



Sociaal Economische Raad  
Social Economic Council

## LETTER OF ADVICE

To the Prime Minister/Minister of General Affairs  
The Honorable Mrs. Silveria Jacobs  
Government administration building  
Soualiga Road # 1  
Philipsburg, Sint Maarten

Philipsburg, April 28<sup>th</sup>, 2020

Our reference: SER 2020/SA/19

Subject: Letter of Advice concerning the draft ordinance on Pension reform Civil Servants.  
In Dutch; Landsverordening, van de tot wijziging van de Pensioenlandsverordening overheidsdienaren, tot wijziging van de Landsverordening leeftijdsgrens ambtenaren, alsmede tot intrekking van de Duurtetoeslagregeling gepensioneerden 1943 (Landsverordening herzieningpensioen overheidsdienaren).

Honorable Prime Minister Jacobs,

The Social Economic Council (hereafter: SER) received the solicited advice request from your predecessor, the former Minister of General Affairs, Mrs. L. Marlin-Romeo, on July 23<sup>rd</sup>. 2019. In the advice request, the former Minister of General Affairs, mentioned that the draft National Ordinance on Civil Servants Pension was being handled in Parliament and that the Members of Parliament expressed the need for a social economic impact study on the pension reform. Unfortunately, at that time, the SER had a lack of capacity among its staff members.

The SER would like to re-emphasize that in accordance with its institutional role, it is essential that the SER renders its advice on all socio-economic topics prior to the Government submitting the legislation to the Parliament of Sint Maarten. The Council of Advice referred to the omission of the exclusion of the SER in the advisory process<sup>1</sup>. The SER refers to article 2 paragraph 1 of the National Ordinance of the SER<sup>2</sup>. The SER's contribution is most valuable in the dynamic process prior to draft legislation reaching the Parliament of Sint Maarten. During the process of amending the draft ordinance in question, this sequence was not upheld. Nevertheless, the SER welcomes the opportunity to contribute in its advisory role to the Government of Sint Maarten. Moreover, the SER acknowledges the pension reform concerns the relationship between the employer (the Government and other entities) and its employees. Taking into consideration that a relatively large group of employees' of the second pillar pension scheme will be affected, the SER recognizes that any changes to the system will have direct and indirect social and economic effects.

In its efforts to compile a comprehensive advice, the SER notes that, while compiling this advice the SER encountered a lack of essential local data. This is a recurrent issue that the SER has highlighted in various advices. Because of this repeated challenge, the SER compiled an advice on the importance of data<sup>3</sup>.

<sup>1</sup> RVA no. SM/03-18-LV dated May 25<sup>th</sup>, 2018, page 11.

<sup>2</sup> National Ordinance Social Economic Council AB 2010, GT no.19.

<sup>3</sup> See SER Advice "**DATA Matters: The value of data to sustainably transform our society**". October 2019.



The underlying advice request specifically requested the SER to perform a social economic study on the impact of the pension reform.

In this advice, the SER illustrates the impact of pension reform in general and the impact of the main proposed changes on various (macro-, meso-, and micro -) levels, based on the available data.

### Limitations

As a result of the restrictions due to the COVID-19 pandemic, the SER was limited in access to essential data for this advice. Also, certain specific data was not available. With insufficient local data, the SER researched the impact of pensions and pension reform in Canada, the USA and OECD countries as examples. When interpreting the examples provided in this advice, bear in mind that some of the aspects described in these countries, where it concerns retirement and retirement payments, are cushioned by more developed benefits- and social protection systems, which also contribute to the wellbeing of the retiree. Some of these additional benefits are not available on Sint Maarten.

### 1. Pension system reform in general

Overall, pension systems around the world are facing a similar challenge, there is strain put on existing guarantees for retirement mainly due to increases in life expectancy. Many countries are therefore considering pension reforms or have implemented reforms already. These reforms aim to support the lives of the elderly retiree, among others. Some reforms have an additional mandatory savings. These savings are usually termed Defined Contributions (DC) while employer-based pensions are termed as defined Benefits Plans (DB), funded by both employer and employee. Usually, governments are challenged with scarce resources which makes it crucial to anticipate the effects when (re)- designing pension plans to secure positive retirement outcomes. A good retirement payment provides a person with adequacy (a retiree's needs are provided for), is sustainable and is flexible (allows individuals to respond to life events).<sup>4</sup> Participation in pension schemes can be voluntary or mandatory. Many civil servants pension schemes are mandatory. Mandatory participation protects individuals from their own inability to save enough for retirement. Additionally, it allows for intergenerational risk sharing. This is ex-ante welfare enhancing as it allows shocks to be divided over a large group of subsequent generations<sup>5</sup>.

While this should be celebrated, the implications for the financial systems, designed to meet retirement needs but already under severe strain in many countries, must be considered.

There are varying formulas used to calculate members' entitlements such as final salary or average salary calculated over a certain number of years. Both methods, final salary and average salary are being implemented worldwide with average salary entitlements gaining prominence to guarantee sustainability. Career-average salary schemes could result in the amount of benefits that members could expect from their pension plans to be lower than in final salary schemes (for similar accrual rates), because salaries at the beginning of an individual's career are lower than the final salary. Sometimes salaries are not indexed to inflation and wage growth<sup>6</sup>. Additionally, changes in pension benefits in most countries are based on individual past salaries and salary increases and thus is dependent on individual choices or careers. As a result, there are varying groups among retiree's with varying levels of payments.

