

CAYMAN ISLANDS GOVERNMENT: FRAMEWORK FOR FISCAL RESPONSIBILITY

1. The Cayman Islands Government remains fully committed to deliver on the promises it has made to the people of the Cayman Islands. These include:
 - Creating a vibrant and sustainable economy;
 - Enhancing tourism and financial services as the twin pillars of the economy; and
 - Creating opportunities for Caymanians.

2. Restoring prudent fiscal management is central to achieving these objectives, and will help create an environment in which people and businesses can plan for the future with confidence. The Cayman Islands Government's fiscal strategy consists of the following five components:
 - Controlling Government expenditure;
 - Limiting new borrowings;
 - Re-aligning the revenue base;
 - Improving the performance of Statutory Authorities and Government Companies; and
 - Reducing costs by working in partnership with the private sector.

3. The Cayman Islands Government's approach will continue to be open and transparent, consistent with the highest standards of governance and democracy. That is why the Cayman Islands Government published its Cayman Islands Government 3 Year Budget Forecast (2010/2011 to 2012/13) ("three year plan") in June 2010, and is committed to strengthening its Public Management and Finance Law (PMFL).

4. This Framework ("the Framework") sets out the key principles that will be encapsulated in the revised PMFL which will also specify the detailed requirements necessary to deliver the principles in practice. Subject to the agreement of the Legislative Assembly, the revised PMFL will enter into force by 1 July 2012.

5. The Cayman Islands Government and the United Kingdom Government reaffirm their commitment to work in partnership and to respect the rights and responsibilities specified in the Framework and the revised PMFL.

POLICY PRINCIPLES

6. The Cayman Islands Government is committed to the following principles:
 - a. Effective **medium-term planning**, to ensure that the full impact of fiscal decisions is understood;
 - b. Putting **value for money** considerations at the heart of the decision making process;
 - c. Effective **management of risk**; and
 - d. Delivering improved **accountability** in all public sector operations.

IMPROVING MEDIUM TERM PLANNING

Strategic Policy Statement

7. The Cayman Islands Government will assess the impact of all proposals and decisions on expenditure, revenues, and borrowing in the context of a Strategic Policy Statement (SPS) covering a period of at least three fiscal years.
8. The SPS will include, as a minimum, the information defined in paragraph 14 of Annex A.

Transparency

9. The SPS will be updated and published annually. The budget that is presented for the forthcoming fiscal year will be consistent with the SPS.

Measurement

10. The collection of accurate internal and external economic, business and social data is fundamental to effective medium term fiscal planning.
11. The Cayman Islands Government will assess any gaps in information that is required and take steps to improve inputs to the SPS, by:
 - publishing and delivering a plan to improve the quality and independence of statistical data gathered from both the public and private sectors in order to measure accurately key national data including economic growth, inflation, and employment;
 - developing robust econometric models to assist with forecasting coercive revenue; and
 - developing a reporting framework to ensure that the Cayman Islands Government receives information about in-year developments in expenditure, performance against objectives and developing risks (whether or not quantifiable) from government departments and other bodies in receipt of public funds.

DELIVERING VALUE FOR MONEY

12. The Cayman Islands Government recognises that achieving value for money is central to the appropriate use of public funds. Central government and other public sector bodies will therefore ensure that effective processes are in place to provide confidence and ensure suitability, effectiveness, prudence, quality, good value and avoidance of error and other waste.

Projects

13. There are five key stages that will be undertaken by the Cayman Islands Government in the planning, development and execution of a project:
 - a. appraisal and business case;
 - b. procurement;
 - c. contract management;

- d. delivery; and
- e. evaluation.

