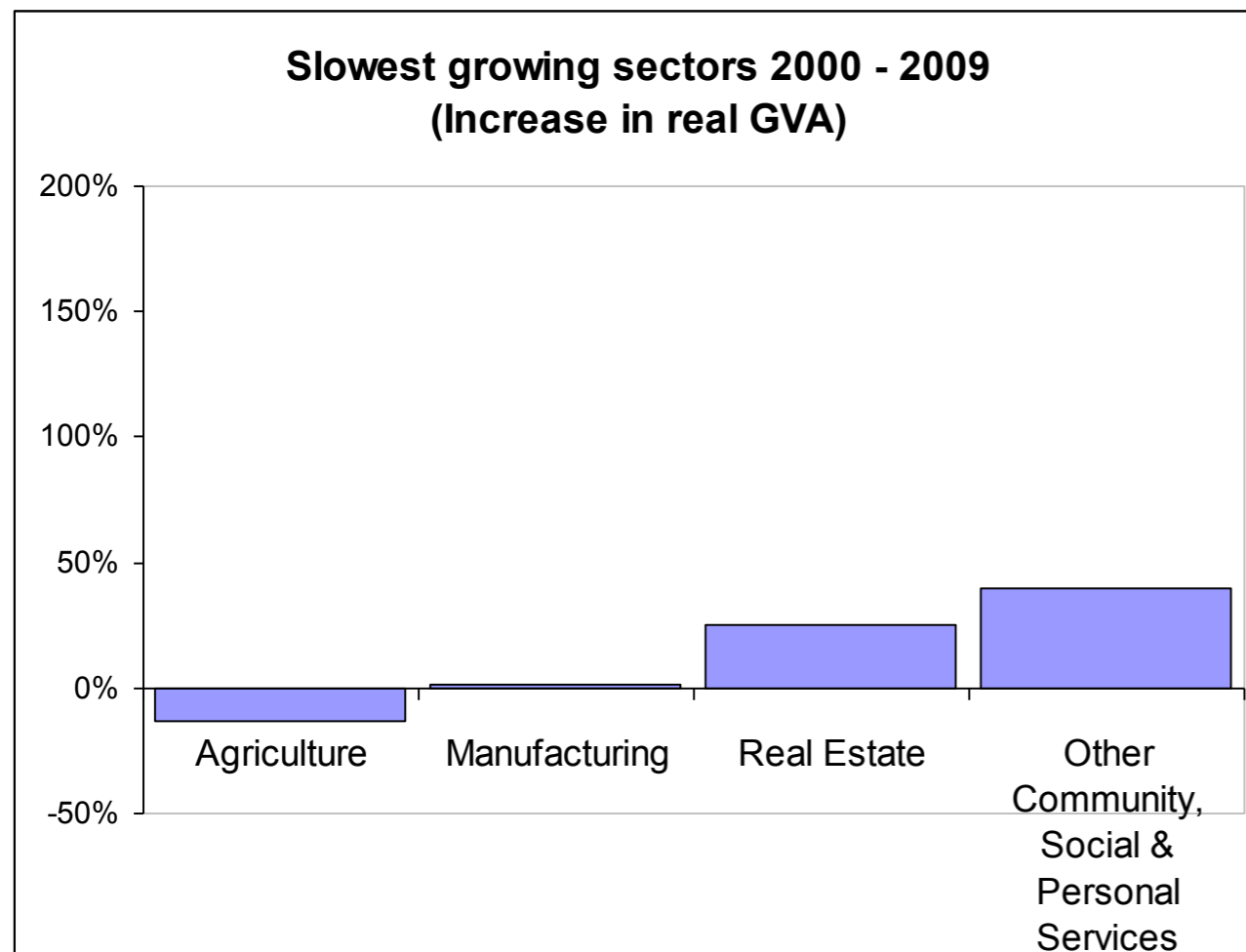


- National Accounts statistics suggest the economy doubled in real terms between 2002 and 2008



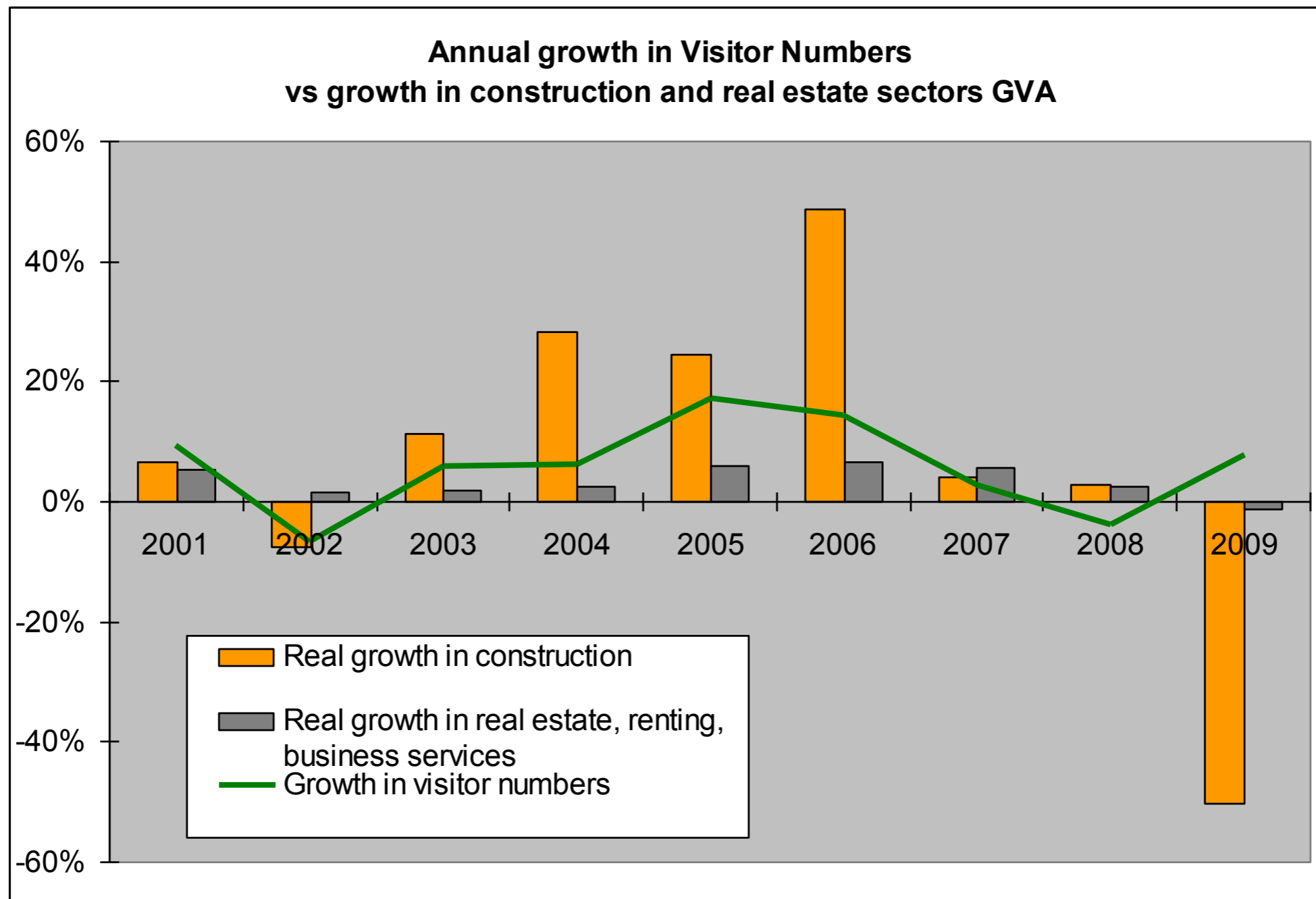
But growth was neither balanced nor sustainable

- Public administration, construction and wholesaling/retailing were the fastest growing sectors
- The construction and sale of new homes, net of imports and the profits and wages of overseas residents, make a direct contribution to GDP
- But only transactions related to the sale or use of existing homes, such as rent, commissions, inspections, conveyancing, loan fees, etc. will generate additional national income