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<sup>4</sup> World Economic Forum. Investing in our Future.

<sup>5</sup> De Nederlandse Bank. DNB. working paper 2015.

<sup>6</sup> Pension Markets in focus.



For the pension fund with DB plans, changes in wages that deviate from what pension funds expected may lead to changes in the estimation of liabilities. Liabilities may therefore increase if wage growth was underestimated in previous calculations. Moreover, increases in life expectancy results in longer periods of benefit payments to retirees for DB pension funds from a defined retirement age, while inflation also impacts the calculations. The pension fund's obligation is to ensure that the fund is not underfunded.

In most countries, the funding ratios of DB plans are still below the pre-financial crisis level. When underfunded, employers may have to contribute more when assets do not cover liabilities arising from the pension guarantee. Other measures to protect funding ratios may be implemented as well. In the larger markets, a significant share of assets is in DB plans. While for some assets of DB plans kept growing, in OECD countries for example, they were not able to keep pace with the growth of liabilities. As a result, this led to a deterioration of funding levels in many countries. However, overall assets increased in OECD countries in 2017<sup>7</sup>. The SER focuses throughout this advice on the DB pension plan as the current system and proposed reform on Sint Maarten is a (DB) funded system.

## **2. Retirees income support the local community and economy**

Retirement payments represent a stable stream of income for the retiree. Retirees with stable, predictable income spend their pension income in their communities, supporting local businesses and economies. In the USA for example, the state of Illinois paid \$1.37 billion to retirees. The pension payment produced \$2.01 billion in total economic output, created over 14.000 jobs and over \$ 550 million in additional earnings. In Ontario, \$27 billion of all income is derived from DB pensions, which annually generates \$3 billion in federal and provincial income tax and \$2 billion in sales taxes<sup>8</sup>.

According to the 2018 Financial Statements of Algemeen Pensioenfonds Sint Maarten (hereafter: APS), APS has 2684 active participants, and 1122 retirement payment recipients. The APS fund has 30 participating employers. APS pays ANG 20 million per year in retirement payments to its retirees with the average payment per retiree being ANG 1.960 per month.

From the macroeconomic perspective, this is at least ANG 20 million per year that is injected into the economy, signifying the importance of APS and its participants to the economy of Sint Maarten. While the Gross Domestic Product (GDP) is ANG 1,815<sup>9</sup> million per year, of that amount, at least ANG 20 million is directly contributed to the economy by retirees alone. Furthermore, this reliable and predictable income also contributes to the economy in the months or years of slow economic activity, providing a constant stable flow to the economy. While the SER recognizes that the Sint Maarten's tourism product contributes a large share to the economy, with at least ANG 20 million paid to retirees (and dependents) alone, it accounts for a relatively significant structural contribution to the local economy. This contribution may be more obvious in the months of lower economic activity. Moreover, retirees account for 33.7% of the population<sup>10</sup>.

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<sup>7</sup> Ibid.

<sup>8</sup> Brown. Canadian Public Pension Leadership Council. The social implications of pensions. February 2019.

<sup>9</sup> GDP 2017 and 2018. CENTRALE BANK VAN CURAÇAO EN SINT MAARTEN Yearly Overview, Sint Maarten 2009-2018.

<sup>10</sup> Labour Force Survey 2018. Department of Statistics Sint Maarten.



## 2.1 Retirement payment at a Household level

Examining from a household level, when a household spends retirement payment, it represents an injection of income in the local economy that generates a chain of economic activities whose impact is greater than the original retirement payment. This multiplier effect can be significant where the spending of the retiree becomes the income of someone else, for example.

The retirement payment represents income that is redistributed into the local economy and impacts economic activities. The impact of the retirement income can be considered as the ability for the retiree to fulfill responsibilities such as grocery shopping, gasoline, house rent, spending on health, taxes and other fees etc.

Analyzing the latest Household Budget Survey<sup>11</sup>, the largest expenditure category is housing, water, electricity, gas and other fuels division with an expenditure of ANG 2,565.82 monthly per household, accounting for 37.4% of total expenditure. The second largest division is transport, accounting for 16% of total expenditure with an amount of ANG 1,096.11 monthly per household. In 2015, the two largest divisions, housing, water, electricity, gas and other fuels and transport, account for over half of total household expenditure<sup>12</sup>. The results also show that households spent ANG 6,106.00 on food and beverages annually, which on average, 17% is spent on bread and cereals, 15% is spent on meat, 12% on milk, cheese, eggs, water and soft drinks, and 11% on vegetables.