Appraisal and business case

14. The Cayman Islands Government will ensure that all projects, whether funded from recurrent surpluses, conventional borrowing or all alternative financing transactions, are suitably appraised before the procurement stage to ensure value for money and that a robust cost-benefit analysis has been carried out.
15. For projects with a lifetime value above CI\$10m and for those where the use of Public Private Partnerships (PPPs) or any other form of alternative financing is being considered, the Cayman Islands Government will also retain independent accounting, legal, financial, economic, environmental and other technical advice as appropriate to ensure robust investment appraisals are produced.
16. For all projects, the business case which results from the appraisal process should: demonstrate the economic need for the project; include a fully argued and costed risk and impact assessment; and specify the benefits the project is designed to deliver to ensure that an informed decision can be made on whether or not to proceed to the procurement stage.
17. PPPs or any other form of alternative financing will only be considered:
 - a. where there is a sound appraisal underpinning the proposed project before the financing means has been determined;
 - b. where a financial appraisal demonstrates improved value for money against a conventionally financed alternative;
 - c. where the long term affordability case has been assessed and agreed by the appropriate technical experts retained by the Cayman Islands Government; and
 - d. where an independent opinion has been received from a qualified accountant of good standing on the correct accounting treatment in the Cayman Islands Government's accounts.
18. PPPs or any other form of alternative financing will not be considered by the Cayman Islands Government for:
 - a. projects with a lifetime value of less than CI\$15 million and therefore too small to justify the transaction costs; or
 - b. projects where the fast pace of change in the sector makes it difficult to effectively define the outputs it requires in a long term contract (such as Information and Communication Technology projects).
19. All proposed capital projects with an expected lifetime value of CI\$10 million or more will be incorporated in the published SPS, and appraisals will be published for public consultation prior to procurement.

Procurement

20. Procurement processes will be open, transparent and competitive. The Cayman Islands Government will adhere to agreed statutory tender processes. For projects with a lifetime

value above CI\$10m and for those where the Public Private Partnerships (PPPs) or any other form of alternative financing is used, the Cayman Islands Government will retain independent accounting, legal, financial, economic, environmental, and other technical advice as appropriate to ensure value for money.

Contract management

21. The Cayman Islands Government will retain sufficient expert advice, whether internal or external, to ensure that it is an "intelligent customer" of services or other arrangements agreed with private sector suppliers.

Delivery

22. The Cayman Islands Government will put together sufficiently competent teams to manage all projects and ensure receipt of high quality services and products as agreed at the procurement stage.

Evaluation

23. For projects with an expected lifetime value of more than CI\$10 million, the Cayman Islands Government will undertake an evaluation of project performance within a reasonable timescale. This evaluation will be made publicly available. This will ensure that the lessons learned will strengthen the decision-making process and overall project performance.

Processes

24. The Cayman Islands Government will establish and maintain robust processes to:
 - a. measure the performance of government departments and other bodies in receipt of public funds;
 - b. allocate expense budgets, profile expenses and monitor actual results against profile budget in a timely manner;
 - c. determine revenue targets, profile receipts and monitor actual results against budget on a timely basis;
 - d. track and quantify developing risks to determine the value of actual and contingent liabilities to assess calls on current expenditure budgets and, in exceptional cases, the reserves;
 - e. report total public sector debt, profile debt repayments and determine debt service costs;
 - f. undertake timely internal and external audits and act on the findings.

MANAGING RISKS

Contingent and actual liabilities

25. The Cayman Islands Government is committed to managing risks and ensuring that contingent and actual liabilities which accrue are consistent with sustainable public finances.

26. The Cayman Islands Government will make contingent and actual liabilities, including (but not limited to) pensions and healthcare schemes, subject to actuarial assessments at least every three years. Actuarial assessments will be published within three months of receipt. The Government will publish its proposals to address the results of the assessments no later than the budget following the receipt of the actuarial assessment.
27. The Cayman Islands Government will set out in the SPS its strategy for managing contingent and actual liabilities and report on progress in delivering the strategy.