Growth in construction far outstripped growth in demand

- The property bubble, fuelled in part by tax concessions and land sales, resulted in the supply of real estate / rental accommodation principally aimed at a non-resident population, far outstripping demand during the boom
- The global asset bubble burst in 2007/8 and there is now an excess of unproductive and under-utilized property assets in TCI
- Growth in (non-cruise) visitor numbers slowed from 2005, fell by only 4% in 2008, but has since recovered

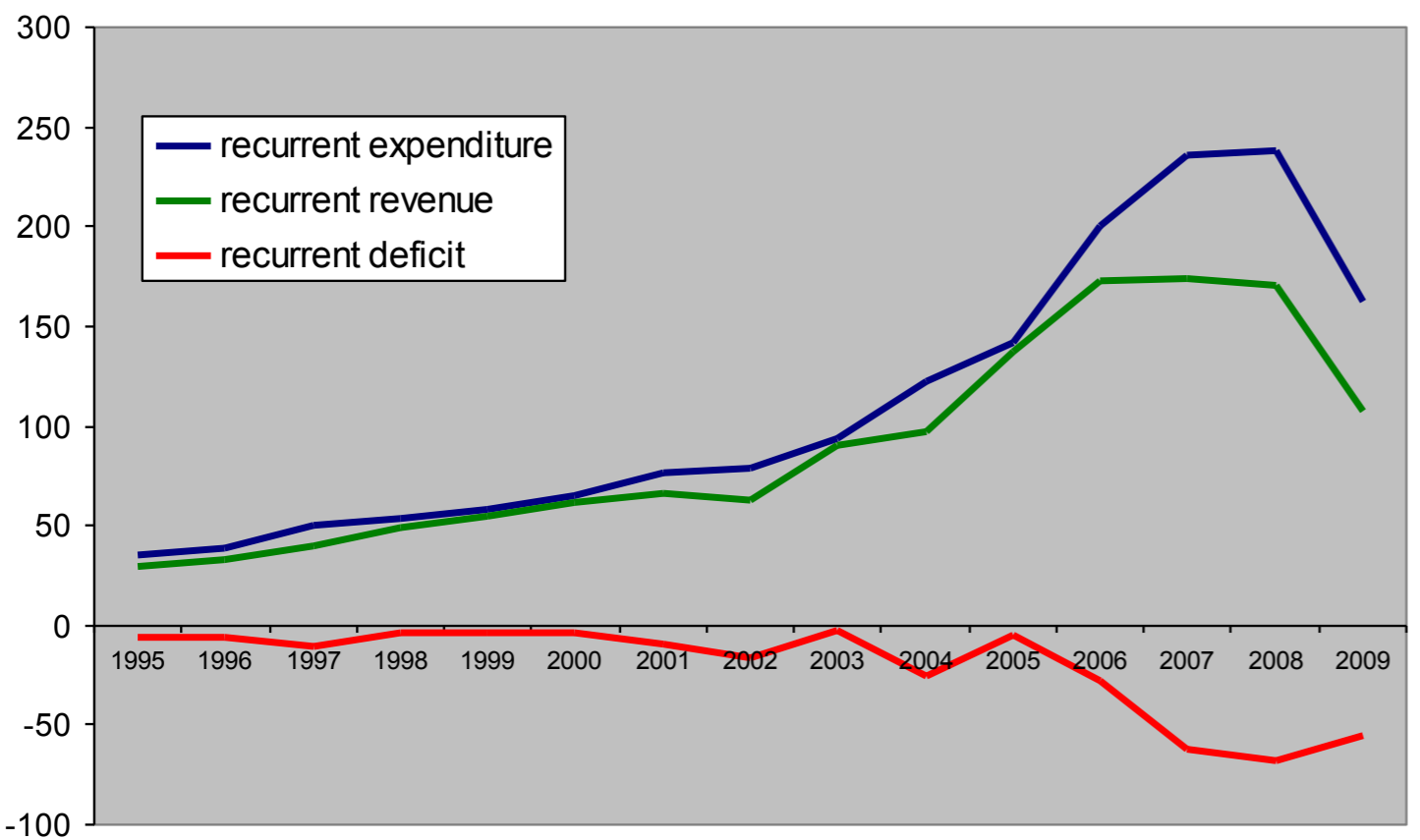


An economy and public sector that lived well beyond their means

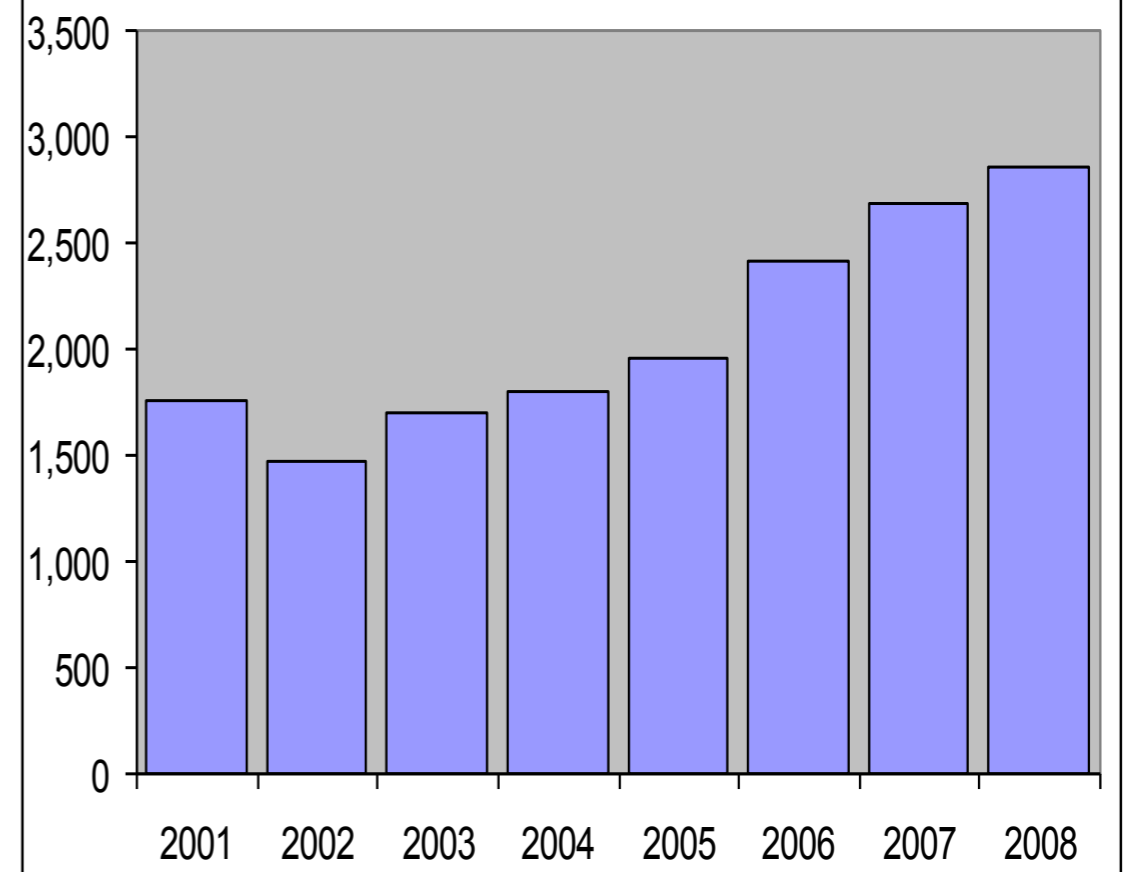


- A narrow industrial base (65% of GDP in construction, finance, hotels and restaurants at peak)
- An unchecked expansion of public spending : a 3 fold increase between 2000 and 2007 compared to a doubling of real GDP; public sector employment almost doubled over same period
- The tax system has been unable to generate sufficient recurring revenues to cover spending
- There has been a growing structural deficit : it will continue to grow unless there are significant reforms

