

Presentation University of Sint Maarten, 22 October 2018

Ladies and gentlemen, welcome to this lecture on “working towards sustainable government finances”. It’s with great pleasure that I stand here before you.

The aim of this lecture is to give you an insight in the work of the boards of financial supervision and the challenges we face, including the legal framework which we have to follow. I have given a similar presentation in Curaçao during our previous board visit in June.

After eight years of financial supervision for the Caribbean part of the Kingdom of the Netherlands we have reached a phase where it’s time to look back at the results and ask ourselves if the toolbox made available to us, is in need of some changes.

SHEET 2

Tonight, I would like to discuss the following with you:

- The legal framework in which the supervisory board is allowed to operate
- The background of the Cft and our tasks
- The budget cycle of Sint Maarten and Curaçao
- The toolbox which we have at our disposal
- The results of financial supervision thus far
- The public finance figures in three countries. I especially focus on debt to GDP ratio.
- The past evaluation in 2015 and the coming evaluation in 2018.

The basis for this supervision differs per country and is also different for the public entities. This is also the reason why three different boards of financial supervision were installed.

I will start by briefly explaining what this basis of supervision is while also giving some background information. Of course, I will refer to the extraordinary circumstances Sint Maarten is facing due to the devastating effects of the hurricanes Irma and Maria.

SHEET 4

Let me start with the financial supervision for Curaçao and Sint Maarten. The citizens and governments of the former Netherlands Antilles started engaging in discussions about a new political structure at the beginning of this century. This had led to a reform of the existing political structures within the Kingdom of the Netherlands in 2010, more specifically on the tenth of October. Moreover, the countries came to an agreement that the Netherlands would restructure the debt of the Netherlands Antilles in the amount of 3.4 billion guilders, upon the condition that financial supervision would be established. The debt to GDP ratio was unsustainable with more than 70% GDP. This agreement was the basis for the financial supervision to ensure sustainable government finances and is laid down in the “Rijkswet financieel toezicht” or in English the Kingdom Act financial supervision Curaçao and Sint Maarten.

SHEET 5

A different structure was chosen for the public entities Saba, Statia and Bonaire. These entities have become special municipalities of the Netherlands. Financial supervision is set in the same manner as the municipal law in the Netherlands. Cft BES is a supervisor on behalf of

the State secretary of the interior and kingdom affairs. Due to the law on grove task neglect, a special situation applies for Statia. Currently the role of the Cft in this is limited.

SHEET 6

Financial supervision in Aruba has a different and shorter history. In 2014, the Cft carried out an investigation into the budget, at the request of the governor. At that time, Aruba was faced with a debt ratio of more than 80% GDP. The Cft gave several recommendations in order for Aruba to obtain a balanced budget. Partly based on the agreements, it was finally decided to establish independent financial supervision, the CAft. The protocol of May 2nd, 2015 formed the basis for financial supervision and the ordinance Aruba temporary financial supervision.

The framework outlined in the national ordinance is applicable until the end of 2018, but the goal of a surplus of a half percent in 2018 will not be reached. Therefore, a new protocol will be negotiated for the period 2019 to 2021. For this protocol and the related ordinance a surplus norm has been established. Aruba should reduce the deficit to 0.5% in 2019, reach a surplus of 0.5% of GDP in 2020 and a 1% surplus in 2021.

SHEET 7 & 8

Now that I have briefly given some background information, I can continue with a further explanation of the supervisory boards and their tasks.

As I mentioned before, currently there are three boards of financial supervision:

- The board of financial supervision Curaçao and Sint Maarten, consisting of four members
- The board of financial supervision Bonaire, Saba and Saba with three members, and
- The board of financial supervision Aruba with three members.

All boards have the same chairman and a member on behalf of the country or public entity. The board members will act independently of the country which they are representing.

The boards are supported by one secretariat. Secretary is Manus Twisk. The Cft has offices in Curaçao, Aruba and Sint Maarten. In principle, the boards pay a visit to the countries and islands three times a year. The members live in the Netherlands, Curaçao, Sint Maarten, Aruba and Bonaire.