Debt

28. Unless in exceptional circumstances different arrangements are agreed in writing by the Cayman Islands Government and the Secretary of State, the Cayman Islands Government will borrow only to fund capital expenditure where:
 - a. The proposed project is forecast to yield sufficient revenues to fund the additional debt service costs; or
 - b. The Government can demonstrate that it has sufficient surplus operating cash flows to fund the additional debt service costs which arise from borrowing to finance such capital expenditure.
29. The Cayman Islands Government will give preference to borrowing from concessional lenders which should ensure that the lender's expertise is brought to projects.
30. To ensure that the level of debt is affordable and consistent with the delivery of macroeconomic and fiscal sustainability and financial stability in the short, medium and long term, the Cayman Islands Government will:
 - a. comply with the borrowing limits defined in Annex A by no later than the dates specified in Annex D;
 - b. remain in compliance with the borrowing limits subsequent to the dates specified in Annex D or such earlier date by which compliance is achieved; and
 - c. put in place arrangements to repay loan principal.
31. The repayment of principal will be achieved either through:
 - a. agreeing a fully amortized structure with the lending institution; or
 - b. establishing a dedicated sinking fund with a binding contribution schedule capable of offsetting the outstanding principal repayment on maturity of the debt.

ACCOUNTABILITY

32. The Cayman Islands Government is committed to delivering improved accountability mechanisms through the transparency delivered by the Framework and subsequently the revised PMFL and by ensuring that public accounts are:
 - a. prepared on a timely basis in line with International Financial Reporting Standards and International Public Sector Accounting Standards; and
 - b. subject to an annual external audit - the results of which will be subject to the Public Accounts Committee's scrutiny and publications.

PARTNERSHIP WITH THE UK

33. In support of the commitments to deliver fiscal responsibility made by the Cayman Islands Government, the United Kingdom Government will:
- a. undertake an annual assessment of the economy of the Cayman Islands, including the state of the public finances;
 - b. provide technical assistance by monitoring compliance with the Framework and the revised PMFL;
 - c. provide support in identifying sources of expertise at the request of the Cayman Islands Government;
 - d. consider requests for technical support made by the Cayman Islands Government where any such requests are accompanied by a business case and specific terms of reference.

Exchange of information

34. The Cayman Islands Government will submit the information specified in Annex C to the person(s) from time to time specified by the United Kingdom Government.
35. The Cayman Islands Government will supply the United Kingdom Government with such other information it may request, including further information on:
- a. any aspect of the SPS, including specific capital investment projects and proposed borrowing; and
 - b. the draft budget.
36. All information will be submitted by the Cayman Islands Government within the timescales specified in Annex C unless, in exceptional circumstances, different timescales are agreed in writing by the Cayman Islands Government and the United Kingdom Government.

Consideration of representations

37. The Cayman Islands Government will consider fully any representations made by the Secretary of State on the information provided.
38. The Cayman Islands Government will not proceed with any project on which the Secretary of State has made representations until fifteen working days after a full written response has been received by the Secretary of State to those representations.

Approvals Process

39. Where the Cayman Islands Government is not in compliance with the Framework, the Cayman Islands Government will present, for the approval of the Secretary of State, a plan that is consistent with the SPS to remedy the breach. The maximum period which may be permitted to rectify a breach is three fiscal years from the point at which the breach occurred or, in exceptional circumstances, such other period that may be agreed in writing between the Cayman Islands Government and the Secretary of State.

40. In the event of any non-compliance by the Cayman Islands Government in the respect of the Framework and until the breach has been rectified the Cayman Islands Government will obtain, on an annual basis, written approval from the Secretary of State before:

- a. the SPS is finalised;
- b. any public borrowing or any refinancing of public borrowing is undertaken;
- c. proceeding with any project with a lifetime value of more than CI\$10 million;
- d. using public assets as collateral as part of any arrangement with a party external to Cayman Islands Government;
- e. the hypothecation of any revenue stream; or
- f. the divestment of public assets.

41. For the avoidance of doubt, any failure to comply with the borrowing limits or forecast failure to comply within the lifetime of the SPS will be deemed a failure to comply with the Framework.

42. In exceptional cases, the Cayman Islands Government may request the Secretary of State's approval to make in-year changes to the approach set out in the SPS. In such cases, the Cayman Islands Government will supply the Secretary of State with:

- a. a written request to make the changes, to be received no later than two months before such changes are considered to be required by the Cayman Islands Government unless a shorter period is agreed in writing by the Cayman Islands Government and the United Kingdom Government;
- b. a compelling evidence based business case to support the request for approval; and
- c. a revised SPS, which sets out the measures the Cayman Islands Government intends to take to return to the course set previously. If approval is granted, the Cayman Islands Government will publish the revised SPS.