Recurrent public expenditure and revenues, \$ million

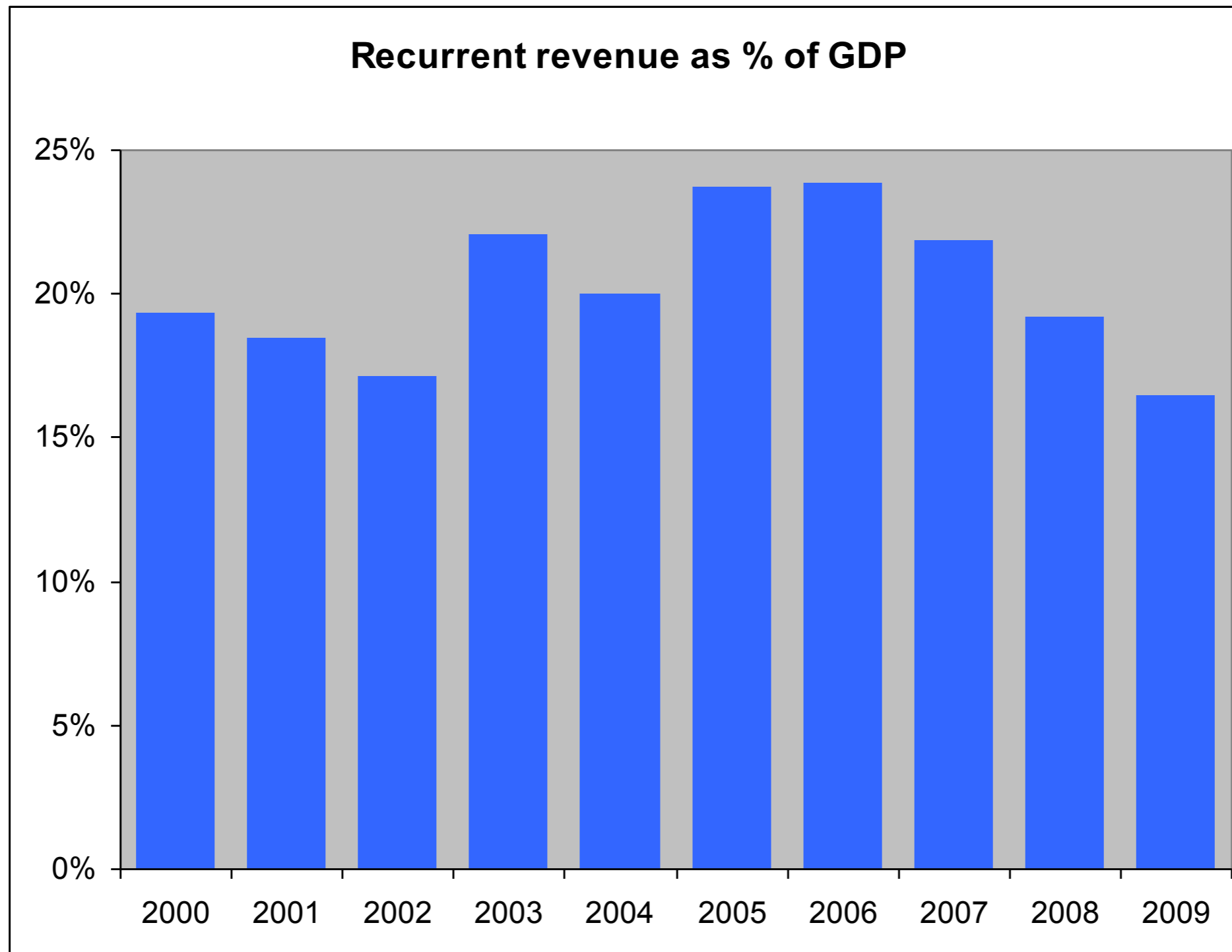


Employment in Public Sector



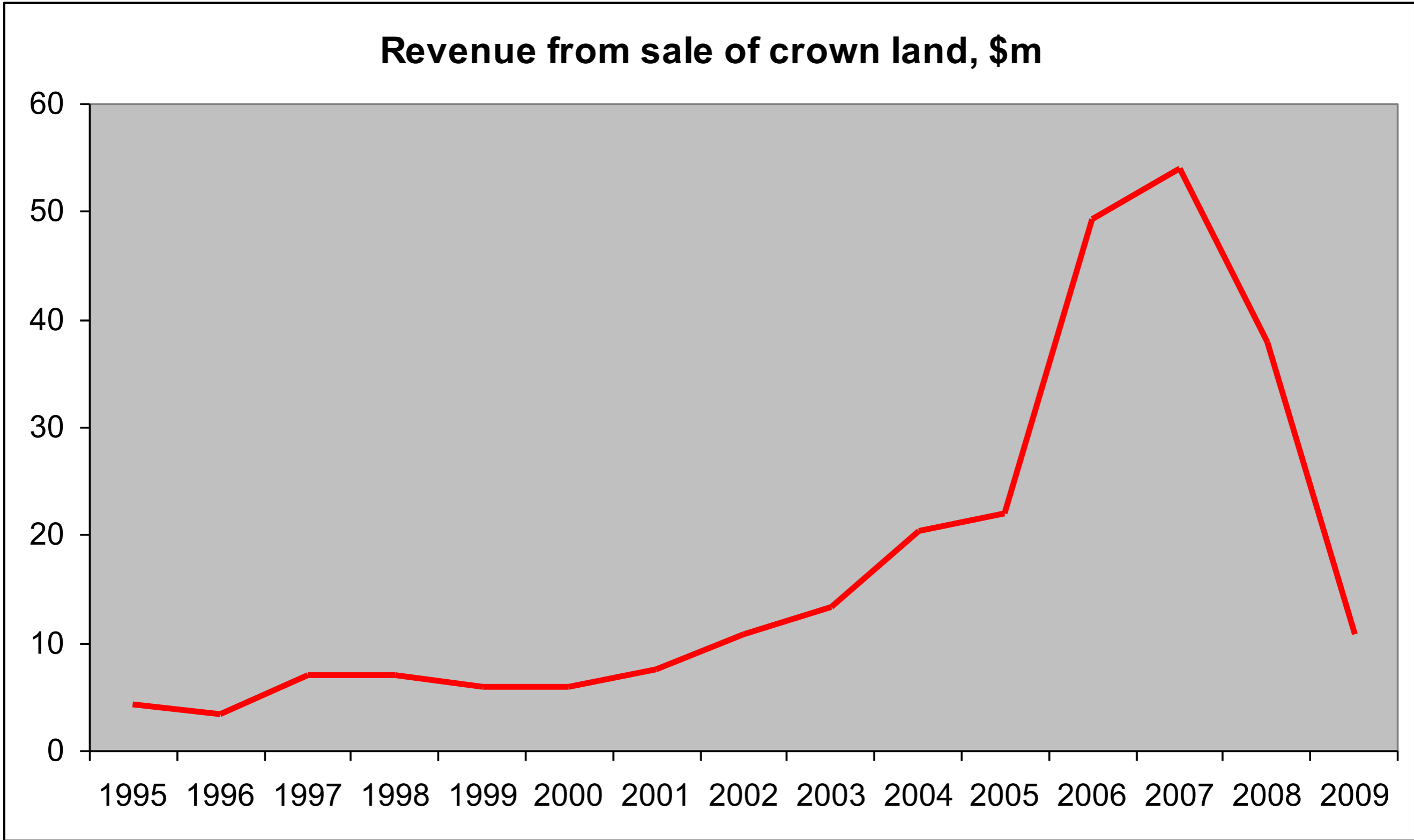
An inefficient, inequitable and inadequately managed tax system

- Narrow tax base falls disproportionately on hospitality industry and on low income groups who tend to pay the most as a proportion of their incomes
- Tax base has been eroded by increasing exemptions and concessions, and inadequate administration



