

COMPLIANCE AUDIT FINANCIAL STATEMENT 2022 OF APS



General Audit Chamber

Algemene Rekenkamer

September 2023



September 2023

General Audit Chamber, Juancho Yrausquin Bldv 10, Philipsburg, Sint Maarten

This document is the English translation of the original Dutch report entitled: "*Rechtmatigheidsonderzoek: Jaarrekening 2022 van het Algemeen Pensioenfonds Sint Maarten*". In the event of textual contradictions or other differences, the original Dutch text prevails.

PREFACE

This is the General Audit Chamber's report detailing the results of its review of the 2022 Financial Statements of the General Pension Fund Sint Maarten (APS).

In 2022, APS' coverage ratio decreased to 98.8% (2021: 104.1%). The Fund has recognized a loss of NAf 45 million for 2022. This is, of course, a negative development. The reduction is mainly due to the results achieved from international investments.

With the approval of the actuary, APS has increased the actuarial interest rate by 0.25% from 3.25% to 3.5%. As a rule, an increase of 0.25 percentage points means an increase in the coverage ratio of approximately 4.5 percentage points.

Because the coverage ratio was below 100% at the end of 2022, a recovery plan was drawn up in accordance with the law. This recovery plan indicates that no further measures are required to achieve a coverage ratio of at least 100% within the given timeframe.

Because the coverage ratio is below 105%, APS has been unable to provide indexation since the introduction of the pension reforms – as allowed by law. Moreover, based on the fund's performance, the pension accrual rate was already reduced from 2% to 1.75% as of January 1, 2021.

CONTENTS

PREFACE	
SUMMARY	1
RECOMMENDATIONS	2
1 OUR AUDIT	3
1.1 Basis for the Audit.....	3
1.2 The objective and audit questions.....	3
1.3 Methodology.....	3
1.4 Reading Guide	3
2 THE FINANCIAL STATEMENTS	4
2.1 Receivables	4
2.2 Pension Provision	4
2.2.1 Accuracy and comprehensiveness of participant records	4
2.3 Coverage Ratio	4
2.3.1 Actuarial Interest Rate.....	5
2.4 2022 Result.....	5
2.5 Return on Investment.....	5
2.6 Local Investments	6
2.6.1 Mary's Fancy.....	6
2.6.2 Parking Lot	6
2.6.3 Professional Office Park	6
2.6.4 Oryx Hills (Welgelegen)	7
2.7 Local Financing	7
2.7.1 Rainforest Adventures St. Maarten Loan.....	7
2.7.2 St. Maarten Investment Agency (SMIA)	7
2.8 Opinion of the 2022 Financial Statements	8
3. LEGAL COMPLIANCE	8
3.1 Legislation	8
3.2 Opinion on legal compliance.....	8

SUMMARY

In accordance with Article 26 of the [National Ordinance General Pension Fund Sint Maarten](#) we conduct an audit of the financial statement of APS. Annually, we send the audited financial statements and our comments to Parliament and the Minister of Finance, as stipulated in Article 18, tenth paragraph of the law.

APS's 2022 Financial Statements provide a true and fair representation of the size and composition of the Fund's assets as of December 31, 2022, and its result for 2022.

APS' coverage ratio at the end of 2022 is 98.8% (2021: 104.1%). This means the liabilities are not covered. Nor is there sufficient capital to cover the general and investment risks. In compliance with the law, APS commissioned a recovery plan in 2023. The plan states that the coverage ratio will be above 100% for five years, starting in 2023.

According to APS's underlying principles and on the advice of the consulting actuary, the [actuarial interest rate](#) was increased from 3.25% at the end of 2021 to 3.50% at the end of 2022. This increased the coverage ratio by 4.2 percentage points. Because of significant losses incurred on the international portfolio, the coverage ratio decreased by 10.3 percentage points.

