Office Memorandum

August 18, 2014

To: Members of the Executive Board

From: The Acting Secretary

Subject: **Kingdom of the Netherlands—Curaçao and Sint Maarten—Deletion—Staff Report for the 2014 Article IV Consultation**

Attached for the **information** of Executive Directors is a deletion from SM/14/211 (7/14/14), which has been proposed by the authorities of the Kingdom of the Netherlands—Curaçao and Sint Maarten and agreed with the staff in accordance with the policy on publication of papers.

Premature Disclosure of Policy Intentions

Page 10, para. 20, second bullet, line 1: "see scope to increase revenue by introducing a property tax and a gaming tax and by further increasing certain excises (e.g., on tobacco and diesel) and fees. They" deleted

Questions may be referred to Mr. Lombardo, EUR (ext. 39937) and Mr. Quayyum, FIN (ext. 30578).

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities.

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FO/DIS/14/136

18. **Transparency and oversight of SOEs need to be improved and a clear dividend policy established.** There is an obvious tension between keeping state-owned enterprises (SOEs) at arm's-length, thus minimizing undue political interference, and ensuring that they maximize the interest of the public shareholder. Some SOEs have in practice soft budget constraints, and translate their accumulated inefficiencies and above-market wages into higher costs of doing business for the rest of the economy (e.g., Curaçao's Aqualectra). Even when they are profitable, in the absence of a solid governance framework, SOEs might gear their operations towards maximizing their own short-term profits, including by minimizing their contribution to the public budget (this is, for example, the case for Sint Maarten's airport and harbor companies). Therefore, the governance of SOEs must be improved, including—as a start—by ensuring the timely availability of reliable financial statements and establishing a clear dividend policy.

19. **A further shift from direct to indirect taxation in the medium term would be desirable.** To boost competitiveness, both countries should consider a further and gradual shift of taxes from income to consumption, along the lines of the 2009 FAD technical assistance, and replace the existing turnover tax—with its negative cascading effects—with a value-added tax (VAT). This has served well many other Caribbean countries.[5]

Authorities' Views

20. **Authorities in both countries agreed with the need to create fiscal buffers and strengthen their medium-term fiscal position:**

- In **Curaçao**, they emphasized that negotiations on pension reform with public sector unions are ongoing, and that they see scope for further expenditure savings.[6] They acknowledged that SOEs' continued financial woes, despite the greater and timelier pass-through of their input costs to retail prices, imply that more work is needed in this key area, which has important implications for the economy's overall efficiency and competitiveness.

- In **Sint Maarten** they ~~see scope to increase revenues by introducing a property tax and a gaming tax and by further increasing certain excises (e.g., on tobacco and diesel) and fees. They~~ intend to strengthen tax administration by deploying new IT systems and additional tax inspectors, and centralizing the tax office. They also expect to enhance administrative effectiveness (and generate some savings) by moving most government departments into the new building. Finally, they see merits in staff's suggestion to introduce a further gradual increase of the retirement age to 65 in the draft pension reform bill, and pledged to consider it carefully.

[5] Cebotari, Aliona, et al, 2013, "Enhancing Fiscal Revenue," in *The Eastern Caribbean Currency Union: Macroeconomics and Financial Systems*, ed. by Alfred Schipke, Aliona Cebotari, and Nita Thacker (International Monetary Fund).

[6] The authorities expect to save an additional NA.f 130 million by 2017 (about 2 percent of GDP) by cutting personnel expenses (by NA.f 50 million), expenditures on goods and services (by NA.f 50 million), and subsidies (by NA.f 30 million) through such measures as centralizing procurement of goods and moving different ministries to a central government office (to be built).