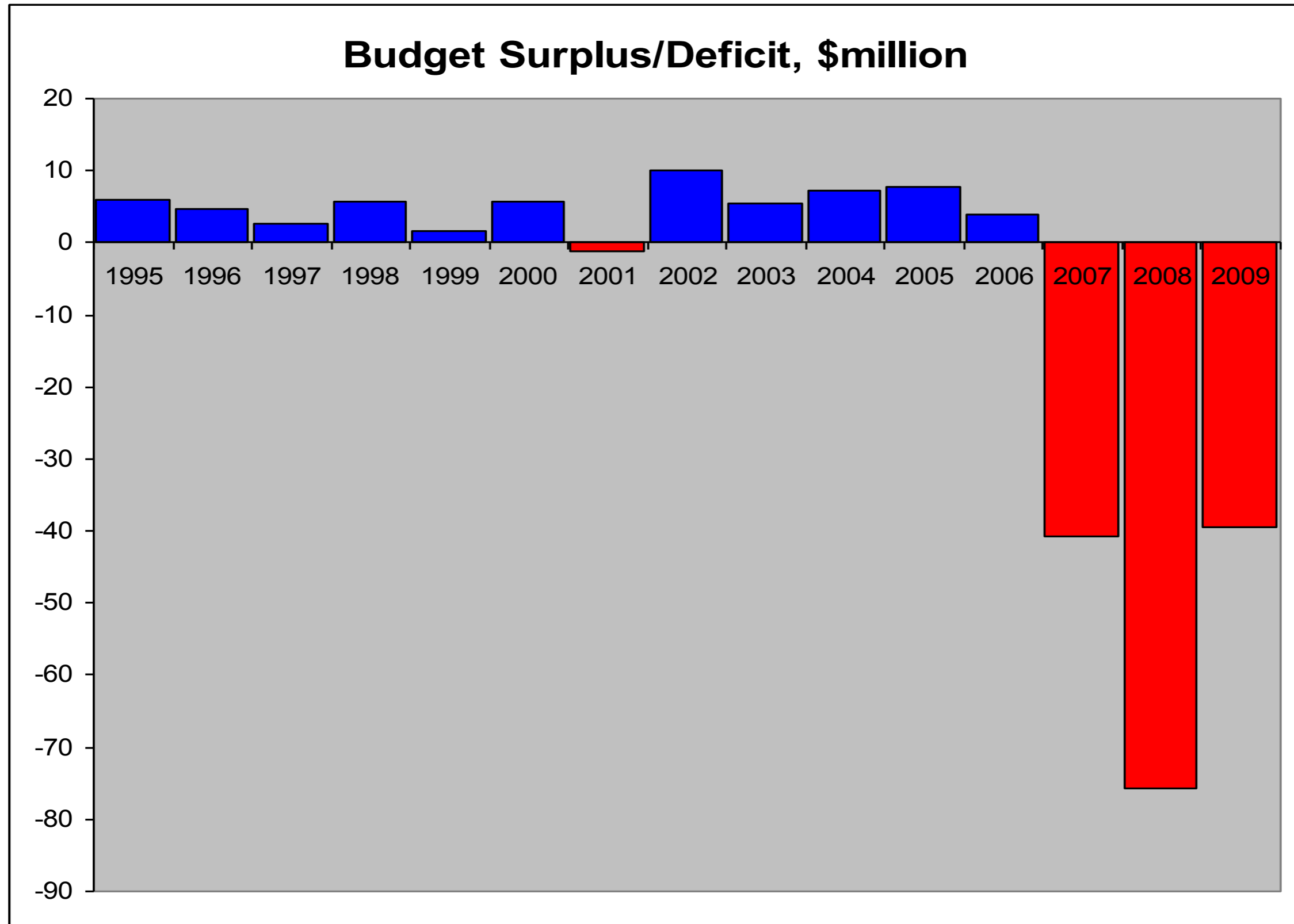
Sale of crown land masked underlying problem but cannot close gap

- Evidence of significant sales below market values



Yawning budget deficit from 2007 despite economic boom

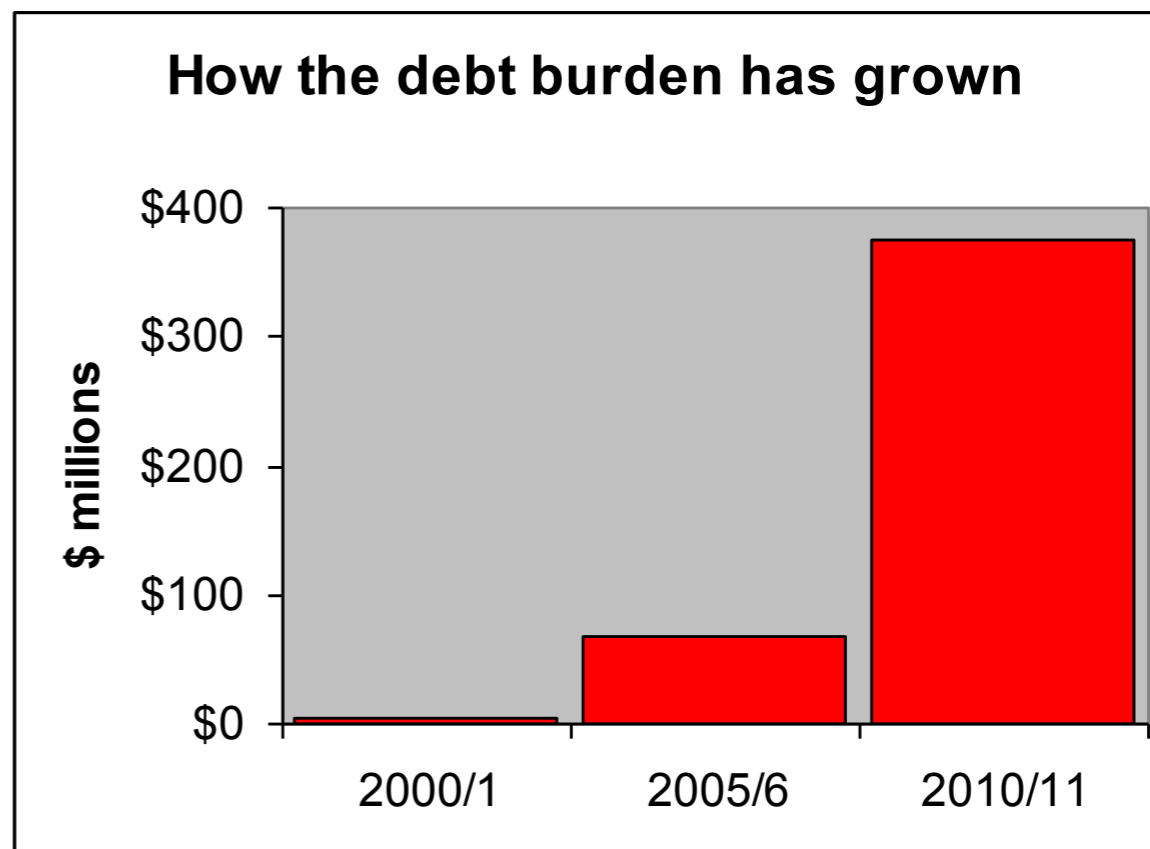
- Significant evidence of poor budgetary planning, control or monitoring of government ministries and departments during this period



