EXAMINATION OF THE COMPONENTS OF THE FISCAL POLICY PAPER

WHICH WAS LAID BEFORE THE HOUSES OF PARLIAMENT

ON APRIL 17, 2014

INDEPENDENT AUDITOR'S REPORT

THE AUDITOR GENERAL OF JAMAICA

FINANCIAL YEAR 2014/15

Auditor General of Jamaica

Auditor General's Department
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June 2014

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This report was prepared by the Auditor General's Department of Jamaica for presentation to the House of Representatives.

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Independent Audit Report
On the
Fiscal Policy Paper – 2014/15

1. I have examined the components of the Fiscal Policy Paper (FPP) laid by the Minister of Finance before the House of Representatives on April 17, 2014. The FPP comprises, as stipulated by the Financial Administration and Audit (FAA) Act: the Fiscal Responsibility Statement, Macro-Economic Framework and Fiscal Management Strategy. My opinions are detailed at **paragraphs 19 to 24** of the report.

Responsibilities of the Minister of Finance

2. The Minister of Finance is responsible for the FPP, including the underlying conventions and assumptions on which the principles of prudent fiscal management are based. Section 48B(2) of the Financial Administration and Audit (FAA) Act provides that, inter alia:

   "*Upon presentation of the annual Estimates of Revenue and Expenditure, the Minister shall lay before both Houses of Parliament -*

   a) a Fiscal Policy Paper containing the information indicated in the Third Schedule and setting out, in accordance with this section–

      i. Macroeconomic Framework;
      ii. A Fiscal Responsibility Statement; and
      iii. *A Fiscal Management Strategy*"

3. Section 48B (3-5) provides that the Macroeconomic Framework is to present an overview of the state of the economy, and an assessment of the prospects for economic growth, including medium-term projections for the main macroeconomic variables. The Fiscal Responsibility Statement should specify the levels of fiscal balance and debt that are prudent in the opinion of the Minister, the proposed fiscal-policy measures, and a declaration that the Minister will adhere to the principles of prudent fiscal management. The Fiscal Management Strategy must provide an assessment of the current and projected finances of the Government, outline plans and policies for economic development, and explain how such plans and policies conform to the Fiscal Responsibility Statement.

4. As outlined in Section 48D of the FAA Act (amended in 2011), the Minister shall act in conformity with the following fiscal management principles –
   a. the public debt is to be reduced to, and thereafter maintained at, a prudent and sustainable level;
   b. fiscal risks are to be managed prudently with particular reference to their quality and level;

c. borrowings are to be geared toward investment activities that support productivity and economic growth; and
d. expenditure is to be managed in a manner that is consistent with the level of revenue generated, so as to achieve the desired fiscal outcomes.

5. Section 48C of the FAA (Amendment) Act 2014 explicitly outlines fiscal targets for which the Minister of Finance should take appropriate measures to achieve. These include:

   a. To attain a fiscal balance, as a percentage of gross domestic product, as at the end of the financial year ending on March 31, 2018 and thereafter, that allows the requirement specified in paragraph (b) to be achieved, and to be maintained or improved thereafter, and the fiscal balance to be attained shall be computed in accordance with the Fifth Schedule;
   b. To reduce the public debt to sixty per cent or less of the gross domestic product by the end of the financial year ending on March 31, 2026 and maintain or improve the ratio thereafter;
   c. To reduce the ratio of wages paid by the Government as a proportion of the gross domestic product to nine per cent or less by the end of the financial year ending on March 31, 2016, and maintain or improve the ratio thereafter;
   d. To ensure that neither the Appropriation Act nor any Supplementary Estimates of Revenue and Expenditure for any financial year will cause any negative deviations from the fiscal balance to be attained pursuant to paragraph (a); and
   e. To ensure that no deviation is recorded in the notional account until the fiscal accounts for the financial year in question have been finalized.

Responsibilities of the Auditor General

6. My responsibility, as set out in Section 48B(6) of the FAA Act, is to examine the components of the Fiscal Policy Paper and provide a report to the Houses of Parliament indicating whether –

   a) the conventions and assumptions underlying the preparation of the Fiscal Policy Paper comply with the principles of prudent fiscal management specified in section 48D;

   b) the reasons given, pursuant to subsection (5)(d)(ii) are reasonable having regard to the circumstances;

   c) pursuant to [her] application of criteria prescribed pursuant to regulations made under section 50 (1), there are any public bodies that do not form part of the specified public sector, and identifying those bodies (if any) which in the preceding financial year formed part of the specified public sector;

d) a public private partnership involves only minimal contingent liabilities accruing to the Government.