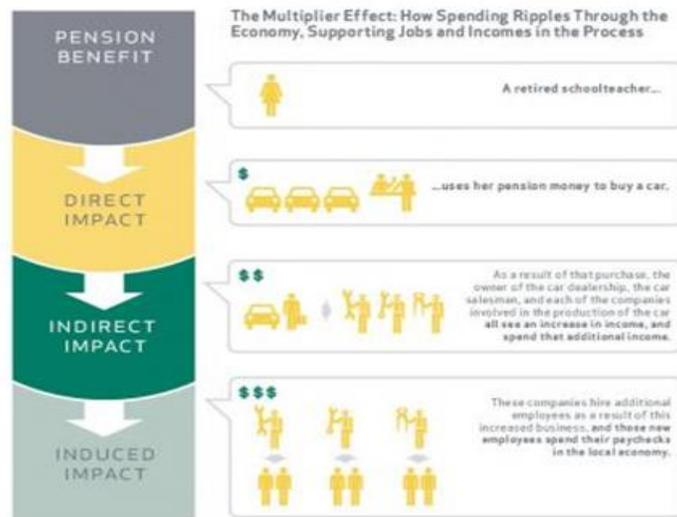


Figure 1: Pensionomics 2018. Measuring the Impact of DB Pension Expenditures

The third division, clothing and footwear with a total expenditure of ANG 55,309,342.79, and per household expenditure of ANG 3,950.67, accounting for 5% of all household expenditure on St. Maarten.

The above illustrates that not only is the retirees' income important for the economy, especially in specific sectors (food, housing, retail and transport), it is also important on an individual level for the independence and the overall survival of the retiree to maintain a level of quality of life.

<sup>11</sup> Household Budget Survey 2015. Total household expenditure: ANG 1,152,535,398.78

<sup>12</sup> Department of Statistics Sint Maarten. Accessible via [http://stat.gov.sx/press\\_release/Household\\_Budget\\_Survey/2017/HBS\\_Results.pdf](http://stat.gov.sx/press_release/Household_Budget_Survey/2017/HBS_Results.pdf)



## **2.2 Impact of DB plans in general on employee stress, health and productivity**

Compared to employees without a pension plan, employees are less stressed about their retirement income. In addition, after retirement retirees are less likely to seek other employment for financial reasons. However, employees would like to maintain their standard of living after retirement. Results of a Canadian survey for example, revealed that predictable, guaranteed income for a lifetime that keeps pace with inflation received 97 per cent support<sup>13</sup>. This is more achievable with a DB plan compared to any other pension arrangements. However, the concern of not having enough money after retirement causes stress for retirees. Financial stress can affect health and workplace productivity. Employees with financial challenges are more likely to be in poor health, higher stress levels, more absence and presenteeism compared to those financially unworried. This could lead employees to not being able to afford retirement. Research shows that in developed economies, more than 60 percent of employees financially struggling over 50 years, would like to retire but cannot. This results in the older employees expecting to work longer than desired. The DB pension plan design was one reason to compensate for these 'hidden pensioners'<sup>14</sup>. The SER learned that there are individuals that fall within this category on Sint Maarten<sup>15</sup>.

## **3. General summary of the Explanatory Memorandum**

The draft National Ordinance on Civil Servants' Pensions aims to adjust the current National Ordinance on Civil Servants Pensions (in Dutch: Pensioenlandsverordening overheidsdienaren 1943). The Explanatory Memorandum explains that the proposals were agreed upon between parties namely the Committee Civil Servants Union (CCSU) formerly known as the Georganiseerd Overleg in Ambtenarenzaken (GOA) the Civil Servants Union, representatives of the Ministry of General Affairs, the Ministry of Finance, the Ministry of Public Health (Department of Social Affairs), the General Pension Fund (APS) and an actuary. These agreements were laid down in the signed Pension Covenant<sup>16</sup>.

The introduction of the Explanatory Memorandum explains that the proposed changes to the existing civil servants pension ordinance are to achieve two goals:

1. The changes will reduce costs for the government.
2. The financial position of the pension fund is strengthened, sustainability is increased, and costs are better managed. This results in lower risks of governments finances.

The main proposed changes are:

- Retirement age increase to 65 (from 62)
- Average pay system (was final pay 70%)
- Conditional indexation (Coverage Ratio above 105%)
- Reduction in premium contribution to 18% (from 25%)
- Pensions accrual from age 18 (was 25)
- Recovery mechanisms for the fund
- One time increase of 10% of built up entitlements
- Conditional accrual amounts 2% per year (can be reduced to 1.75%)

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<sup>13</sup> Brown. Canadian Public Pension Leadership Council. The social implications of pensions. February 2019.

<sup>14</sup> Ibid.

<sup>15</sup> Meeting with APS. February 17<sup>th</sup>, 2020. Presentation from the Department of Personnel Affairs. March 12<sup>th</sup>, 2020.

<sup>16</sup> Pension Covenant was signed in January 2017.