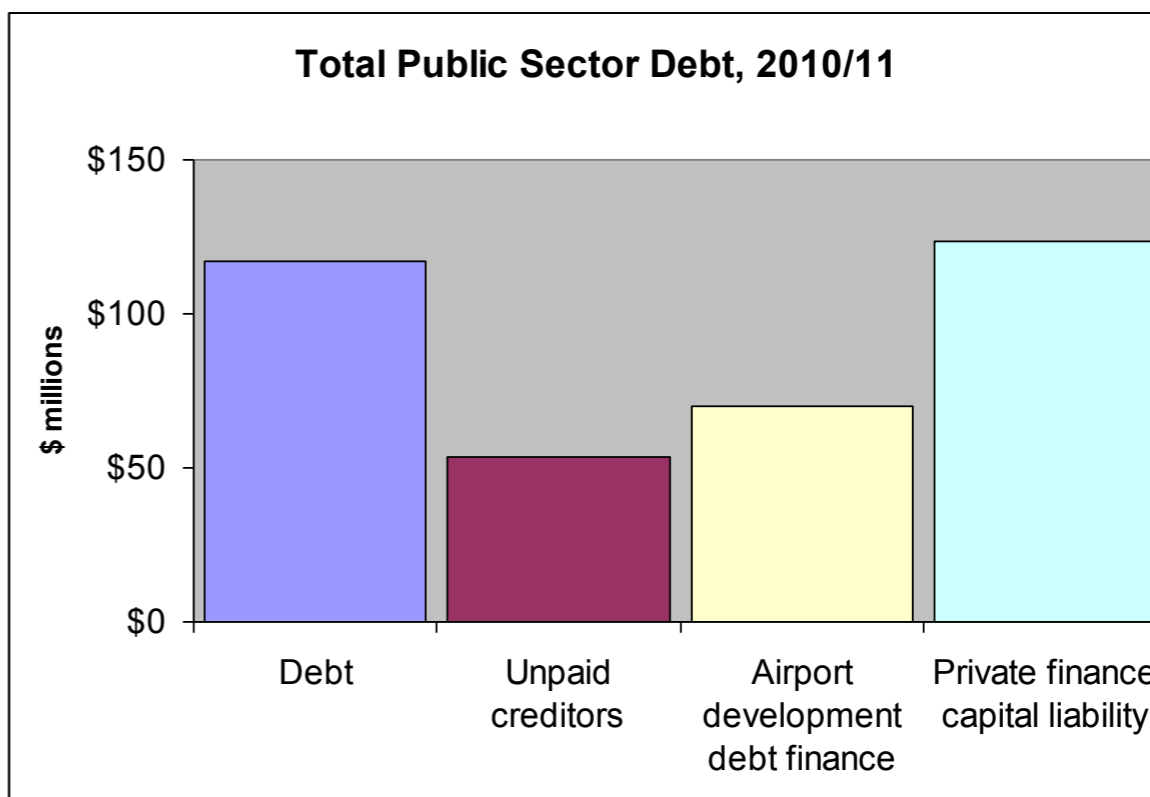
As a result, growth in national debt accelerated



- Significant unpaid bills have accumulated since 2006
 - many TCI businesses were not paid, and
 - many overseas businesses threatened multi-million dollar legal actions for repeated non-payment



- Total public sector liabilities now around \$365 million
 - including unpaid creditors and capital liability for new hospitals
- As a result debt interest payments have increased significantly as a % of public spending and are now c\$14m pa



Growing the TCI economy is vital but will not close the deficit



- How long will it take to close budget deficit assuming tax and total public spending unchanged?
 - assumes tax take is around 25% of GDP as per peak 2006/7, and
 - public expenditure unchanged at c\$200m from current financial year

What if GDP grows by % pa from now on?	Estimated year budget balance reached	Estimated public sector debt* as % of estimated GDP at end of period assuming debt interest 6% pa
3%	2027	260%
5%	2019	140%
8%	2016	90%
10%	2014	75%

- Near term growth unlikely while US economy remains weak
- More modest medium term growth possible if TCI is able to grow and diversify
 - its tourist base to increase the productivity of its existing assets (major new investment in Providenciales airport is first vital step, plus new flights/origins to grow visitor numbers and increase competition in air travel);
 - its accommodation portfolio (for example, to include branded hotels, smaller units, more fractional ownership)
 - other business sectors to provide alternative jobs and incomes
- But to do so will require public sector reform to improve the openness and competitiveness of the business and economic environment

- Review and modify tax system / administration to expand tax base and increase revenues
- Cut wasteful public expenditures and implement public sector reforms to improve efficiency

Many other countries, both regionally and globally, are undertaking similar actions to control their public sector costs and finances, and to reduce their indebtedness.

The Turks and Caicos Islands



Tax Reform

February 2011

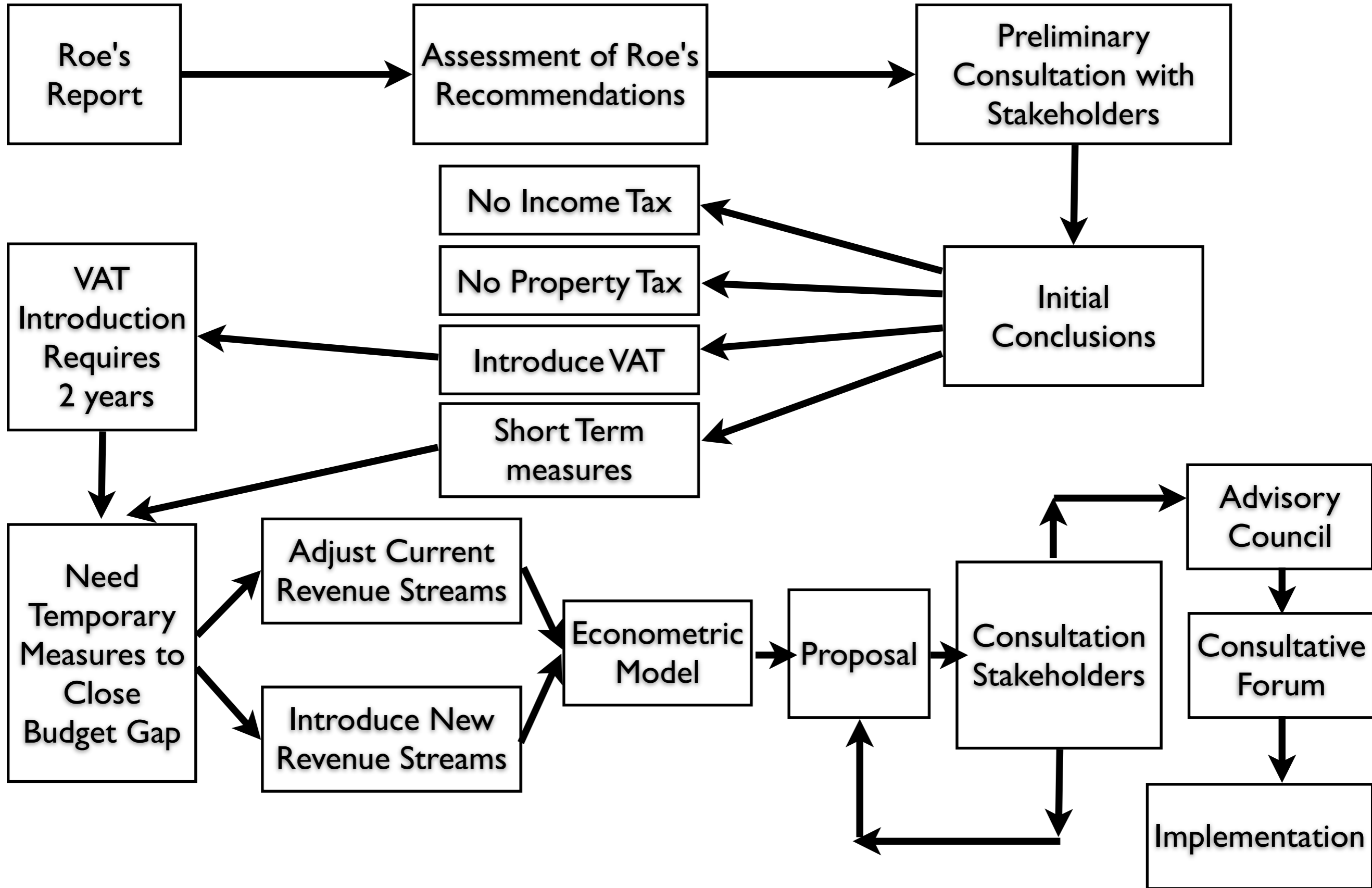
This Project was funded by EuropeAid

Leaving the tax system as it is and wait for the economy to recover is not an option.

Why?