7. I conducted my examination in accordance with standards issued by the International Association of Supreme Audit Institutions and International Standard on Assurance Engagement (ISAE) 3000 – *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information* issued by the International Auditing Standard Board. These standards require that I comply with ethical requirements and plan and perform the engagement to obtain sufficient and appropriate evidence to base my opinion in line with the criteria, which are established in section 48D of the FAA Act.

Methodology

8. The examination included:
   - review of the provisions of the FAA Act;
   - review of the Fiscal Policy Paper for financial years (FYs) 2013/14 and 2012/2013;
   - review of evidence and clarifications on the FPP FY 2014/15 provided by the Ministry of Finance;
   - obtaining representations[1] from the Ministry of Finance;
   - consulting with technical experts in keeping with International Standards on Assurance Engagements (ISAE) 3000; and
   - performing such other procedures considered necessary in the circumstances.
   - Additionally, my examination of the Fiscal Policy Paper considered the Third Schedule to the FAA Act. This schedule sets out the required minimum contents of the Paper.

9. I did not comment on the merit of the Finance Minister's fiscal strategy. My comments are restricted to the requirement as stated in section 48B(6) of the FAA Act.

10. Amendments to the FAA Act introduced new fiscal rules, which became effective on April 1, 2014. The amended Act repealed section 48C(1), which stipulated fiscal measures the Minister of Finance should attain by March 31, 2016, as well 48C(2) and (3). Under the amended Act, the Minister's responsibility to take appropriate measures to reduce the ratio of wages paid by the Government as a proportion of GDP to 9 per cent is the only fiscal target that has not changed either in terms of numerical target or the timeline for achieving same.

11. The Fiscal Policy Paper, which was tabled on April 17, 2014, does not incorporate the fiscal measures now outlined in FAA (Amended) Act 2014 section 48C, with the

[1] Written confirmation of information provided

exception of the fiscal rule to reduce wages as a percentage of GDP to 9 per cent by March 31, 2016.

12. Consequently, the basis (fiscal measures) on which the Paper was prepared is no longer legally applicable and the legally applicable fiscal measures were not considered in the paper.

Basis of Qualified Opinion

13. Section 48D (a) requires that *"[public] debt is to be reduced to, and thereafter maintained at, a prudent and sustainable level."* Further, the Act specifies the fiscal target for the public debt to be achieved by financial year ending March 31, 2026 [section 48C (1) (b)]. However, there is a difference between the definition of public debt in the FAA (Amendment) Act 2014 and the coverage of the public debt being presented in FPP FY 2014/15. Public Debt, as defined in the amended Act means *"the consolidated debt of the specified public sector, including its government guaranteed debt (after netting out the cross holdings of debt of entities within the specified public sector, other than holdings by the Bank of Jamaica)."* The coverage for public debt in the FPP FY 2014/15 refers to the stock of public debt directly contracted by the Central Government, Bank of Jamaica debt and Government guaranteed external debt. Because the debt to GDP projections being presented in the FPP FY 2014/15 is not in keeping with the definition of public debt, I am not able to determine how the government will achieve the stipulated debt to GDP target.

14. The Minister of Finance did not disclose sufficient information in the FPP to allow me to determine whether the conventions and assumptions underlying the preparation of the Fiscal Policy Paper comply with fiscal management principle B specified in section 48D. Principle B requires that "Fiscal risks are to be managed prudently with particular reference to their quality and level." The MoFP though disclosing the sources of fiscal risks did not quantify the impact the realisation of the risks may have on their targets. The Ministry has indicated that the timing and uncertainty associated with these risks impede its ability to quantify same. However, the absence of this critical information provides me with no basis on which to provide reasonable comment that this principle has been complied with in the FPP. (**See page 12-13** of the attached report).

15. Section 48D(c) requires that "Borrowings are to be geared toward investment activities that support productivity and economic growth." The Ministry states that *"The investment activities of the GOJ that support productivity and economic growth are usually contained in the Capital Budget."* Our analysis shows that capital expenditure as a percentage of loan receipts is projected to decrease to 31 per cent in FY 2014/15 compared to 37 per cent in FY 2013/14, with a further projected reduction to 20 per cent in FY 2015/16. Further, during the period 2011/12 to 2013/14, the actual capital spending has been less than what was budgeted, in

keeping with the government's expenditure containment measures as a result of lower revenue outturn. The government has signalled in the past that a likely fiscal adjustment to address revenue shortfall will be a reduction in the capital budget. Should that be the case, it can result in a lowering of the capital to loan receipt ratio. (**See page 13-14** of the attached report).

16. Section 48B (5) (d) (ii) of the FAA Act requires the Minister to compare the outcome of the fiscal indicators with the targets established for the previous financial year and give reason for any deviations. Section 48B (6) of the FAA Act requires that the Auditor General indicates whether the reasons given pursuant to subsection (5) (d) (ii) are reasonable having regard to the circumstances.