Signed: 
Premier, Cayman Islands

Date: 23rd Nov. 2011.

Signed: 
Minister for Overseas Territories, Foreign and Commonwealth Office

Date: 27/11/11

ANNEX A: DEFINITIONS

1. **Expenditure**, unless otherwise specified, refers to all public expenditure (inclusive of grants, capital and recurrent expenditure).
2. **Public accounts** include all the accounts of the Cayman Islands Government and of all Statutory Authorities/Government Companies.
3. **Public borrowing** includes:
 - conventional borrowing from commercial and concessional institutions;
 - the capitalised value of all alternative financing transactions (including PFI/PPP arrangements) that will place future financial obligations (in terms of increased expenditure or reduced revenue) on the Cayman Islands Government;
 - the risk weighted debts and PPP/PFI arrangements of statutory authorities, government corporations and companies;
 - borrowing that is contracted by the Cayman Islands Government, but then on-lent; and
 - any other debt guaranteed by the Cayman Islands Government.
4. Public borrowing taken out to clear "informal debt" or debt owed by one public sector entity or another (including arrears of such debts) will be treated as new debt.
5. The risk weighting attached to debts and PPP/PFI arrangements of Statutory Authorities/Government Companies will be agreed with the Secretary of State according to the following criteria:

Risk-weighting	Description
100%	Outstanding contractual commitments to PFI or PPP arrangements of any form, agencies with a consistent demand for grants
80%	A high likelihood of grants being required
50%	Moderate likelihood of grants being required
20%	No grants required in the last three years

6. A list of Statutory Authorities/Government Companies with assigned risk-weights is attached at Annex B. Risk-weights can be updated to reflect recent financial performance at the request of either the Cayman Islands Government or the Secretary of State.
7. The Cayman Islands Government and the Secretary of State will agree risk-weights for new Statutory Authorities/Government Companies before any such Statutory Authority/Government Company can take on debt.
8. **Borrowing limits** mean the following:

<u>Net Debt</u>	80% maximum of operating revenue	of <u>Debt Service</u>	10% maximum of operating revenue	of <u>Liquid Assets</u>	At least 25% of operating expenses
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9. **Operating Revenue** consists of coercive and non coercive revenue as defined in the PMFL.

10. **Net Debt** is defined as the total outstanding value of public borrowing minus liquid assets.
11. **Debt service** is defined as annual payments resulting from public borrowing commitments and finance leases or any other form of borrowing.
12. **Liquid Assets** are defined as the lowest balance of liquid funds at the disposal of the Cayman Islands Government during the fiscal years, which shall be forecast in the Strategic Policy Statement. These funds should not be pledged against budgeted expenses or liabilities of any form.
13. **Past fiscal performance**, unless otherwise specified, should be assessed on the basis of audited financial statements for the previous financial year, where available. In the event that such statements are unavailable, the summary Operating Statement with associated variance analysis to original budget should be used.
14. **Lifetime value** is defined as the discounted net present value of financing obligations calculated using a discount rate of 3.5% - which shall be subject to periodic review to assess its appropriateness.
15. **Strategic Policy Statement** means a document which, at a minimum, sets out:
 - A statement of the Cayman Islands Government's economic and fiscal objectives;
 - A summary of the broad outcomes, the specific outcomes, and the links between them, that the Cayman Islands Government intends to achieve in the next financial year and for at least the following two financial years;
 - A summary of recent economic statistics, trends and forecasts;
 - A statement of the prior two years fiscal performance, and analysis of variance from previous budgets and plans;
 - A statement of existing public sector borrowing, including Statutory Authorities/ Government Companies (whether guaranteed by government or not). For each loan this should include quantum, currency, date and origin of issue, maturity, and interest rate structure;
 - The Accounts Receivable Aging Summary of the Cayman Islands Government and the associated Bad Debt Summary;
 - The detailed breakdown of forecast operating revenue and expenses for the current and next three financial years;
 - A statement detailing the actual and contingent liabilities of the Cayman Islands Government and an explanation of how each will be managed/financed, progress to date and intended financing for the current and next three financial years;
 - A capital investment plan for the next financial year and for each of the following two financial years. This should include details of new and continuing projects which are anticipated to have a lifetime value of over CI\$10m for the next financial year and for each of the following two financial years;
 - Anticipated revenue and expense measures and actions for the next financial year and for each of the following two financial years;
 - A statement of the current position and forecasts for the next three financial years for each of the following:
 - Forecast summary Operating Statement;
 - Forecast summary Balance Sheet;
 - Forecast summary Statement of Cash Flows;