- USA economy will recover slowly
- Large unused stock of rooms and condos
- Additional burden to debt's service and repayment
- Need a more efficient and less volatile tax system

Tax Reform Process



Total annual Recurrent Revenue has stabilized around 125 US\$ million



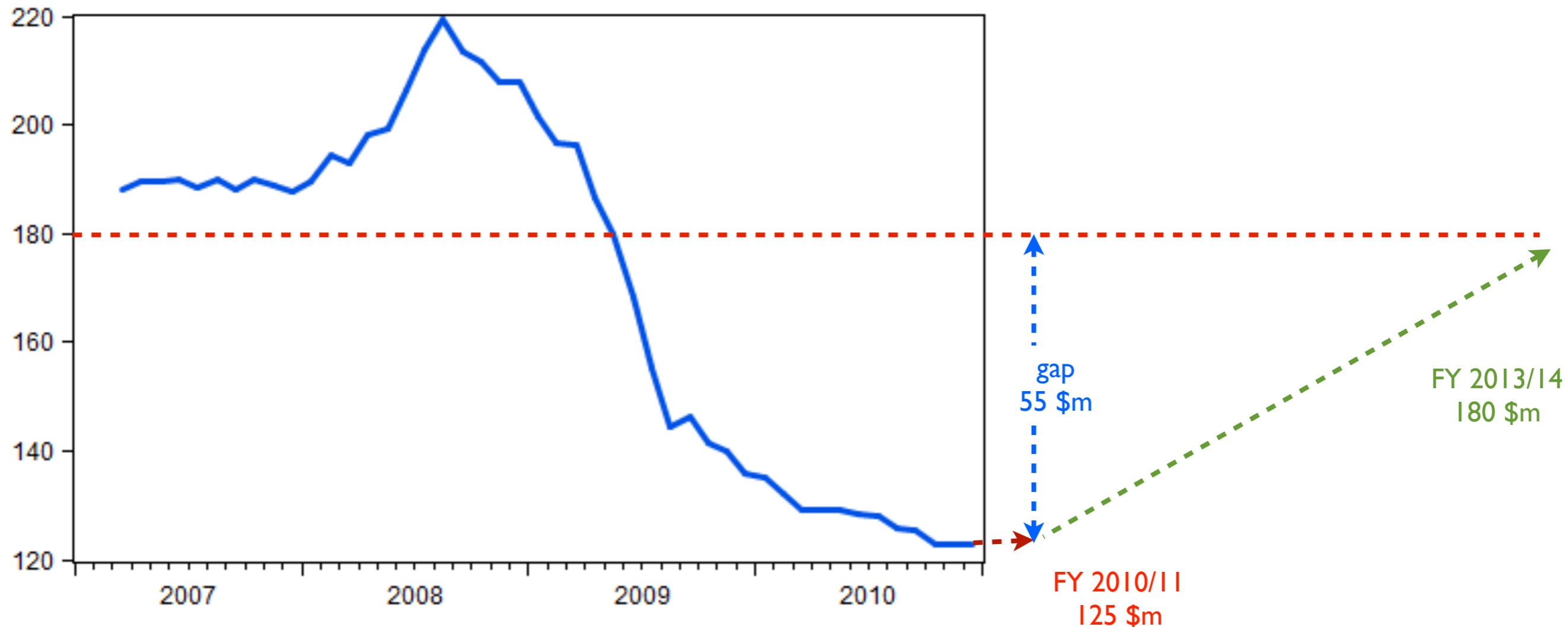
Need to review and modify the tax system and its administration to:

- Expand the tax base
- Increase revenues, and
- Have a more efficient revenue system

Our target is to surpass 180 \$ million by FY 2013/14

How to do this?

Recurrent Revenues (US\$ million)



- Eliminate exemptions
- Expand the tax base to no/low taxed economic sectors
- Simplify and adjust current tax/fee rates
- Introduce more efficient taxes (VAT)
- Improve tax administration

	Additional Revenue	
	FY 2011/12	FY 2013/14
<i>Current Revenues Streams</i>		
1. Customs Processing Fee (4%)	15.5 \$m	
2. Work Permits (10% PAYE - NHIB)	4.1 \$m	
3. Business Licence (simplification)	0.9 \$m	
4. Other Fees and Charges (update rates)	9.9 \$m	
<i>New Revenues</i>		
5. Electricity and Water Tax	5.2 \$m	
6. Bank and Insurance Tax	5.9 \$m	
7. VAT and Excises	-	77.4 \$m
<i>Total Additional Revenue</i>	41.5 \$m	

VAT introduction will reduce Import Tariffs and eliminate Accommodation Tax, Telecom Tax, Vehicle hire tax, Electricity & Water Tax, and Bank and Insurance Tax.

Custom Processing Fee: Recent changes to tariffs have stabilized its downward trend

But we need to restore the revenue lost and have a less volatile import duty system:

- Eliminate exemptions (ongoing process)
- Introduce a 4% Custom Processing Fee (CPF) to be paid on value of all imports

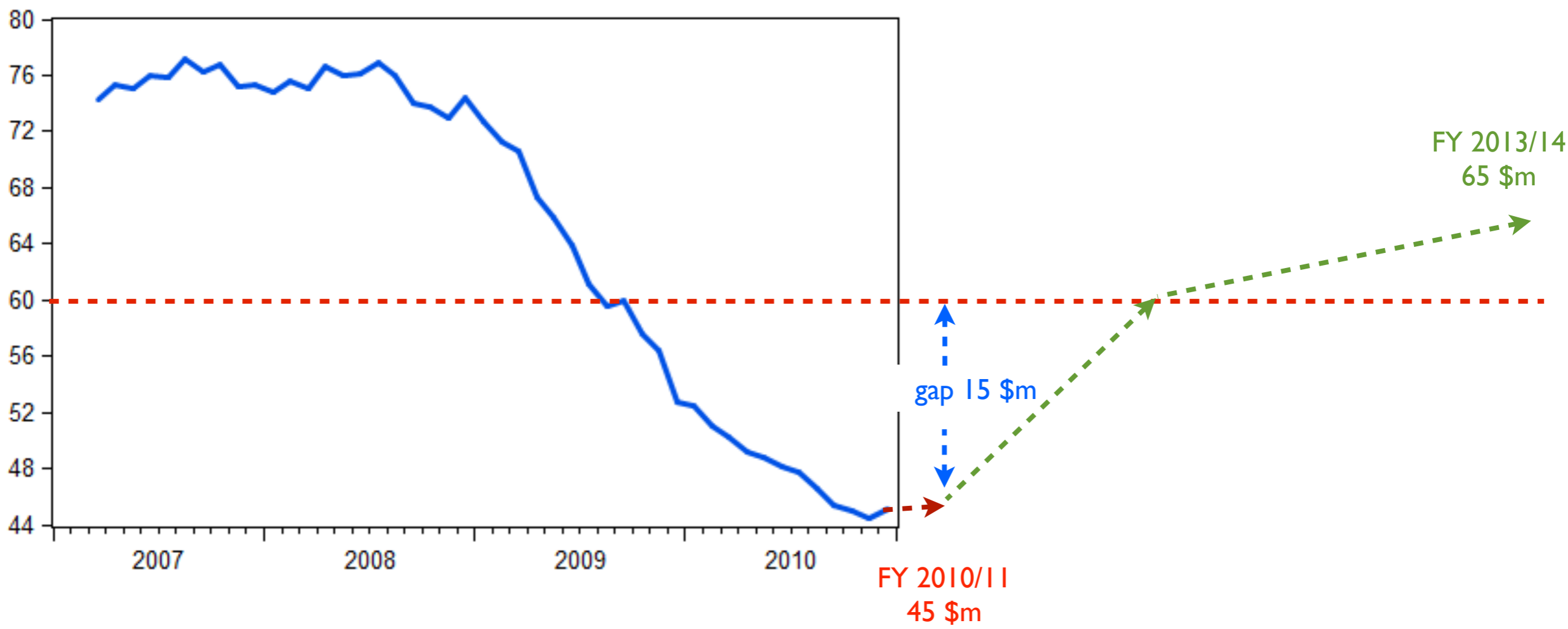
➡ CPF is a processing fee not an import duty.

➡ It will be levied on all goods (no exemptions) and on all importers.