17. The lack of pertinent information from the Ministry affected my assessment of the reasonableness of the variances between established targets and the outcome of the fiscal indicators. The MoFP did not submit to me, as promised, an addendum that should have provided the necessary information. My review of the 2014/15 FPP revealed that, although some fiscal risks were mentioned therein, they were not quantified or reflected in the projections. Consequently, it was not clear to me as to what extent deviations, such as underperformance of revenue, were due to forecast errors, modification of assumptions, or unforeseen events/ shocks (**See pages 17 to 24** of the attached report).

18. In order for me to indicate whether there are any public bodies that do not form part of the specified public sector, and to identify those bodies which in the preceding financial year formed part of the specified public sector, the Act requires that I apply criteria prescribed in the attendant Regulations. However, these Regulations have not yet been tabled. Further, the Minister was not able to indicate those public bodies in the absence of the criteria.

Opinion

19. On the basis of the limitations in **paragraphs 13** above, I do not form an opinion on whether the FPP FY 2014/15 complies with the fiscal management principle stated in Section 48D (a) of the FAA Act.

20. On the basis of the limitation in **paragraph 14** above, I do not form an opinion on whether the FPP FY 2014/15 complies with the fiscal management principle stated in section 48D (b) of the FAA Act.

21. I consider the effect of the matters mentioned in **paragraph 15** above, as having a material effect on the Minister's compliance with the specified fiscal management principle outlined in the Act. On that basis, I do not conclude that the FPP FY 2014/15 complies with the fiscal management principle stated in section 48D (c) of the FAA Act.

22. As it pertains to Section 48D (d) which requires that "expenditure is to be managed in a manner that is consistent with the level of revenue generated, so as to achieve the desired fiscal outcomes", nothing has come to my attention that causes me to believe that the FPP tabled by the Minister of Finance on April 17, 2014 has not complied with the section 48D (d) of the FAA Act.

23. On the basis of the limitation indicated at **paragraph 16 and 17** above, I do not form an opinion on the explanation provided by the Minister for the variances between established targets and the outcome of the fiscal indicators.

24. On the basis of the limitation indicated in **paragraph 18** above, I am unable to comment on whether there are any public bodies that do not form part of the specified public sector.

Compliance with Third Schedule of the FAA Act

25. My review revealed that the content of the FPP FY 2014/15 is keeping with the requirements of the Third Schedule of the FAA Act for the most part. The FPP FY 2014/15 has included the minimum content under the Fiscal Responsibility Statement and Macroeconomic Framework components. However, except for information on public private partnerships (Section B (5)) and specified public bodies (Section B (6)), the Fiscal Management Strategy contains the minimum requirements in keeping with the Third Schedule of the FAA Act.

Recommendations

26. In the event that there is a breach of the fiscal rules, an Annex itemizing such breaches and sanctions should be provided in the FPP or a statement to indicate that no such breaches occurred.

27. The Ministry should take the necessary steps to ensure that future FPPs incorporate the performance of the key fiscal risks. This will indicate what fiscal risks have materialized during the previous financial year, and the associated cost.

28. MOFP has stated its concern regarding public disclosure of market sensitive assumptions. In that regard, I propose that the Ministry provides the Auditor General's Department with an addendum to the FPP, which provides the following information: (i) sensitivity analysis based on the perceived fiscal risks, and, (ii) quantification of the growth and cost savings measures. This will aid in the assessment of the variances between the fiscal targets and the outturns, as well as the explanations provided by the Ministry.

29. An assessment of the impact of tax administrative/compliance measures over the medium term period should be considered and included in the FPP in light of the consistent revenue shortfall.

30. The Ministry should explain in future FPPs the reasons why stepped-up compliance actions did not lead to the expected revenue increases that were initially targeted; and to clarify the measures that will be undertaken in order to overcome the difficulties in achieving the revenue targets from stepped-up compliance.

Pamela Monroe Ellis, FCCA, FCA, CISA
Auditor General

Part A: Principles of Prudent Fiscal Management

Criterion A: Total [public] debt is to be reduced to, and thereafter maintained at, a prudent and sustainable level.

Related Target: To reduce the public debt to sixty per cent or less of the gross domestic product by the end of the financial year March 31, 2026 and maintain or improve the ratio thereafter.

31. 'Sustainable level' is defined as *"that level of a fiscal indicator that does not compromise the required fiscal space necessary to meet socio-economic objectives"*[2]. As it relates to 'prudent', the Ministry has indicated that a prudent debt level is 60 per cent of GDP[3].