- Abolishment of cost of living allowance (duurtetoeslag)
- No transitional arrangement (overgangsregeling)

Table 1. Overview main changes APS-participants/beneficiaries

Government/ APS pension fund	Beneficiaries/participants Current benefits	Beneficiaries/participants Proposed benefit changes
Cost reduction Government	Retirement 62	Retirement 65
Premium reduction from 25% to 18%	Final salary system 70%	Average salary system
Reduction of cost due to abolishment of cost of living allowance	Automatic indexation	Conditional indexation
APS	Premium 8%	8%
increase coverage ratio >100		
Recovery mechanisms	Cost of living allowance (duurtetoeslag)	Abolishment cost of living allowance. One time increase 10%
	Transitional arrangement (overgangsregeling) 60-62	No transitional arrangement (one-time option with penalty)
	Accrual rate 2%	Conditional Accrual 2%-1.75%

### **3.1 SER's general concerns and observations regarding the draft ordinance**

The SER observes that in general, as stated in the Explanatory Memorandum, the aim of the proposed reform is mainly focused on savings and cost reductions from the perspective of government, next to ensuring the sustainability of the fund. The SER acknowledges that any reform requires careful thought. Yet, the SER observed that the Explanatory Memorandum does not concretely incorporate the social and economic effect of the proposals, especially from the employee/retiree perspective.

From governments perspective, the Explanatory Memorandum explains that the government will save ANG 4.1 million per year in premiums alone compared to 9.2 million when keeping the pension scheme unreformed. Considering Sint Maarten's budgetary challenges, the SER understands that this amount of savings can be redirected to other government responsibilities and services. However, the Explanatory Memorandum does not indicate where these savings will be redirected. The large deficit financing needs will increase debt from relatively low levels to its peak of about 46½ percent of GDP in 2020<sup>17</sup>.

In total for government and the other public entities registered at the APS, the amount saved with the implementation of the proposed reform is ANG 17.4 million in the long-term<sup>18</sup>.

Below the SER will assess the main changes in the draft ordinance.

<sup>17</sup> International Monetary Fund. IMF Country Report No. 19/23. January 2019.

<sup>18</sup> Explanatory Memorandum.



### **3.1.1 Cost of living allowance**

The Cost of Living Allowance (COLA) (in Dutch: duurtetoeslag) is an amount paid as a supplement for the increase in cost of living. On Sint Maarten the COLA is paid by the employer, such as the government of Sint Maarten and the other employers participating in the APS pension fund<sup>19</sup>. The proposal in the draft ordinance is to abolish the cost of living allowance. Current retirees receiving COLA will continue to receive the COLA based on the old regulations. The eligibility of the COLA will be halted for those eligible, but not yet retired, with the implementation of the reform. Once the reform is implemented, they will receive a one-time 10% increase of built up entitlements. To be able to assess the impact of this measure, the SER refers to the Consumer Price Index (CPI) of Sint Maarten. The Press Release of November 28<sup>th</sup>, 2019 of the Department of Statistics, stated that, overall, prices were up from last quarter (0.35%) in 2019 and slightly up from the previous year (0.09%)<sup>20</sup>.

Based on the latest Household Budget Survey, four categories have the largest percentage weight (influence) of the total CPI: food and non-alcoholic beverages (7.2%), housing, water, electricity, gas and other fuels (36.1%), transport (14.6%) and miscellaneous goods and services (13.4%).

The increases were in the categories:

- Food and non-alcoholic beverages (+0.27%)
- Alcoholic beverages, tobacco and narcotics (+0.77%)
- Housing, water, electricity, gas and other fuels' (+0.49%)
- Furnishings, household equipment and maintenance' (+1.51%)
- Recreation and culture (+0.66%)
- Education (+0.51%)
- Miscellaneous goods and services (+1.10%).

Specifically, food and non-alcoholic beverages, the cost of the subcategory 'Food' increased by 0.48 percent. This was mainly due to the rise in the price of meat (+0.99%), vegetables (+1.15%) and food products n.e.c1 (+2.59%). Prices in the subcategory 'Non-alcoholic beverages' decreased by 0.9 percent. This was driven by a decrease (-1.12%) in the prices of coffee, tea and cocoa.

Furthermore, the Labor Force Survey (LFS)<sup>21</sup>, shows that there is a large group of persons unemployed as a result of Hurricane Irma<sup>22</sup>. Specifically, individuals with no income (21%) are from main age categories between 25-44 and 45-60. From a household level, this indicates that these individuals live in a household with at least one person with income. Considering that 33.7% of the population is retired, for some households, this could mean that a retiree may be the head of the household and living with other persons with no income.

<sup>19</sup> Financial Statement APS 2018.

<sup>20</sup> Department of Statistics Sint Maarten. November 28<sup>th</sup>, 2019. Press Release.

<sup>21</sup> Department of Statistics Sint Maarten. Labour Force Survey 2018.

<sup>22</sup> This will increase as a result of the measures due the pandemic related to COVID-19.



The APS pension plan which is payable from retirement for the rest of the individual's life, protects against market and longevity risk especially in economic downturns, while the indexation of benefits protects against inflation risk. The SER recognizes that the abolishment of the cost of living allowance constitutes a savings for the employer. However, the SER contends that by abolishing the cost of living allowance, which served to compensate the rise in prices of essential goods, will negatively impact the retiree's payment and the ability to meet their responsibilities. Moreover, the SER learned that the cost of living allowance can account for about a third of the retirement pay of the retiree.

### **3.1.2 Conditional indexation**

With the proposed reform, the indexation will be conditional. This condition is dependent on the financial position of the pension fund. A coverage ratio of at least 105% will allow the retirement payment to be indexed. The SER understands that the aim is to have the pension fund in a positive financial position and the reform aims to achieve that. The pension base is the individual's salary, however, the SER notes that there has been no indexation of government employee's salary since 2012. This already positions the pension base for the (active) participants and by extension the future retirement payment at a lower level than if indexed.