✓ CPF will generate \$ 15.5 in additional Revenue (FY 2011/12)

✓ Import Duty together with the Custom Processing Fee will generate 60 \$ million in FY 2011/12 and 65 \$million by FY 2013/14

Import Duty (US\$ million)



Work Permits: Downturn in construction sector has impacted on work permit revenues

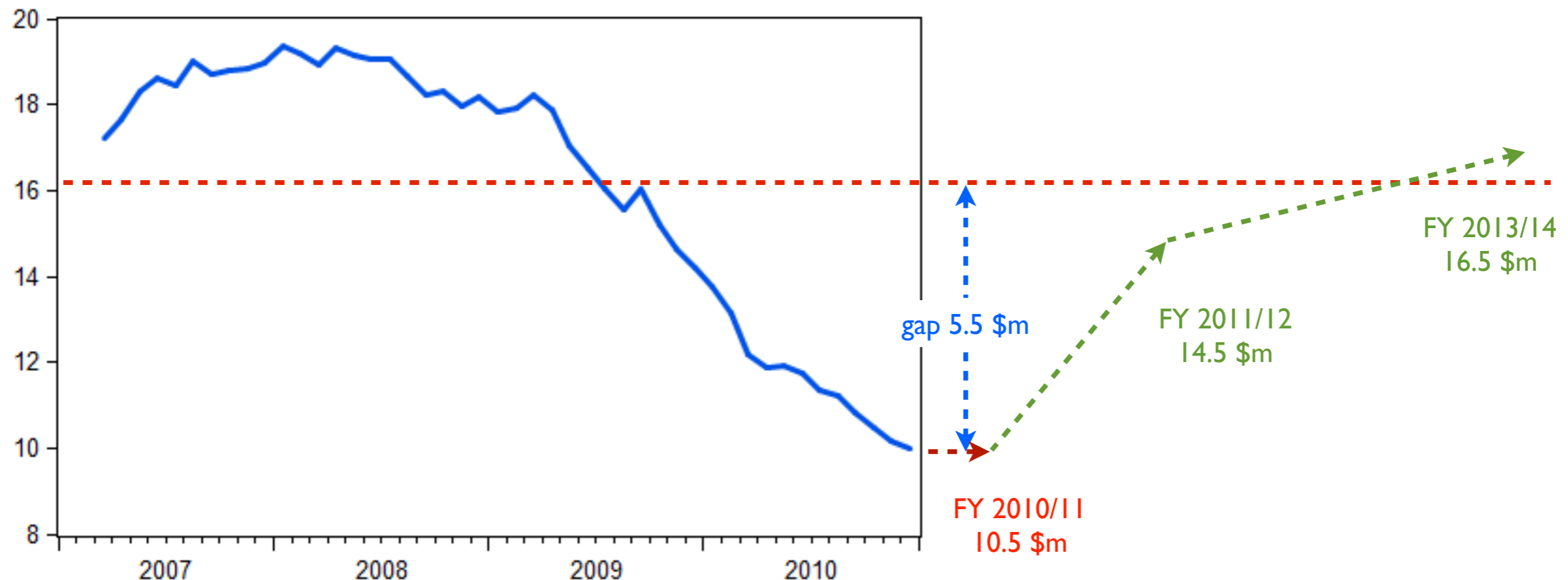
Need to review and modify the work permit system and its administration to:

- Have a more efficient collection system (NHIB)
- Replace current work permit regime and **repatriation program fee**
- Be more equitable -based on salary- not on employment type
- Increase revenues (Work Permit fees not updated since 1996)
- Have a less volatile system (from annual fee to PAYE monthly payments)
- Proposal: **10% of monthly salary, paid by employer to NHIB**

Revenue Target is to surpass 16 \$ million in FY 2013/14

✓ New system would generate an additional 4.1 m in Revenue in FY 2011/12

Work Permit and Residency Fees (US\$ million)





Inflation Rate 1996-2010 ==> 36%

Job Type	Annual Salary	Current Permit Fee	Proposed Monthly Fee	Annual Fee
Accountant	\$100,000.00	\$7,000.00	\$833.33	\$10,000.00
	\$60,000.00	\$7,000.00	\$500.00	\$6,000.00
Chef	\$35,000.00	\$2,500.00	\$291.66	\$3,500.00
	\$22,000.00	\$2,500.00	\$183.33	\$2,200.00
Barber	\$23,000.00	\$1,000.00	\$191.66	\$2,300.00
	\$15,000.00	\$1,000.00	\$125.00	\$1,500.00
Waiter	\$12,000.00	\$300.00	\$100.00	\$1,200.00
	\$8,000.00	\$300.00	\$66.66	\$800.00
Self Employed	\$60,000.00	\$7,000.00	\$463.00	\$6,000.00
	\$40,000.00	\$7,000.00	\$314.00	\$4,000.00



- Reduce the number (Elimination)
- More efficient charges and fees system (Consolidation)
- Update remaining charges and fees to reflect inflation (Update)

Elimination

1. Administration Fee Business Licence
2. Temporary Work Permits
3. Audit Fees
4. Dental Fees
5. Examination Fees
6. ID Card Fees
7. Medical Fees
8. Salt Cay Boat Fees
9. Tender Document Fees
10. School Fees
11. Migrant Health Processing Fee
12. Taxi meters

Consolidation

1. Casino Licence
2. Fishing Licence
3. Liquor Licence
4. Sand Licence
5. Gaming Location Licence
6. Casino Certificates
7. Stamp Duty Miscellaneous
8. Money Transfer Levy

Update

Most Charges and Fees have not been updated since 1996

Inflation 1996 - 2010: 36%

Charges and Fees will be updated to reflect inflation

There will be periodic updates in the future

- Introduce New Business Classification
- Based on economic sectors:
 - ✓ Primary
 - ✓ Secondary
 - ✓ Services
- and size of business:
 - ✓ Small
 - ✓ Medium
 - ✓ Large
- Update current fees
- Increase fees by 35% (Inflation 1996-2010 => 36%)
- Minimum Fee of \$ 300.00

There will be periodic updates to reflect inflation

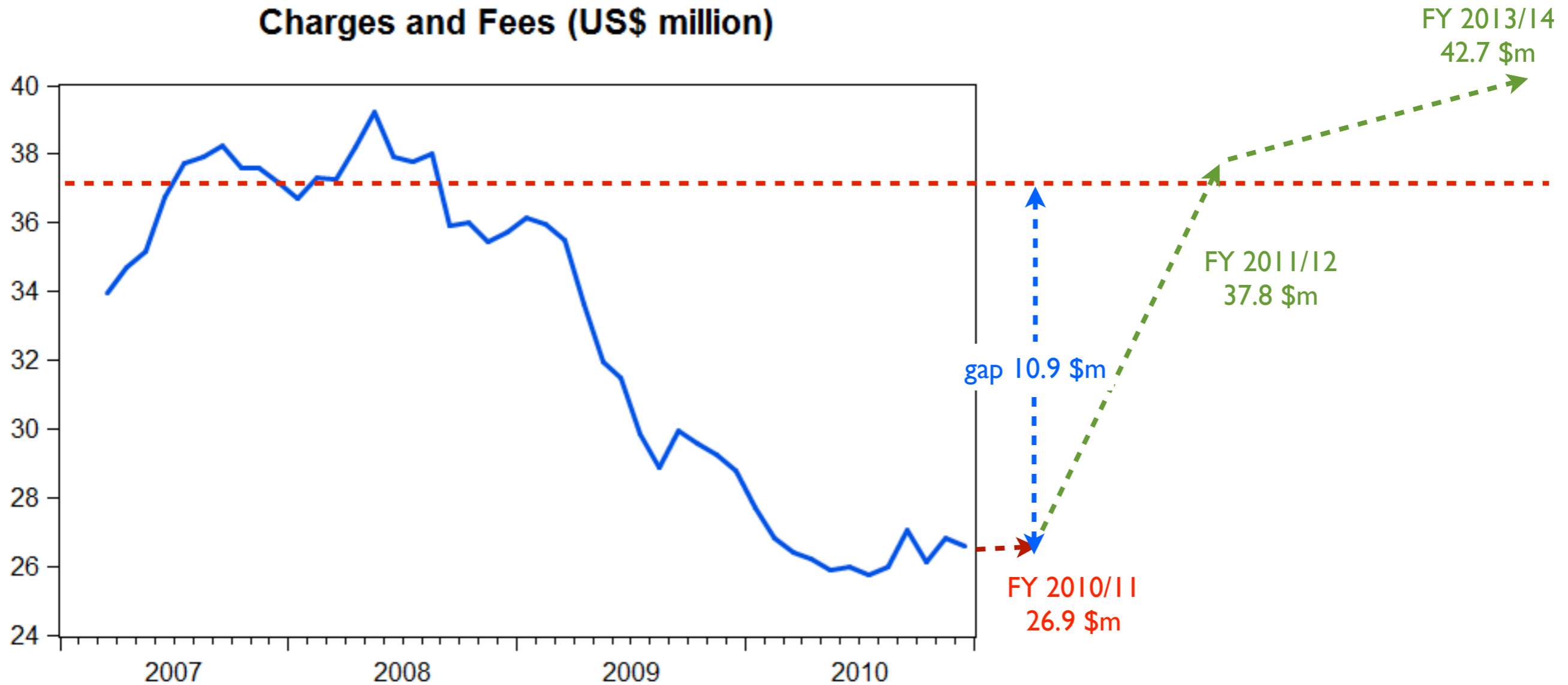
Charges and Fees: Outlook for 2011 - 2013