Total Public Debt

32. The stock of Public Debt is budgeted to increase to J$2,090,410mn in FY 2014/15, which represent an increase of 7.4 per cent ($144,405mn), when compared to the outturn for the previous fiscal year. The projected total debt comprises; domestic debt of $1,096,484.5mn and external debt of $993,924.9mn. Further, the FPP FY 2014/15 indicated that the debt to GDP ratio is projected to decrease over the next three years, including a reduction to 129 per cent at the end of FY 2014/15, down from 132 per cent at the end of FY 2013/14 (Table 1). However, although the debt/GDP projection is trending downward over the medium term, this represents an average adjustment of 10 percentage points higher than the projections contained in the FPP FY 2013/14 (Table 2), which implies that the Government has encountered greater challenges in the achievement of the target.

Table 1: Debt/GDP Projections from FY 2014/15 FPP

Fiscal Year	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
Total Debt (J$M)	1,570,268	1,662,270	1,812,635	1,946,005	2,090,410	2,188,370	2,253,047
Nominal GDP	1,223,982	1,260,000	1,336,300	1,475,400	1,617,000	1,784,100	1,967,200
Debt/GDP Ratio (%)	128.3	131.5	135.6	131.9	129.3	122.7	114.5

Table 2: Debt/GDP Projections from FY 2013/14 FPP

Fiscal Year	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16	2016/17
Total Debt (J$M)	1,570,368	1,662,270	1,812,635	1,889,712	1,984,049	2,067,218	2,143,136
Nominal GDP	1,223,982	1,263,310	1,352,000	1,492,000	1,659,000	1,845,000	2,046,000
Debt/GDP Ratio (%)	128.3	131.5	134.1	126.7	119.6	112.0	104.7

[2] Section 48A, FAA (Amendment) Act, 2011
[3] Pg. 2, Par. 5 - Fiscal Responsibility Statement, FY 2011/12

Comments

33. I make reference to the definition of public debt in the FAA (Amendment) Act 2014, which states:

> *"Public debt means the consolidated debt of the specified public sector, including its government guaranteed debt (after netting out the cross holdings of debt of entities within the specified public sector, other than holdings by the Bank of Jamaica)."*

Further, the Act specifies the fiscal target for the public debt to be achieved by financial year ending March 31, 2026 (Section 48C (1)(b)).

34. However, there is a difference between the above definition and the coverage of the public debt being presented in FPP FY 2014/15, which refers to the stock of public debt directly contracted by the Central Government, Bank of Jamaica debt and Government guaranteed external debt. In addition, the stock of debt reported in the Extended Fund Facility by the IMF includes central government debt, government guaranteed external debt, government guaranteed domestic debt, and debt of the PetroCaribe Development Fund (PCDF).

Criterion B: Fiscal risks are to be managed prudently with particular reference to their quality and level.

Related Target: The Act did not specify a related target for this criterion.

35. The Ministry of Finance's definitions for 'quality' and 'level' are: (i) Quality is the possibility & likelihood of these risks becoming a cost to the Government; and (ii) Level is the quantum of cost that could be transferred to the budget if the risks materialize."

Fiscal Risk

36. The management of fiscal risks is critical to managing the growth of the public debt and other economic variables. Examples of fiscal risks include: contingent liabilities, natural disasters, interest rate risk, as well as the risk to elements of expenditure and revenue over the medium term. The FPP identifies the key sources of fiscal risks[4]. However, because of the uncertainties in the timing and amount for fiscal risks, GOJ may not, or inadequately provide for them in the budget. If the risks do materialise,

[4] See Box 2, Part III, Page 41 of FPP FY 2014/15

they could significantly reduce revenue and/or increase expenditure, and possibly result in increased debt levels.

37. I recommended in my 2013/14 FPP report, that "The Ministry of Finance should take the necessary steps to ensure that future FPPs incorporate the performance of the key fiscal risks. This will indicate what fiscal risks have materialized during the previous financial year, and the associated cost." However, the effect of the fiscal risks has still not been fully quantified, for example, with the aid of sensitivity analysis, or comprehensively explained in the 2014/15 FPP.

38. For example, in relation to Other Entities Debt Assumption, the FPP did not disclose those high risk entities or their exposures. This fiscal risk had materialized in FY 2013/14 with the assumption of debt of Clarendon Alumina Production and Wallenford Coffee Company.

39. However, the Ministry has indicated that given the definition for fiscal risks, it is not practical to set a specific target. The Ministry further stated that "Within this context, the intent is to continuously assess, monitor and manage these risks so as to minimize (a) the possibility & likelihood of these risks becoming a cost to the Government (*quality of risks*) and (b) the quantum of cost that could be transferred to the budget if the risks materialize (*level of risks*)."

Criterion C: Borrowings are to be geared toward investment activities that support productivity and economic growth.