[SHEET 9/10/11 – pictures](#)

I hereby introduce you to the board members:

- For the Cft Curaçao and Sint Maarten, I am pleased to introduce the new member on behalf of Sint Maarten, mr. Russell Voges. He was appointed per October first and he succeeded Maria Plantz.
- Gregory Damoen is the member of the Cft on behalf of Curaçao.
- On behalf of the Netherlands is Henk Kamp, who succeeded Sybilla Dekker on July first.
- For the CAFT, Mrs. Hellen van der Wal is the member on behalf of Aruba, who succeeded Robert Croes in August.
- For the Cft BES is Herbert Domacasse the member on behalf of the public entities.

SHEET 12

An overview of the tasks of the Cft Curaçao and Sint Maarten is presented on this sheet. The Kingdom Council of Ministers is the “actual” supervisory body (or regulator), as the council is authorized to give an instruction and the Cft can advise the council here to. The Cft has a monitoring and signaling role and checks whether the budgets meet the standards in the applicable law. The Cft can provide solicited and unsolicited advice to the governments and the Kingdom council. We alter between the role of ruthless truth teller on the one hand and trusted advisor on the other. The countries must comply with the standards, and in principle the Cft does not have a say in the exact manner in which this is achieved. After all, the countries are autonomous and the Cft is not there to enforce local policy. However, the separation of these two roles can of course not be made so strictly. The Cft also wants to be a sparring partner for the countries, but cannot lose sight of our primary supervision role. Together with the countries and public entities we want to work towards sustainable government finances, it takes two to tango!

Importantly, the ultimate goal of financial management is an unqualified audit certificate on the annual report. There are large differences between the islands. Since 2014, Saba has had such an unqualified certificate. Last week an agreement was made that Curaçao will have such a certificate on the annual report of 2021. Currently, a roadmap towards such a goal is being drawn up. The coming days we will discuss this issue with Sint Maarten.

SHEET 13

The relationship structure is different when it comes to the public entities Bonaire, Statia and Saba. The state secretary of the ministry of

the interior and Kingdom relations is the main supervisor and is also the one who actually approves the budgets. The state secretary can intervene and use tools such as “voorafgaand toezicht” (meaning that no financial obligation can be made without pre-approval of checking the budget). Contrary to the supervision as laid down in the Act on supervision Curaçao and Sint Maarten, the supervision of public entities is not of a temporary nature.

SHEET 15

It is important to notice that the Cft supervises the entire budget cycle. During the entire process, the Cft issues solicited or unsolicited advice normally within two weeks. This cycle has the following steps. The budgeting process consists of a draft and a final budget and quarterly and annual reports. In February, May, August and November a quarterly report should be sent to the Cft. In practice most quarterly reports are on time, but this is unfortunately not the case for the budget in most countries. We believe that it is very important that the budget cycle should be managed in a strict and orderly manner because the annual report is a crucial building stone for the new budget.

SHEET 16/17

Which instruments is the Cft allowed to use? In the media it is frequently asked “why does the Cft not intervene?” Truth is the Cft can’t always intervene because the role of the Cft is strictly defined in the applicable laws and regulations. The starting point is the central budgeting standard.

For Curaçao and Sint Maarten the central norm is set in article 15 of Rft and for Aruba in article 14 of the LAft. For Curaçao and Sint Maarten the balanced budget principle applies along with an interest to income

ratio of five percent. At the current low interest rate, this interest norm is not effective. For Aruba the deficit and surplus rule applies.

The countries are required to submit the approved budget for an advice on the basis of Article 12. In its advice, the Cft must check the budget against the central norm.

This check or assessment also includes other aspects, namely:

- All expected expenses and income are posted in the budget and multi-year budget
- Income and expenses are properly explained
- The budget is set up in such a way that it meets the criteria of orderliness and controllability

In practice, we often see that the budget lacks sufficient and thorough explanation. This makes our assessment complicated.

Based on article 11, the Cft can also assess the draft budget. Normally we do this if we receive a request from the country.