- Operating expenses performance by Ministry/Portfolio;
- Operating Revenue performance by Ministry and Portfolio;
- Reserve levels for each month;
- Borrowing;
- Performance against borrowing limits;
- Surplus or deficit, being the difference between total operating revenue and total operating expenses;
- Net worth;
- Net cash flows for each of its operating, investing and financing activities;
- The anticipated impact of any proposals to refinance existing debt;
- The value of contingent and actual liabilities, including pensions and healthcare schemes, and the steps taken to mitigate these liabilities;
- The approximate amount of executive expenses allocated to each minister, official member, the Office of the Complaints Commissioner, the Office of the Information Commissioner and the Audit Office for each financial year,.

ANNEX B: STATUTORY AUTHORITY AND GOVERNMENT COMPANY RISK-WEIGHTS

<i>Statutory Agency/Government Company</i>	<i>Risk Weight</i>
<i>Cayman Airways Ltd</i>	80%
<i>National Housing Development Trust</i>	80%
<i>Tourism Attractions Board</i>	80%
<i>Cayman Turtle Farm (1983) Ltd</i>	80%
<i>Cayman Islands Development Bank</i>	50%
<i>Cayman Islands Airports Authority</i>	20%
<i>University College of the Cayman Islands</i>	20%
<i>Port Authority</i>	20%
<i>Water Authority</i>	20%
<i>Civil Aviation Authority</i>	20%

ANNEX C: MONITORING

The Cayman Islands Government will provide the following information to the United Kingdom Government:

- Triennially: Actuarial reviews of contingent and actual liabilities, including healthcare and pensions provisions.
- Annually:
- (i) Annual audit reports for the Cayman Islands Government and Statutory Authorities/Government Companies.
 - (ii) Debt and PPP/PFI breakdown for Cayman Islands Government and Statutory Authorities/Government Companies.
 - (iii) Annual updates on GDP figures, employment, and the performance of key sectors to the extent that this is not separately identified in budget documentation or the SPS.
 - (iv) The Cayman Islands Government's SPS, accompanied by a written request for any approvals that may be necessary over the course of the next fiscal year owing to the Cayman Islands Government failing to comply with the Framework. Both should be submitted to the United Kingdom Government no later than three weeks before the SPS is due to be published.
 - (v) The Cayman Islands Government budget in draft no less than three weeks before it is due to be presented, and when finalised.
- Monthly:
- (i) Liquid Assets fund balances and variance analysis.
 - (ii) Revenue and capital and operating expenses, actual performance and forecast reports with accompanying variance analysis.
- On request:
- (i) Details of the stock and composition of debt, currency, date and origin of issue, maturity, and interest rate structure.
 - (ii) Updates on capital project progress.
 - (iii) Details of proposed capital investments, PFI, PPP and alternative forms of private finance, an independent accounting opinion on the IFRS accounting treatment and the capitalised value of the arrangement, and implications for public expenditure prepared and signed off by appropriate independent professionals.
 - (iv) Completed investment appraisals.
 - (v) Such other information as may reasonably be requested.

ANNEX D: TRANSITIONAL PROVISIONS

1. The unprecedented global financial crisis has forced the Cayman Islands Government to operate beyond the borrowing limits defined in Annex A.
2. The Cayman Islands Government will return to compliance with the borrowing limits by the following dates:
 - **Net debt:** by no later than the end of the Cayman Islands Government financial year 2015-16;
 - **Debt service:** by no later than the end of the Cayman Islands Government financial year 2015-16; and
 - **Liquid assets:** by no later than the end of the Cayman Islands Government financial year 2015-16.