Moreover, the SER observes that there are no immediate measures set for the APS to undertake to ensure a quicker move toward a healthy financial position. In absence of immediate measures for the APS to undertake and in combination with the abolishment of the cost of living allowance, the retiree will be (immediately) negatively impacted. The current (active) participant may benefit in the future if and when indexation is possible. Although the active participant is contributing now, without a healthy financial position, there is no guarantee of retirement payment in the future. There is also no guarantee of the value of the retirement payment now compared to the future. This depends heavily on the current economic downturn due to COVID-19, and whether the value of the guilder will remain the same. This is highly dependent on the level of reserves of the Central Bank of Curacao and Sint Maarten (CBCS).

	Pension per year <sup>23</sup>	COLA per year
Person 1	7131.00	2076.00
Person 2	31104.00	11760.00
Person 3	42435.00	16200.00
Person 4	14244.00	2160.00
Person 5	42303.00	14904.00
Person 6	59559.00	15756.00
Person 7	36390.00	14604.00
Person 8	44754.00	13980.00
Person 9	69117.00	18096.00
Person 10	20643.00	4560.00
Person 11	21849.00	10908.00
Person 12	55209.00	18120.00

Table 2. Examples of retirement payment and COLA per year

<sup>23</sup> Information APS. Amounts in ANG.



### **3.1.3 Average-salary system**

The proposed reform will adjust the final-salary (70%) to an average- salary retirement payment. The retirement payment is dependent on the employee’s salary and career choices over the years. Referring to the salary income on Sint Maarten, most households earn under ANG 5.000,- .

While the SER acknowledges that there are a number of APS participants that may be in the higher salary scales, the SER deduces from the Labor Force Survey 2018<sup>24</sup> and information from APS that a majority of individuals are in the lower salary scales. Additionally, considering that not all civil servants are placed in the correct salary scale or remain in a (lower) salary scale for several years, it will impact the payment of retirement pay. Hence, the SER anticipates that the switch to average pay will have a negative impact, specifically for those persons in the lower salary scales. Moreover, for those employees taking longer to make a career move, the average- salary pay system negatively impacts them.

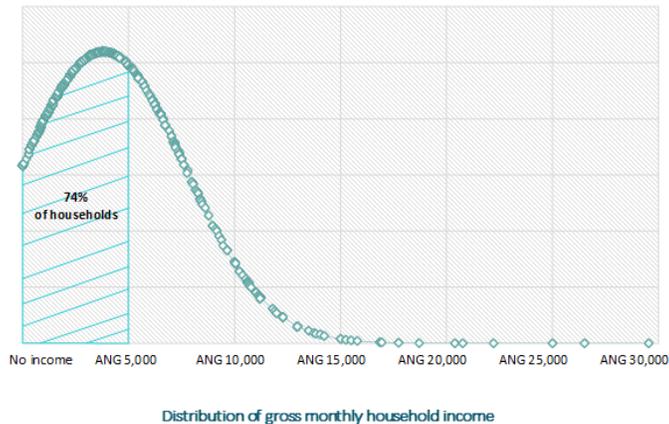


Figure 2. Department of Statistics Sint Maarten

Nevertheless, the SER acknowledges that maintaining the final-salary system is not sustainable in the long term while the average-salary mitigates undesirable effects ensuring sustainability and is built on solidarity.

### **3.1.4 Raise in retirement age to 65**

Globally, the retirement age is increasing and has a significant impact on pension funds, as a result of persons working longer and contributing to the fund thereby keeping the fund sustainable. The proposed reform proposes to increase the retirement age to 65. The SER sees this increase as logical as it falls in line with the expected age increase of the eligibility for AOV old age pension (see SER advice on increase on pension age).

In the draft national ordinance, there is the option to retire at 62, however this will cost the retiree a six per cent (6%) reduction per year if the retiree chooses early retirement. The SER recognizes that this measure is implemented to disincentivize the employee from early retirement and to compensate for payment for longer term (lifetime) payments. From the perspective of the impact on productivity, however, there is no guarantee that the senior employee is (still) productive between 62-65 years. This is especially concerning in absence of the flexibility of part- time work within governments’ current regulations.

<sup>24</sup> Department of Statistics Sint Maarten.



Moreover, the senior employee working longer may have a negative effect on labor mobility not allowing younger persons to gain employment or to move to another function within the civil service (with a higher salary). Additionally, considering the already low remigration rate of students (young professionals) returning to the island, this could negatively impact labor mobility. The SER refers to its Letter of Advice on Remigration<sup>25</sup>.

The SER would also like to highlight that while the maximum amount of working years (previously 35) is detached from the retirement age, the SER observes there is no consideration given in the draft ordinance for employees performing strenuous work. The employees of the Coast Guard are exempted and can retire based on the National Ordinance regulating the legal status of the Coast Guard<sup>26</sup>. Other employees performing strenuous work (physical as well as psychological) may not be able to work up to age 65.