The eco-hotel project at Mary's Fancy was started in 2019 but was suspended by 2022 due to increasing costs and operational problems. The Parking Lot project, secured in 2016, is currently not a top priority. The Professional Office Park encountered obstacles, including permitting and costs, prompting a revision of plans. Mortgage restrictions shifted Oryx Hills' housing strategy; the impact on earnings is unclear. APS financed Rainforest Adventures, which is now discussing restructuring, and the St. Maarten Investment Agency is facing financial challenges and a change in objective. Starting in 2023, the Curaçao Financial Group will oversee APS' local investments. This will impact SMIA's future costs and results. We may investigate SMIA more in-depth in the future.

RECOMMENDATIONS

- 1. Implement a recovery plan and improve monitoring:** APS's coverage ratio falling below the legally required minimum of 100% by the end of 2022 is a serious concern. We recommend strict implementation and close monitoring of the recovery plan to restore the minimum funding ratio of 100% and achieve the target coverage ratio of 105%. This includes implementing the recovery plan's recommendations and strategies and regular reporting on progress to relevant government agencies and stakeholders.
- 2. Review of real estate projects:** Considering the challenges numerous real estate projects face and their postponement, we strongly advise APS to reevaluate their feasibility. It is important to comprehensively analyze the economic feasibility, costs, and expected returns. Projects that are deemed to be infeasible may have to be discontinued to prevent any further financial losses.
- 3. Improve risk management of local investments:** Local investments should have a sharpened risk management strategy, including a thorough analysis of the financial health of external entities to which loans have been made, given the challenges related to non-performance and financing restructuring.
- 4. Ensure a complete board:** In 2022, the board of APS was not complete. Undertake action to fill the vacancies on the board, in accordance with Article 5, section 1 of the National Ordinance APS.

1 OUR AUDIT

1.1 Basis for the audit

We audit the APS in accordance with article 26 of the [National Ordinance General Pension Fund Sint Maarten](#) (hereinafter: Lv APS). Each year we send the audited financial statements and our comments to Parliament and the Minister of Finance pursuant to article 18, tenth paragraph of the Lv APS. This report contains the results of our examination of APS's 2022 Financial Statements.

1.2 The objective and audit questions

There are two objectives of this audit. To inform Parliament and the Minister of Finance of our opinion on the accuracy of the financial statements and legal compliance. In addition, we advise Parliament, the Minister of Finance, and the APS about ways to improve.

The following audit questions have been formulated:

1. Do APS' 2022 Financial Statements provide a true and fair representation of its financial position as of December 31, 2022, and its results for 2022?
2. Did the APS act in accordance with the National Ordinance APS in 2022?

1.3 Methodology

Based on our review, we have concluded that we can rely on the findings of APS's external auditor, who performed the audit of the 2022 Financial Statements. Furthermore, we gathered audit evidence. On this basis, we formed our opinion on the 2022 Financial Statements.

1.4 Reading Guide

This report addresses the following in order:

Chapter 2: Results on the financial position and performance of APS, including an analysis of local investments;

Chapter 3: Findings of our review of APS' legal and regulatory compliance;

2 THE FINANCIAL STATEMENTS

Here we present our findings and opinion on the question, "Do APS' 2022 Financial Statements provide a true and fair representation of its financial position as of December 31, 2022, and its results for 2022?"

2.1 Receivables

At the end of 2022, APS' receivable from the government is ANG 16.8 million (end 2021: ANG 14.8 million). In the auditor's report to the 2022 Financial Statements, APS' outstanding receivable from the government is no longer listed as a qualification. The Auditor stated the reasons for this are:

1. The government's recent payment behavior; and
2. the applicable materiality.

According to APS, no provision was made because there was no doubt about collectability.¹ An unqualified audit opinion was issued by the auditor.

2.2 Pension Provision

APS's actuary issued an actuarial opinion for fiscal year 2022 on May 25, 2023. His opinion on the pension provision (VPV) states:²

"The provision for pension liabilities, in accordance with the prescribed calculation methods and underlying principles, has been determined to be adequate, when taken as a whole."