Related Target: The Act did not specify a related target for this criterion.

40. The Ministry has not established specific targets for this principle. However, the Ministry provided a definition for **'**investment activities that support productivity and economic growth': **"***this means expenditure which seeks to enhance the country's economic capacity. Examples of this would relate to investments in physical infrastructure, transportation rehabilitation, and education-and-health."*

41. The Ministry further states that *"The investments activities of the GOJ that support productivity and economic growth are usually contained in the Capital Budget."* Our analysis shows that capital expenditure as a percentage of loan receipts is projected to decrease to 31 per cent in FY 2014/15 compared to 37 per cent in FY 2013/14, with a further projected reduction to 20 per cent in FY 2015/16, and a significant increase of 73 per cent in FY 2016/17; owing to the drastic reduction in loan receipts. (Table 3: Figure 1). However, I found that during the period 2011/12 to 2013/14, the actual capital spending had been less than what was budgeted, in keeping with the

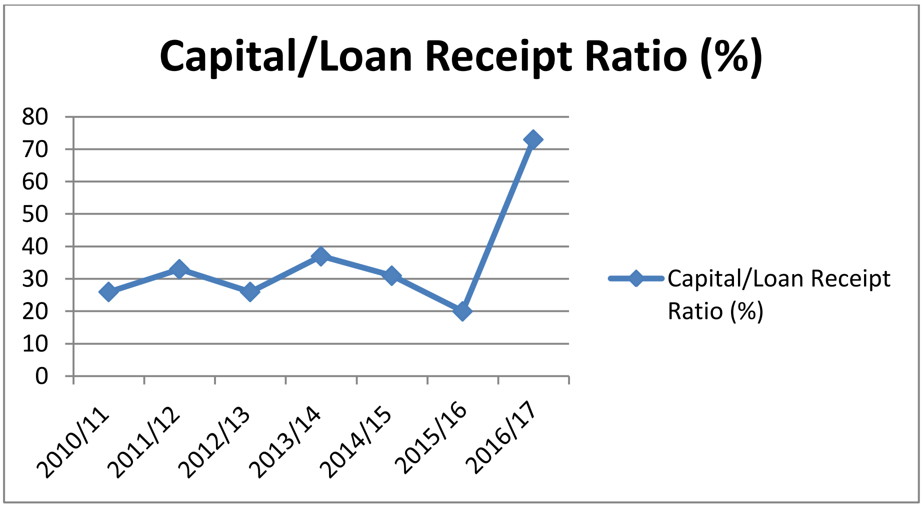
government expenditure containment measures as a result of lower revenue outturn. The government has signalled in the past that a likely fiscal adjustment to address revenue shortfall will be a reduction in the capital budget. Should that be the case, it can result in a lowering of the capital to loan receipt ratio.

Table 3: Use of Central Government Borrowing

Fiscal Year	2010/11 (J$ million)	2011/12 (J$ million)	2012/13 (J$ million)	2013/14 (J$ million)	2014/15 (J$ million)	2015/16 (J$ million)	2016/17 (J$ million)
Loan Receipts	212,968.9	163,520.5	144,347.1	94,290.6	110,894.5	185,465.2	56,462.9
Capital	55,594.1	53,230.9	37,757.9	35,171.8	34,628.1	37,326.6	41,157.1
Capital/Loan Receipt Ratio (%)	26	33	26	37	31	20	73
Capital: Budget less actual	-14,739.7	9,975.5	1,735.1	9,550.0			

Source: Ministry of Finance

Figure 1: Capital to loan receipt ratio (%) for FYs 2010/11 to 2016/17



Source: Ministry of Finance

Criterion D: Expenditure is to be managed in a manner that is consistent with the level of revenue generated, so as to achieve the desired fiscal outcomes.

RELATED TARGET: To reduce the ratio of wages paid by the government as a proportion of the Gross Domestic Product to 9 per cent or less by the end of the Financial Year ending on March 31, 2016 [FAA Act, Section 48C (c)]

42. The main factors that impact on this principle, vis-à-vis the identified targets, include Tax Revenue, Wages & Salaries, Interest Costs, Recurrent Programme Expenditure, and Capital Expenditure.

Tax Revenue

43. For FY 2014/15, tax revenue of $384,286.0mn, which accounts for approximately 89.8 per cent of total revenue, is budgeted to grow by 11.8 per cent ($40,449.8mn) over collections in FY 2013/14. This year's (2014/15) FPP explained that: "The tax revenue forecast for FY 2014/15 is expected to be positively impacted by stepped-up compliance activities by TAJ and JCA. These compliance activities are forecast to bolster tax revenue flows by about 0.4 per cent of GDP. The budgeted increase in tax revenue is also predicated on a projected 9.6 per cent growth in nominal income in FY 2014/15 as well as upward movements in other macroeconomic variables." However, **Table 4** shows that the tax revenue targets have not been achieved in the last six years.