Additionally, life expectancy on Sint Maarten is 78.5 years. Based on a retirement age of 65 translates into at least 13.5 years of retirement payments. However, due to the absence of major preventive health care efforts<sup>27</sup> and a high rate of non-communicable disease (NCDs) on the island, the SER points out that because of this it is currently uncertain if retirees are living longer. When using international mortality tables for calculations, this aspect must also be considered and placed in context of the actual local situation.

With the possibility of the accrual of pension from the age of 18, the SER recognizes this is one way to expand the participants base and a longer period for pension accrual. The SER is concerned that 18-year-old persons are not in school or not pursuing higher levels of education. The LFS 2018<sup>28</sup> reveals that of 15 to 25-year-old employed, 42% has completed secondary education and 19.9% has tertiary education, while 17.7 % work in as service or market sales workers. With this level of education, these are usually the lower paid jobs in the sector. The LFS 2018 additionally shows that of persons with a secondary education the majority is paid up to income categories ranging from ANG 1 - 2500,- , with the largest group earning between ANG 2000 -2500,-. This is compounded by the effects of Hurricane Irma where most reported loss of hours worked and thus loss of income. Consequently, if employed by an employer participating in the APS fund, starting at the age of 18 with secondary education, the accrued retirement payment will most likely be low.

Additionally, those employed from the age of 18 combined with the proposed retirement age of 65, will work for a total of 47 years. The Explanatory Memorandum further states that once the maximum pension is accrued, no premium is owed. This proposal from the standpoint of the SER, lacks the incentive for the employee to work longer than the accrual phase. Should the employee work longer than the accrual phase, this can have a negative impact on productivity as well as (psycho-) social wellbeing. The SER anticipates that participants will opt to exit the pension fund once this equilibrium is reached, thereby negatively impacting the funds' sustainability and consequently, the aim of this measure will be ineffective.

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<sup>25</sup> Letter of advice concerning remigration to Sint Maarten. June 8th, 2016.

<sup>26</sup> Landsverordening rechtpositie Kustwacht AB. 2013. GT no. 659.

<sup>27</sup> Preventive health care advice from SER is forthcoming.

<sup>28</sup> Labour Force Survey 2018. Department of Statistics Sint Maarten.



### **3.1.5 Transitional arrangement**

Currently there are different transitional arrangements over the various historical phases of pension adjustments (VUT, those registered before January 1<sup>st</sup>, 1998 and between 60-62). In the proposed reform, the transitional arrangement is abolished. There remains one option which is the choice to retire earlier, at the age of 62 years. This comes with a penalty of 6 per cent (6%) per year. Those eligible for early retirement based on the older regulations will receive a one-time ten per cent (10%) COLA increase. The SER observes there is no other justification for the 10% other than it is better for the fund<sup>29</sup>. Referring to what is already stated previously, the SER sees room for a more flexible system where it concerns early retirement, the transitional arrangement and the one-time 10% COLA increase.

Furthermore, analyzing the cash flow projections of the current regulation versus the proposed regulation under the assumption of average salary system, abolishment of COLA, and increased pension age to 65 shows a negative effect on the economy because of decreased retirement payment.

<b>Year</b>	<b>Current regulation</b>	<b>Proposed regulation</b>
<b>2020</b>	23.338.000	21.125.000
<b>2021</b>	25.415.000	20.893.000
<b>2022</b>	26.999.000	21.180.000
<b>2023</b>	28.514.000	23.133.000
<b>2024</b>	30.465.000	25.498.000
<b>2025</b>	32.555.000	27.292.000
<b>2026</b>	34.513.000	29.001.000
<b>2027</b>	36.213.000	31.183.000
<b>2028</b>	37.801.000	33.457.000
<b>2029</b>	39.443.000	35.535.000

Table 3. Ten-year cashflow projections<sup>30</sup>

Overall, this combination of abolishment of COLA, conditional indexation, average salary system, results in a net lower retirement income (combined with low AOV amount) for the (future) retiree. This has a negative effect on the retiree and by extension the economy and tax revenues as the retiree's disposable income and purchasing power is lowered.

<sup>29</sup> The SER learned this is agreed in the workgroup.

<sup>30</sup> Cashflow projections. Algemeen Pensioenfonds Sint Maarten (APS).



### **3.1.7 The APS**

Research shows that, in general, pension assets can have a positive effect on economic growth<sup>31</sup>. Pension plans provide an important source of reliable income. DB plans are a cost-effective way to provide secure lifetime income for the retiree and their beneficiaries after a lifetime of work.

In OECD countries for example, it was established that growth of funded pension systems has a positive effect on economic growth. In the USA, the economic gains are considerable. Nationwide, over \$1.2 trillion in total economic output resulted from DB pension expenditures in 2016<sup>32</sup>. Because pensions payment secure income to retirees, pensions provide local economies with stable sources of revenue. Retirees who spend their paychecks regularly in their local economies, especially during economic down times, provide a stable stream of revenue to local businesses and income for local employees. This illustrates that the presence of the APS pension fund provides a certain stability for the retiree as well as the local economy. Also, the presence of APS, can potentially contribute positively to economic growth. Research reveals for example that a 1% increase in pensions assets can contribute to economic growth by 0.14%<sup>33</sup>.