At the end of 2022, the APS' VPV is ANG 829.4 million (2021: ANG 841.7 million). Total pension assets in 2022 are ANG 819.7 million (2021: ANG 876.5 million)³. The coverage ratio can be subsequently calculated by using the following formula:

$$\frac{\text{Pension Assets (ANG 819,732,000⁴)}}{\text{VPV (ANG 829,398,000)}} * 100 = \text{Coverage Ratio (98,8\%)}$$

2.2.1 Accuracy and comprehensiveness of participant records

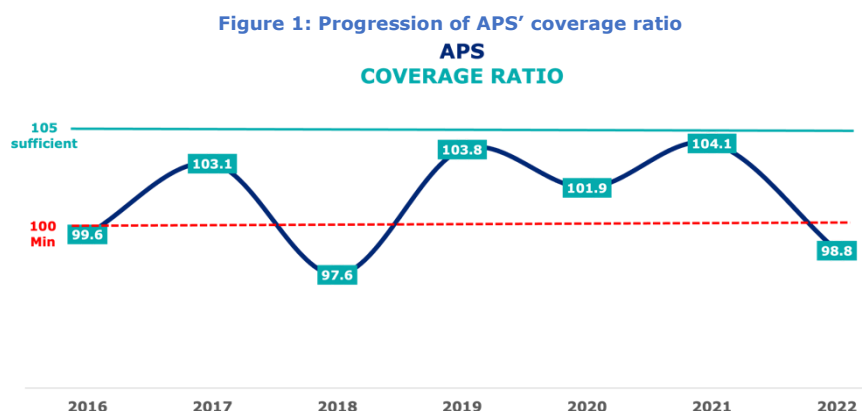
The auditor issued an unqualified audit opinion on the 2022 statement of basic data. According to the auditor, the premium analysis showed that only one participant still holds "Active" status while no premium was collected (2021: 40 cases). APS' external auditor certified⁵ that the statement of basic data used by the certifying actuary as of Dec. 31, 2022, was prepared in accordance with applicable criteria.⁶

2.3 Coverage Ratio

APS' set target is to attain a coverage ratio of 105%.⁷

At the end of 2022, APS's coverage ratio is 98.8% (2021: 104.1%). Figure 1 shows the progression of the coverage ratio.

The coverage ratio at the end of 2022 decreased by 5.3 percentage points compared to the previous year.



¹ Response management via email dated September 4, 2023.

² Certification Report Willis Towers Watson Fiscal Year 2022, Actuarial Statement, opinion on page 11.

³ Certification Report Willis Towers Watson Fiscal Year 2022, Key Figures, page 9.

⁴ According to page 20 of the 2022 Financial Statements, assets amount to ANG 819,935,000. According to the actuary's certification report (page 9), assets are ANG 819,732,000. A difference of ANG 203,000. When calculating the VPV, we used the figure from the actuary's certification report.

⁵ Participant's date of birth, former participant, pensioner, eligible partner, eligible orphans; gender, date of marriage/divorce, date of death, starting date of participation, date of retirement, income information (including salary; part-time percentage, disability percentage, income limits).

⁶ Grant Thornton Assurance-Report of the Independent Auditor on Basic Data dated May 31, 2023.

⁷ Page 29 APS 2022 Financial Statements.

Reasons include the negative result on international investments of -10.3%. The increase in the actuarial interest rate to 3.5% (2021: 3.25% increased the coverage ratio by 4.2 percentage points).⁸

A coverage ratio of 98.8% means that by the end of 2022, the available assets will not cover the pension liabilities. Moreover, the assets are insufficient to cover the general and investment risks. This implies that APS will be in a situation of coverage deficit at the end of 2022.⁹

2.3.1 Actuarial Interest Rate

APS promises pension payments to participants. But how does the APS know how much is needed to pay all pensions 20, 30, 40 years from now? For that, APS uses the actuarial interest rate. APS determines the actuarial interest rate based on internal policy.

Example:

Let's say you promise to pay someone ANG 100 after ten years. To fulfill your promise, you can deposit ANG 100 in a savings account today. The bank will give you interest annually, so you do not need to deposit the entire ANG 100 today. If the interest rate is 1%, you only need to deposit ANG 90.53 now. This deposit will grow with interest over ten years and become ANG 100. On the other hand, if the interest rate is 2%, you only need ANG 82.05 as a deposit today. The higher the interest rate, the lower the deposit you need to make today.