Table 4: Tax Revenue – Budgeted vs. Actual

Fiscal Year	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15
Tax Revenue Budget J$M	265,071.6	291,674.5	287,211.3	308,215.3	335,625.1	360,517.6	384,286.0
Tax Revenue Actual J$M	246,216.6	265,860.2	279,874.2	289,882.2	319,764.9	343,836.1	-
Variance J$M	-18,855.00	-25,814.30	-7,337.10	-18,333.10	-15,860.20	16.681.5	-
Variance %	-7.11%	-8.85%	-2.55%	-5.95%	-4.73%	-4.63%	-

Table 5: Trends in Revenue & Grants, Expenditure and Primary Balance

	Actual 2010/11	Actual 2011/12	Actual 2012/13	Prov. 2013/14	Proj. 2014/15	Proj. 2015/16	Proj. 2016/17
Revenue & Grants	**314,558.5**	**322,149.8**	**344,677.7**	**397,178.2**	**427,888.5**	**451,558.5**	**493,553.1**
Expenditure	**388,767.9**	**403,122.2**	**399,278.9**	**395,420.7**	**439,282.6**	**447,867.8**	**465,920.6**
Programme	76,917.9	89,699.4	87,201.5	93,967.7	110,281.1	119,103.5	128,631.8
Wages & Salaries	127,901.3	139,556.9	147,381.8	153,361.7	161,704.3	161,321.1	176,224.2
Interest	128,354.7	120,635.0	126,937.7	109,919.5	132,669.1	130,116.8	119,907.5
Capital Expenditure	55,594.1	53,230.9	37,757.9	35,171.8	34,628.1	37,326.3	41,157.1
Primary Balance[5]	**54,145.2**	**39,662.6**	**72,336.5**	**111,677.1**	**121,275.0**	**133,807.7**	**147,540.1**
Primary Balance % of GDP	4.5%	5.0%	6.0%	7.5%	7.5%	7.5%	7.5%

[5] Primary balance is the difference between Revenue & Grants and Expenditure (excluding interest cost).

Wages & Salaries

44. The FPP FY 2014/15 projects that the wages and salaries will be $161,704.3mn in FY 2014/15, which represents a 3.4 per cent increase over FY 2013/14. Wages and salaries is expected to be 10 per cent of GDP, compared to 10.6 per cent of GDP in FY 2013/14. The FPP projects that this will be 9 per cent of GDP in both FYs 2015/16 and 2016/17, which is within the legislated target.

Interest Cost

45. The FPP projected interest cost of $132,669.1mn for FY 2014/15, which represents an increase of 20.7 per cent compared with the figure for the previous year. Interest cost as a percentage of GDP, is estimated to be 8.1 per cent in FY 2014/15 compared to 7.5 per cent in FY 2013/14, largely due to higher domestic interest rate, increased provision on guaranteed loans and the depreciation of the Jamaican dollar.

Recurrent Programme Expenditure

46. The recurrent programme expenditure is budgeted to be $110,281.1mn, a 17.4 per cent increase over the outturn for the previous fiscal year. This is projected to be 6.8 per cent and 6.7 per cent of GDP in FY 2014/15 and 2015/16 respectively.

Capital Expenditure

47. The capital expenditure projection for FY 2014/15 is $34,628.1mn, which is 1.5 per cent less than the provisional expenditure in FY 2013/14. This represents a decrease from the 2.4 per cent of GDP outturn in FY 2013/14 to 2.1 per cent of GDP projected for FY 2014/15. The FPP FY 2014/15 indicated that the reduction was mainly due to the transfer of recurring maintenance, non-capital and one-off type expenditures to the Recurrent Budget of the respective MDAs.

Primary Balance

48. The government continues to maintain a primary surplus target of 7.5 per cent of GDP over the medium term in keeping with the terms of the IMF Extended Fund Facilities. See **Table 5.**

Part B: Reasonableness of Deviation of Fiscal Indicators

49. Section 48B (5)(d)(ii) of the FAA Act requires the Minister to compare the outcome of the fiscal indicators with the targets for the previous financial year and give reasons for any deviations.

50. Section 48B (6) of the FAA Act requires that the Auditor General indicates whether the reasons given pursuant to subsection (5)(d)(ii) are reasonable having regard to the circumstances.

51. I have reviewed the explanations provided in the FPP, as shown in Table 6. In making a determination regarding the reasonableness of the explanations provided by the Minister, I applied the following criteria:

    - whether initial projections considered fiscal risks; and
    - my ability to confirm the Minister's explanation with observed data.