As mentioned earlier, the SER notes that the proposed measures mainly focus on changes for the active participant and the current retiree to ensure pension obligations are secured. Additionally, the aim of the reform is to ensure a positive coverage ratio of (at least) 105% for the APS pension fund. While the coverage ratio is determined by the APS's obligations and investments, there is no mention of alternative measures for the pension fund investments to immediately implement to ensure that this target is achieved at a quicker rate. The Financial Statements of the APS reveals that the fund has been underperforming since its inception in 2011<sup>34</sup>. The premium income was insufficient to cover the expenses. One reason for the insufficient premium income is that the government paid only 22% of premium income to APS instead of the legally required 25%. Of the 25% that must be contributed to the fund, the employee's contribution is 8%. In reality, the government paid 22% in premium while the employees share remained 8%. Based on the aforementioned, the SER would like to highlight the following.

Firstly, the government of Sint Maarten as the major contributor to the fund is part of the problem of the underfunding. The lack of living up to its legal obligation to the APS fund has resulted in insufficient premium income versus expenses over the years and has contributed to the fund not being financially sound. The APS has repeatedly reminded government in the past to pay its legal premium obligation including the retroactive payment of the premium difference owed (3%) to prevent solvency issues<sup>35</sup>. Based on a previous advice request in 2016, the SER extensively advised government not to legally decrease the pension premium to 22%<sup>36</sup>. Furthermore, in the 2018 Financial Statements of the APS, it is mentioned that government still had outstanding payments to APS, including advanced pension payments for former political authorities paid for by the Algemeen Pensioenfonds Curacao (APC)<sup>37</sup>.

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<sup>31</sup> Meeting held February 17<sup>th</sup>, 2020.

<sup>32</sup> Pension economics 2018. Measuring the Impact of DB Pension Expenditures.

<sup>33</sup> CPB Netherlands. Discussion Paper 279. Economic growth and funded pension systems.

<sup>34</sup> 2018 Financial Statements APS.

<sup>35</sup> See among others: Financial Statements of the APS of the years 2011, 2012, 2013 and 2014.

<sup>36</sup> Letter of advice concerning amendments from 25% to 22% to the "National Ordinance concerning Civil Service Pensions" [Pensioenlandsverordening Overheidsdienaren]. February 2016.

<sup>37</sup> 2018 Financial Statement APS, page 54.



Moreover, the SER notes that it is unclear whether the underperformance of the fund was solely due to government not living up to its legal obligation in the past.

Secondly, the SER would like to highlight that a coverage ratio of above 100% (105%) is not only dependent on 'obligations' but also dependent on 'investments' made by the APS. Investments are made to ensure that the fund earns additional income to cover its obligations in the long term. In 2018 the APS fund had a loss on investments made of ANG 37 million<sup>38</sup>. The SER points out that next to the 'recovery mechanisms' outlined in the draft ordinance, there are no other measures that the APS must immediately take to guarantee a better return on investment in the future. The 'recovery mechanisms' constitute drafting a plan within 5 years to ensure that the coverage ratio increases to above 100%. If the plan's measures do not remedy the coverage ratio in 5 years, then the pension payments to retirees will be reduced<sup>39</sup>. Further analysis of article I, under paragraph JJ, article 89a sub 4, provides various other options that APS management can use for the execution of recovery mechanisms, such as a one-time increase of extra pension contribution for the participants. However, the SER observes there is no specification if this contribution increase is equally shared between the employer and employee. The SER questions who bears the risk of the implementation of the 'recovery plan mechanisms'. The SER notes that combined with the other proposed measures, any increase in contribution for the active participant alone will translate into reduced benefit payment risk along with increased contribution risk for the active participants (employees). From a risk sharing perspective, these measures shift the risks mainly on the (active) participants of the fund, thereby making it seem as though the participants are exclusively responsible for the underperformance and recovery of the APS-fund.

Furthermore, the SER notes that next to the fact that a decision can be made to defer from investments as established in articles 15 and 16 of the National Ordinance of APS, there are no specifics about the nature of investments. While investments have a large role to play in maintaining an optimal coverage ratio. The SER recognizes this is also dependent on the now volatile international financial markets. However, the SER is of the opinion that the APS must immediately take steps to mitigate investment risks. This is also pointed out in the annual report of the General Audit Chamber where it is stated that 'the coverage rate at the end of 2018 is 97.6% (in 2017 it was: 103.1%). The assets are insufficient to cover both the general- and investment risks. The decrease in the coverage ratio is primarily due to the negative return on international investments. As a result, among others, the coverage ratio dropped by 5.5%'<sup>40</sup>.

The SER concurs that the Asset and Liability Management (ALM) study must be executed to ascertain if reform or adaptation measures should be carried out at the level of investment behavior as this also contributes to the long-term sustainability of the fund. Additionally, the SER observes that international investments account for 40% (and 60 % domestic)<sup>41</sup>. Considering the current volatile international financial markets as a result of the COVID-19 pandemic, and to reduce investment risks, the SER is of the opinion that article 16 sub 2 of the National Ordinance regulating APS should be used to regulate and make this international investment percentage more flexible.