SHEET 18

If the Cft is of the opinion that the adopted budget does not meet the standards of Article 15, the board can issue recommendations. The country will then be given the opportunity to still meet the central norm. However, if the country is not able to do so, the Cft can resort to advising the kingdom council into giving an instruction on the basis of article 13. For Sint Maarten, this occurred in 2015 and for Curaçao this occurred in 2012. As also the law states, it is an ultimate remedium.

SHEET 19

As indicated earlier, the Cft supervises the entire budgeting process. During the year the financial situation could worsen to such an extent that the Cft would proceed to make recommendations, this too may result in an advice to the kingdom council to give an instruction.

Article 14 of the Act on supervision, stipulates that the approved budget must be submitted by December 15th. If no budget has been received on that date and there is no indication that the (draft) budget will be sent within a reasonable period of time, the Cft can also advise to giving an instruction. This is called a procedural instruction, purely aimed at providing a budget. Such a discussion was held with Sint Maarten in December 2017. Finally, the government succeeding in drafting the revised budget, so that this procedural instruction was avoided.

SHEET 20

Hurricane Irma has had an immense impact on the population of Sint Maarten and had of course disastrous consequences for the economy and government finances of Sint Maarten. The reconstruction is ongoing and step by step work is being done to restore the country. Public finances are a central part of this. The Kingdom act for financial supervision provides for this exceptional circumstance in Article 25.

Based on this clause - the LAft and FinBES have a similar clause - Sint Maarten was allowed by the Kingdom council to present a deficit for 2017 and 2018. In the meantime, liquidity support is also being provided to Sint Maarten. The second installment has been paid out recently. Despite the difficult times Sint Maarten faces it is important to

have a properly and orderly budget cycle, especially in relation with the current liquidity support.

SHEET 21

The Cft is dependent on the information it receives from the countries in order to perform its tasks. The law also stipulates a requirement for the government to provide information to the Cft. This means that the Cft can request all information it deems necessary for the performance of its tasks and that the Cft must have access to all information carriers. In practice, we see that this article, article 8, sometimes presents us with challenges. I will explain more about this later. In addition, also other figures of institutions such as SZV or reports by in example the General Audit Chamber of Sint Maarten are important sources of information for the Cft.

SHEET 22/23

The aforementioned brings us to the question: What are the results of supervision till now? In general, I can say the following:

- The countries have made small steps towards a better budget discipline. I will come to this on the next sheet.
- Supervision has a positive effect on the public debate regarding government finances and has created more transparency.
- Quarterly reports and annual accounts are now being drawn up, submitted and approved.
- More confidence by international institution as the IMF or financial markets.
- The countries can make use of the Dutch subscription for capital expenditures' loans, which means that the governments can borrow at very low interest rates.

SHEET 24

Let us take a look at the debt to GDP ratio. Since 2010, in all countries we see an increasing debt to GDP ratio, although circumstances are different. For example, Curaçao did have a balanced budget in 2013 until 2016 but loans for the new hospital increased the debt. In 2017 there was a deficit also due to too much temporary measures in the past.

As you can see, Sint Maarten's debt to GDP ratio is rising above 45% of GDP if the planned loans regarding liquidity support and capital investment for 2018 and 2019 are included. Sint Maarten realized deficits in 2014 and 2015, which led to the instruction and the possibility for getting capital loans was postponed. The 2018 numbers also include the received liquidity support. In the future some surplus will be needed to cover this debt ratio and will discuss this issue with the government of Sint Maarten. Of course, this will not be something for the short term, but it is important to discuss this subject and next days we start this debate with the government of Sint Maarten.

Despite of several positive (sheet 23) effects, we do see a significant increase of the debt ratios, since ten/ ten/ ten. We must conclude that sustainable government finances are not yet reached. Important is the compensation of the deficit. It is good to see that in the Financial Recovery Plan this issue of "the compensation of the past deficits" was dealt with. Plans were drawn up to have a surplus starting 2021 as this is the only way to lower the GDP to debt ratio. As you know Aruba has a much higher debt to GDP ratio than Sint Maarten, so they must have a surplus perhaps for thirty years to go back to a sustainable level of debt.