52. My review of the 2014/15 FPP revealed that, though some fiscal risks were mentioned therein, they were not quantified or reflected in the projections. Consequently, it was not clear to what extent deviations, such as underperformance of revenue, were due to forecast errors, modification of assumptions, or unforeseen events/shocks. In my reports on the 2011/12, 2012/13 and 2013/14 FPPs, I recommended that fiscal risks should be identified and reflected accordingly in the FPP.

53. The response provided by the Minister of Finance with respect to the explanations for fiscal deviation is shown in Table 6.

Table 6: Audit Comments on the Explanations for Fiscal Deviations for FY 2013-14

	Prov	Budget					
Item	**Apr - Mar**	**Apr - Mar**	**Diff**	**Diff %**	**GOJ's Explanation as Stated in FY2013-14 FPP**	**Audit Comments**	**Ministry's Response**
Revenue & Grants	**397,178.2**	**407,160.3**	**-9,982.1**	**-2.5%**			
Tax Revenue	343,836.1	360,517.6	-16,681.5	-4.6%	The shortfall was influenced by lower collections from most types. The significant shortfall arose largely from:		
					• significantly lower than budgeted collections from the administrative/ compliance activities;	Every year, there is a compliance component. Compliance measures have under-performed significantly in the last four fiscal years, at least.	
					• faster than programmed decline in imports;	The expectation was for decline in import, and so tax revenue would be lost. However, we needed this assumption to be provided at the beginning of the fiscal year 2013/14 and for projections for the (lost) revenue from declining import.	Noted. It's not practical to detail all the assumptions in the FPP. The MOFP is however willing to provide the assumptions on imports for 2014/14 to the AGD.
					• reduced employment in some sectors of the economy;	The Minister needs to quantify the effect of the net reduction in employment on tax revenue.	
					• lower than programmed inflation; and		
					• underperformance of some of the new measures implemented in March 2013 and April 2013;		

Income and Profit	112,647.7	119,153.6	-6,505.9	-5.5%	• Reduced employment in some sectors of the economy, lower than expected collection from compliance effort and less than budgeted wages for the fiscal year, negatively affected PAYE.	The Minister needs to quantify the effect of the net reduction in employment on tax revenue.	Noted. It is difficult to isolate and quantify all the various impacts as there are confounding factors that do impact economic activity and revenue flows.
					• Corporate taxes performed below budget...mainly due to lower than targeted flows from administrative efforts. Similar to Corporate taxes, the underperformance of Other Individuals/Self-Employed resulted largely from lower than budgeted collections from administrative efforts.		
					• With respect to Tax on Dividend, the shortfall arose as companies had declared dividends earlier than anticipated, during the previous fiscal year, to avoid the increased rate from 5% to 15%, effective April 2013.		
Production and Consumption							
Betting, Gaming & Lottery	2,455.7	3,740.0	-1,284.2	-34.3%	The budgeted receipts from the proposed new measures were not realized. The amendments to the fee structure and gross profit tax for the BGL sector were not implemented as originally proposed due to setbacks in passage of the legislation. The expected legislation is expected to be in effect during FY 2014/15.	Since the legislation to implement this new revenue measure during the FY 2013/14 was not enacted, the Ministry should have anticipated that this would have impacted on the collection, given that this measure was set to take effect at the start of the fiscal year.	The MOFP did not anticipate that kind of delay with the legislation.
Education Tax	18,103.8	19,272.7	-1,168.8	-6.1%	The Education Tax, which fell short		

					of budget by $1,168.8mn, was impacted by the same factors that resulted in lower PAYE collections (lower than anticipated employment and compliance). [Part III Page 7]		
Contractors Levy	991.5	1,427.3	-435.8	-30.5	• The shortfall emanated largely from the slower than anticipated pick up in construction activity during FY 2013/14.	The provisional outturn for FY 2013/14 of 2.5 per cent increase matches projection from the previous year.	
GCT (Local)	61,265.1	59,552.8	1,712.3	2.9%	These three tax types were positively impacted in FY 2013/14 by the carry-over of collections that were programmed for March 31, 2013 but with that date falling on a weekend, the due date for payment was extended to April 2, 2013. As was reported in the April 2013 FPP, this factor also contributed to the shortfall in these three tax types in FY 2012/13.		
Telephone Call Tax	6,539.8	5,697.1	842.7	14.8%			
Accommodation Tax	1717.7	1,264.6	453.1	35.%			
International Trade	113,891.8	121,928.2	-8,036.4	-6.6%	• All sub-categories with the exception of Travel Tax and Stamp Duty registered shortfalls. The shortfalls arose mainly from a sharper than budgeted reduction in imports.		
Travel Tax	9,187.0	6,865.0	2,322.0	33.8%	• This considerable increase was due mainly to improved compliance in the collection of the air passenger levy, including collection of arrears. The levy was introduced in September 2012 but underperformed during the first few months of implementation as some airlines		