<sup>38</sup> 2018 Financial Statement APS, page 62.

<sup>39</sup> Explanatory Memorandum under paragraph: 'Herstelmechanisme'.

<sup>40</sup> General Audit Chamber. Compliance Audit 2018 APS Financial Statements.

Accessible via: <http://www.arsxm.org/wp-content/uploads/2019/12/Jaarrekening-2018-APS-ENG.pdf>

<sup>41</sup> Algemeen Pensioenfonds Sint Maarten (APS). Accessible via: <https://www.apsxm.org/investments/>



In this way when the risks of international financial markets are too high, the 40% investment rate can be reduced accordingly. When international markets are more stable this can be increased up to 40% again. The SER sees this as another way to safeguard and prevent a drop-in coverage ratio and underperformance of the fund and the resulting negative consequences for the participants and retirees.

Thirdly, the premium decrease from 25% to 18% regards a decrease for the government as the employees still have to contribute 8% of their income (minus the AOV-Franchise). This is a benefit for the employer part of the premium and not the employees (active participants). Looking at the possibility to have the coverage ratio increase at a faster rate, the SER sees room for the premium to be set higher at 20% for example. This will still guarantee a reduction in cost for the employer while aiming to increase the probability of obtaining a coverage ratio above 100% or to 105% in combination with the other proposed measures, such as raise in retirement age and implementation of an average salary system. This will result in a more proportionate spread of the risks.

#### **4. The SER's additional observations**

The SER notes that the pension reform proposal in its current form puts great emphasis on government's savings and insufficiently considers the (potential negative) social and economic impact for active participants and retirees. The SER acknowledges that this requires careful thought and the development of consensus. However, while the SER recognizes the importance of reform for long term sustainability of the pension fund, the SER emphasizes that the reform must be fair and balanced. This means striking a balance between sustainability and the reality of the current employee, the future retiree and the pension fund. The Pension Covenant was signed in January 2017. Nevertheless, taking into account the recovery phase Sint Maarten is currently in, decisions must not only measure outcomes but must also consider unintended consequences, such as the economic impact after the passing of Hurricane Irma and the current COVID-19 crisis (such as reduced economic activity, loss of jobs rising prices of house rent, house maintenance, cost of living etc.) in addition to the social impact on an individual level. The objective should also aim at keeping retirees out of government assistance.

Furthermore, the SER recognizes that this group concerns a relatively large portion of employees with a second pillar pension. As such, the SER considers the pension reform as very crucial however, there are many concerns and (potential) negative impacts as a result of the proposals in the current draft ordinance. Combined with the advices and concerns already brought forward by the Council of Advice and the General Audit Chamber <sup>42</sup>, including concerns expressed by other stakeholders<sup>43</sup>, the SER is of the opinion that the reform proposal should be reassessed. The reassessment must also consider the cost of living on Sint Maarten, the economy, social aspects including the recovery and rebuilding phase that the country is currently in. The SER recognizes that this requires careful thought and the development of a new consensus. Based on the assessment of the SER and the concerns of all stakeholders involved, including the social and economic effects due to the hurricane and the COVID-19 crisis, the SER is of the opinion that the draft ordinance in its current form is not ready for decision making and must be reassessed.

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<sup>42</sup> The SER refers to the advice of the Council of Advice, and the General Audit Chamber.

<sup>43</sup> Meeting with CCSU representatives on February 7<sup>th</sup>, 2020.



## **5. Advice:**

Taking all the concerns from the key stakeholders involved into consideration, the majority of the SER advises the Government of Sint Maarten;

1. To implement the average pay system immediately in order to protect the sustainability of the APS pension funds
2. To establish the pensionable age as 65 years old for all beneficiaries of the APS pension funds without stipulations for early retirement
3. To reassess the other reform proposals in the draft ordinance
4. To revisit the reform in consideration of the local social and economic reality
5. To strive to achieve new consensus on key issues with the government employee representatives, thereby striking a new balance in the reform proposal
6. To review and implement the advice points in the SER advice titled 'DATA Matters', to establish the necessary DATA banks to substantiate legislative changes with large macroeconomic effect.

**Dissenting view of the minority:** Shirley Pantophlet-Gregoria, member of the WICLU-WIFOL

### **Burden of responsibility and early retirement**

The advice to Government to implement the average pay system immediately fails to take into account other mechanisms which could place the responsibility of payment on the employer (in this case the Government of Sint Maarten) rather than on the employee. Requesting the immediate implementation of the average pay system does not address the decided upon 18% salary contribution by employers instead of, for example, 20%, or the role of APS in making sound, sustainable investments. The negative impact on the retiree, as highlighted in the advice, remains unaddressed in advocating for the average pay system. Furthermore, while the retirement age for AOV is in the process of being raised to 65 years, advising against early optional retirement schemes (one- time option at 62) further compounds the highlighted negative impacts that may be experienced by retirees.

Should you require any additional information after reading the above, please feel free to contact us at your earliest convenience.

We trust to have sufficiently informed you herewith.

Respectfully,

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ir. Damien D.E Richardson  
Chairman

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Gerard M.C. Richardson  
Secretary-General

Cc: The Minister of Finance, the honorable A. Irion