The actuarial interest rate increased from 3.25% to 3.5% as of December 31, 2022. An increase in the actuarial interest rate positively affects the coverage ratio. The actuarial interest rate works on a similar methodology for determining the provision that is currently required. The increase is based on internal policy reviewed by the actuary.

Recovery Plan:

The coverage ratio at the end of 2022 is 98.8%, below the minimum of 100%. Because the coverage ratio is below 100%, APS is required by law to prepare a recovery plan.¹⁰

The consulting actuary prepared the recovery plan on request of APS.¹¹ On July 2, 2023, the Board approved the recovery plan. The Minister of Finance, the Minister of General Affairs, and the Central Bank of Curaçao and Sint Maarten (hereinafter: CBCS) have given their approval to the recovery plan. The board adopted the plan on September 1, 2023.¹²

The plan comprises two forecasts of the coverage ratio that assess whether the minimum coverage ratio of 100% and the "targeted" coverage ratio of 105% will be achieved and the factors that may influence them. The estimates are made for five years (2023 to 2027). The recovery forecast is based on the financial position as of January 1, 2023, considering the yield assumptions provided in the ALM study.

Furthermore, one forecast predicts an increase in the actuarial interest rate for 2023 and 2024, while the other assumes a constant rate of 3.5%. According to both forecasts, the coverage ratio is expected to exceed 100% starting in 2023.

2.4 2022 Result

The Financial Statements for 2022 show an adverse result of ANG 44.5 million, which is a significant decrease from the positive ANG 19.8 million in 2021.¹³ The primary reason for the decline of ANG 64.3 million was due to lower returns on investments (ANG 126.3 million) and a drawdown of the Pension Provision (a benefit of ANG 63.7 million), because of the increase in the actuarial interest rate.

2.5 Return on Investment

The average return on all investments was negative over 2022.¹⁴ Compared to the previous year, the return of the international portfolio is lower¹⁵ and that of local investments is higher.¹⁶ The overall average negative return is -6.13% (2021: 7.26%) and is below the investment target of 5.5%. As a result of the ANG 88.7 million¹⁷ negative result due to investments and inflation, the coverage ratio decreased by 10.3%.¹⁸ Figure 2 depicts the return on investments as of 2011.

⁸ Certification Report Willis Towers Watson Fiscal Year 2022, Summary, Comments and Recommendations, page 6.

⁹ Idem, page 13.

¹⁰ Section 89a of the National Ordinance Revising Pension of Civil Servants.

¹¹ WTW, APS recovery plan 2023, June 30, 2023.

¹² Response management on the memorandum of findings, dated September 14th, 2023.

¹³ Paragraph 3.2 of the Financial Statement 2022 of APS.

¹⁴ Financial Statements 2022, *Financial highlights*, page 20.

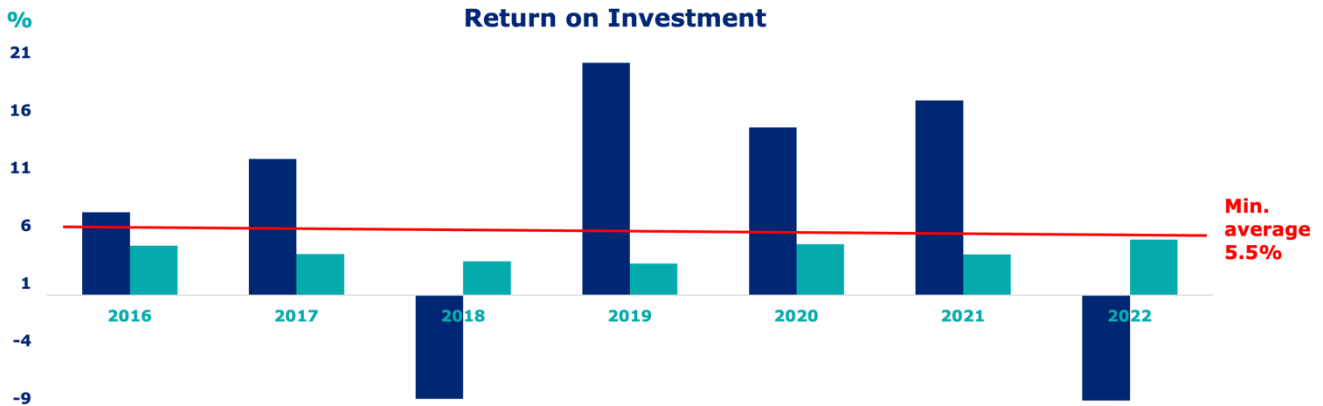
¹⁵ Yield international portfolio in 2022 -21.13% and in 2021 16.91%.