					did not remit the collections in a timely manner. In FY 2013/14, the Jamaica Customs Agency moved aggressively against airlines that have been delinquent in remitting taxes due to the GOJ, resulting in improved compliance and increased inflows.		
SCT (Import)	25,962.5	30,456.1	-4,493.5	-14.8%	• A significant contributor to the shortfall was a sharp decline in importation of tobacco products arising from the ban on cigarette smoking in public spaces. Lower than programmed importation of motor vehicles, especially new motor vehicles, and refined petroleum products also led to the shortfall in SCT collections.		
Custom Duty	25,559.3	28,892.4	-3,333.1	-11.5%	In addition to the sharper than budgeted reduction in imports, Custom Duty and GCT were also impacted by lower than programmed collections from compliance/administrative improvements.		
GCT (Import)	51,237.5	53,893.0	-2,655.5	-4.9%			
Environmental Levy	2,084.2	2,346.1	-261.9	-11.2%	Similar to International Trade taxes, lower import values contributed to the underperformance of the Environmental Levy.		
Non-Tax Revenue	41,047.1	34,553.2	6,493.9	18.8%	On April 1, 2013, the CAF was introduced to supplant the Customs User Fee (CUF) and other fees that previously applied at Jamaica Customs Department and this measure has contributed to the		

					improved revenue performance.		
					Also contributing to the higher Non-tax revenue intake were unprogrammed receipts of $5,475.0mn and $1,533.0mn from telecommunications companies Digicel and LIME, respectively. These payments were for renewal of the respective telecommunications licenses ahead of schedule.		
Bauxite Levy	1,009.5	1,540.2	-530.7	-34.5%	The shortfall stemmed from a combination of lower than anticipated aluminium prices on the London Metal Exchange (LME), as well as below programmed bauxite production.		
Capital Revenue	658.1	1,127.0	-468.9	-41.6%	Lower than budgeted collections from loan repayments and royalties from the bauxite/alumina sector contributed most significantly to the shortfall.		
Grants	10,627.4	9,422.3	1,205.1	12.8%	The increase in Grants was due to the receipt of unprogrammed budget support inflows from the European Union (EU), which outweighed shortfall in Grants for capital programmes that stemmed from the slower than planned execution of capital spending.		
Expenditure	**395,420.7**	**415,206.1**	**-19,785.4**	**-4.8%**			
Recurrent Expenditure	360,248.9	370,484.3	-10,235.3	-2.8%	Lower interest payments, particularly on the domestic side,		

					were primarily responsible for the reduced recurrent expenditure.		
Programmes	93,967.7	93,664.2	303.5	0.3%			
Wages & Salaries	156,361.7	157,253.3	-891.7	-0.6%			
Interest	109,919.5	119,566.8	-9.647.2	-8.1%			
Domestic	68,728.9	75,523.1	-6.794.2	-9.0%	The lower than budgeted Domestic Interest payments were due mainly to greater than anticipated saving from the National Debt Exchange (NDX) undertaken in February 2013.		
External	41,190.6	44,043.6	-2,853.1	-6.5%	The lower External Interest costs resulted mainly from a combination of slower than programmed disbursement of external loans as well as a reduction in the amount spent against a contingency provision for loan raising expenses.		
Capital Expenditure	35,171.8	44,721.8	-9,550.1	-21.4%	This reduction reflected restraint in government spending against the backdrop of lower than budgeted revenue, as well as a slower pace of project implementation.		
Fiscal Balance (Surplus+/ Deficit-)	**1,757.5**	**-8,045.8**	**9,803.4**	**121.8%**			
Loan Receipts	**94,290.6**	**103,279.6**	**-8,989.0**	**-8.7%**	The shortfall from external sources was nevertheless made up on the domestic side in the form of higher inflows from the PetroCaribe Development Fund.	No explanation provided for variances on the external loan receipts.	
Domestic	40,119.9	13,777.5	26,342.4	191.2%			
External	54,170.7	89,502.1	-35,331.4	-39.5%			
Project Loans	10,377.2	13,134.1	-2,756.8	-21.0%			
Other	43,793.5	76,368.0	-32,574.5	-42.7%			

Amortization	**106,640.2**	**105,680.4**	**959.8**	**0.9%**			
Domestic	76,604.4	76,387.4	217.0	0.3%			
External	30,035.8	29,293.0	742.8	2.5%			
Primary Balance (Surplus+/Deficit-)	**111,677.1**	**111,520.9**	**156.1**	**0.1%**			

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