Revenue	2008	2009	2010	2011	2012	2013
Charges & Fees	35,767	29,298	26,994	37,788	40,186	42,738

✓ Adjustments to Charges and Fees would generate an additional 10.9 m in Revenue in FY 2011/12

Charges and Fees (US\$ million)



New Revenues: needed to close the budget gap and have more efficient system

In the short term to close the budget gap:

- Broaden the tax base to non/low taxed sectors
 - ➡ Electricity & Water sector
 - ➡ Financial sector
- Pave the way to VAT introduction

In the medium term to have a more efficient tax system:

- Introduce Broad base VAT to replace sale taxes
- Modify Excise system to be consistent with International Practices

New Streams

Electricity & Water taxes

Bank and Insurance Tax

VAT

Excises

Electricity and Water sales tax: threshold will apply to Residential Consumption

To be charged on Commercial and Residential Customers

Residential Customers below a threshold will not pay

Tax rate would be 10% on the total value of the monthly bill

It would replace the proposed Environmental Tax

It would be a temporary tax until VAT is introduced in FY 2013/14

✓ Electricity and Water Sales tax would generate 5.2 m in Revenue in FY 2011/12

Revenue	2008	2009	2010		2011	2012	2013
Electricity & Water tax			-		5,223	5,568	-

To be charged on all Services provided by Financial Institutions that do not involve interest margin (ATM services, Cheques, Money transfer, debit cards, etc.)

Mortgages, deposits, loans, etc. will not pay

Tax rate would be 10% on the total value of the services charged to customers

It would replace Money Transfer Fees and Stamp Duty Miscellaneous

It would be a temporary tax until VAT is introduced in FY 2013/14

✓ Bank and Insurance Tax would generate 5.9 m in Revenue in FY 2011/12

Revenue	2008	2009	2010	2011	2012	2013
Bank and Insurance Tax			-	5,939	6,331	-

VAT will replace:

- Accommodation tax
- Telecommunication tax
- Vehicle hire tax
- Electricity and Water tax
- Bank and Insurance tax

VAT and Import Duties:

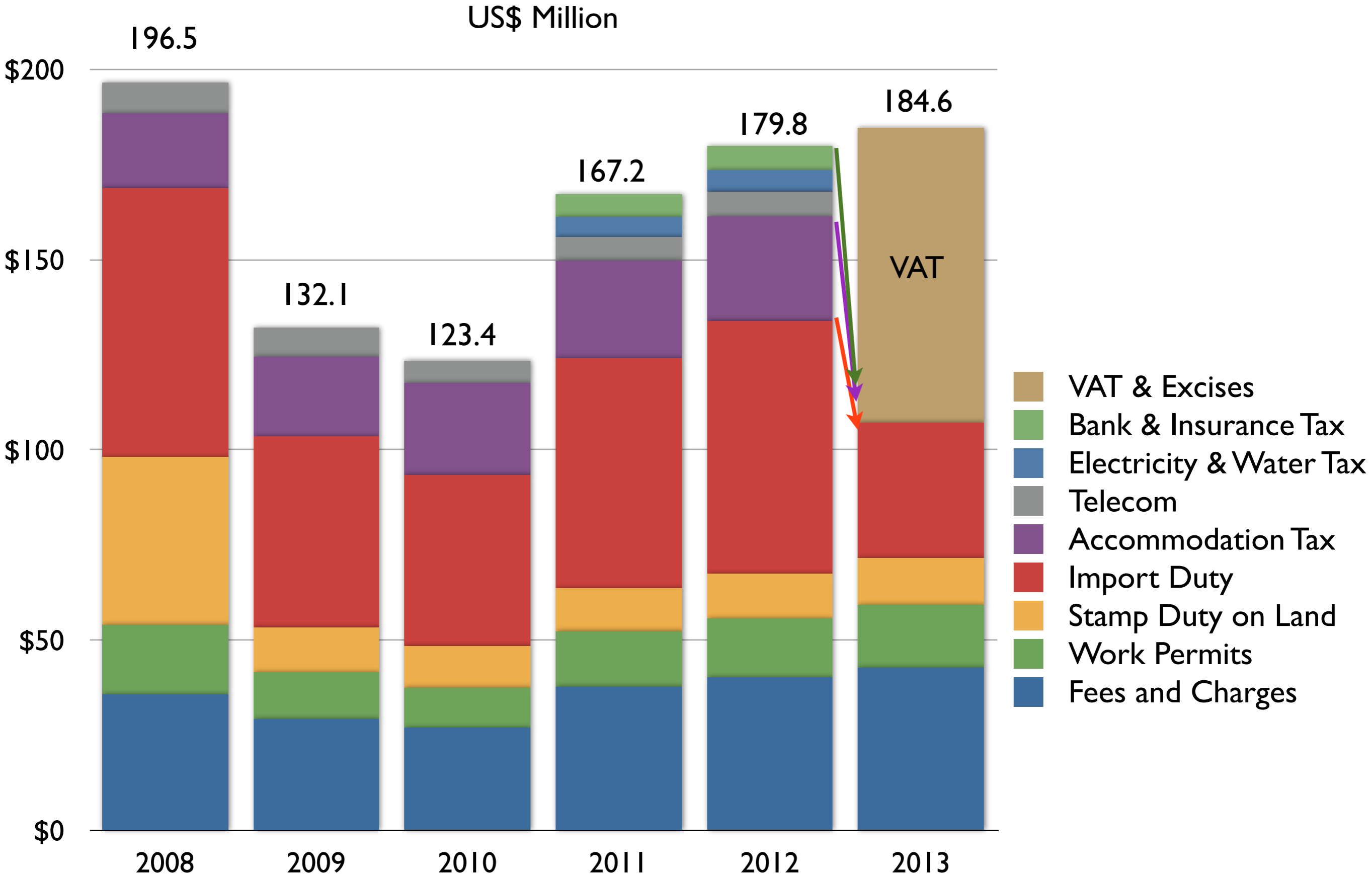
- Reduction of Import Duty

Advantages of VAT:

- Neutral tax (does not affect consumers and traders decisions: everybody pays the same rate).
- Non cascading tax (no tax on tax)
- Self enforcement tax (improves compliance)
- Crediting system (Input tax and Output Tax)
- Non regressive tax (if you consume more you pay more)
- Capital goods are non taxed (investment incentive)
- Threshold (Only large traders will register) (easier to administer)

Revenue	2008	2009	2010	2011	2012	2013
VAT				-	-	69,907
Excises						7,528

Revenue Outlook 2011-2013





Revenue Administration

Measures to improve revenue administration

- Enhance legal framework to promote self assessment.
- Enhance computerization (revenue administration departments).
- Produce additional and accurate information to properly evaluate programs.
- Improve integration & exchange of Information among government agencies.
- Introduce a single registration system and introduction of a common TIN.
- Provide additional training of staff in audit & enforcement.
- Improve taxpayer service so that clients are aware of their responsibilities & consequences of non compliance.
- Consolidate Collection & Enforcement activities in the RCU.

Thank you !



This Project was funded by EuropeAid