SHEET 25

Let me pay more attention to Sint Maarten. Achieving a balanced budget is currently a huge challenge for Sint Maarten. Hurricane Irma has brought an increase in expenses and decrease in income, leading to additional deficits for an already weak financial structure. The right measures and priorities are needed in order for Sint Maarten to achieve surpluses in the future. For example, the compliance of taxes should be raised as it is very important that in these difficult times, everyone pays their fair share of taxes

As I have stated before, and I cannot stress this enough, a sound financial management is of great importance. Also for Sint Maarten, the target should be to obtain an unqualified audit certificate on the annual accounts in the coming years.

Lastly, but important as well I would like to emphasize the high priority for economic recovery. Together the government, business sector and residents must strive to work together to achieve this. Again, we have taken note of the Financial Recovery Plan presented by the government that should lead to financial and economic recovery. We applaud the attention for sustainable finance in that plan.

SHEET 26

In 2015 the first evaluation of the kingdom Act on supervision took place. This is a legally required evaluation. The committee specifically set up for this purpose, examined whether the countries complied with the legal standards for the last three years. Only then can the supervision be canceled. The committee's conclusion in 2015 was clear. None of the countries have met the standards for three years. Supervision therefore continues to exist. In this evaluation the committee made a number of recommendations:

- The governments should improve their 'own' institutions.
- Good financial management is a necessary precondition for orderly budget discipline.
- Arrangements should be made regarding the capital budget. With Curaçao we almost finalized these arrangements and with Sint Maarten we will do in the coming months.
- The countries should incorporate a debt ratio related rule in their own legislation

SHEET 27

The next evaluation takes place in 2018. Once again, a committee has been set up to evaluate whether the countries have met the standards in the past three years. It is expected that the committee will present its findings by the end of December.

- It is almost certain to say that the standards of the kingdom Act again have not been met and that supervision cannot yet be stopped: None of the countries have complied with the balanced budget rule over the past three years and therefore financial supervision has to remain in the near future

In addition:

- The Financial regulation for the BES will not be evaluated as this is not a temporary law
- For Aruba a new framework (protocol and ordinance) should be passed before January first.

SHEET 28

Some important steps towards sustainable government finances have been made, but we are not there yet and there is still a lot to do. There are, of course, several reasons for this. For example, the countries are

still young, the institutions are still under development, and getting the required talents is often a challenge. An important question, of course, is also the role of the supervisor. It takes two to tango ... As the presentation shows, our toolbox is not unlimited. There are some limits to what we can do in our role as supervisory boards. One could ask the question whether the law limits us too much.

This brings us to the following three discussion points:

- **First: What is a sustainable debt to GDP ratio and how could it best be included in the regulations under normal circumstances?**
With the IMF we believe that a debt to GDP ratio of approximately 40% is a sustainable debt ratio for these islands. Previously we have already advised to use a bandwidth of 5%. In line with the recommendations of the evaluation committee, it is good to have more attention to this debt to GDP ratio and ultimately have this incorporated in the regulations.
- **Second: Enforceable requirement to provide information;** I previously indicated that the government has an obligation to provide information to the Cft. However, we depend on the goodwill that we receive from the countries. If certain information is not provided, the Cft has no legal means to enforce this. This discussion took place with Curaçao. A stricter and enforceable obligation for the governments to provide information would contribute to the effectiveness of supervision from the Cft. We believe that the Cft should be able to advise the Kingdom council to give an 'administrative instruction' aimed at providing specific information. I certainly hope such an instruction will not be needed but it would be an effective tool.

- **Third:** the evaluation committee emphasized in 2015 that **sound financial management** is a necessary condition for an orderly budget process. Supervision of the progress in financial management is also an explicit part of the job description of the Cft. However, it is not an independent norm. Seeing the great importance of orderly financial management, the Cft is of the opinion that the introduction of standards that relate to financial management will contribute to the effectiveness of supervision. One could think of deadlines to obtain an unqualified auditor's report on annual report.

I have given you an overview of our supervision in the last 8 years. There are still many challenges ahead. It will be a long way to achieve sustainable government finances. Important is that we work together, also in the interest of the next generation. It takes two to Tango! Thank you for your attention.