¹⁶ Yield local portfolio in 2022 4.84% and in 2021 3.54%.

¹⁷ Actuarial Advisory Report Reporting Year 2022 Willis Towers Watson, Financial Position, page 15.

¹⁸ Actuarial Advisory Report Reporting Year 2022 Willis Towers Watson, Financial Position, page 9.

Figure 2: Returns on the local and international portfolios



2.6 Local Investments

In our report on the APS's 2019 Financial Statements, we summarize the status of the development of local investments (then). In this report on APS's 2022 Financial Statements, we briefly update our findings.

2.6.1 Mary's Fancy

Since the acquisition in 2014, the investment objective has been to develop an eco-hotel. In 2019, APS received the necessary permits for demolition and (re)construction of the property. In the fourth quarter of 2020, construction was scheduled to start.¹⁹ The expected lead time is fifteen months.

In January 2021, APS applied for a building permit, for which it had not yet received approval as of the date of completion of the 2022 Financial Statements (June 2023).²⁰

In 2022, the Fund searched for a contractor and operator for the project, however in 2023, the project was suspended due to rising costs and challenges in identifying a suitable operator.²¹

2.6.2 Parking Lot

This property was acquired by APS in September 2016 as part of the debt settlement agreement with the government. The intention was to construct a multi-level parking facility with commercial uses on the ground floor near the government building. The expected completion date for this project was set for 2020.

APS reports that the development is a low priority compared to other projects.²²



2.6.3 Professional Office Park

In December 2016, APS acquired the "Professional Office Park", which included two commercial properties and an empty plot of land. The rental income from the properties contributes to the Fund's revenue. The vacant land will be utilized for various purposes, including the construction of the new APS office as part of a larger building. The decision to construct the new office has been in the works since 2016.

As of the end of 2022, the project encountered several major obstacles such as the absence of necessary permits, rising costs, and an oversupply of office space. These issues have led to unfavorable market conditions for commercial development. Consequently, the ongoing *design and build contract* has been put on hold. APS is currently reevaluating the project with a fresh proposal, critically assessing its feasibility and direction.²³

¹⁹ APS response dated July 21, 2020.

²⁰ Response management on the memorandum of findings, dated September 14th, 2023.

²¹ APS 2022 Financial Statements, pages 14 and 48: "Local investments, Mary's Fancy Plantation/De Castro Properties".

²² APS 2022 Financial Statements, pages 14 and 15 and 49: "Parking lot Development".

²³ APS 2022 Financial Statements, pages 14 and 48 "Professional Office Park".

2.6.4 Oryx Hills (Welgelegen)

The Oryx Hills project totals 62 homes.²⁴ The initial plan for APS was to promote affordable housing and provide full financing. However, due to several reasons, the plan was altered to offer homes through a lease-to-own arrangement, and financing would be obtained through a third-party lender, Banco di Caribe.

The decision to implement rent-to-own and leasing was driven by a shortage of mortgage-eligible participants. Without this change, the properties would have remained mostly vacant, negatively impacting the fund's returns. According to APS, at the end of 2022, a total of 44 homes have been rented out via lease or lease-to-own, 8 homes have been sold through a mortgage and 10 homes are vacant.²⁵

In response, APS notes:²⁶

"Under the current rules of the CBCS, APS may only provide mortgages for Oryx to participants of the fund and only through a commercial bank as administrator of the mortgages. As a result, the market for Oryx homes is and remains limited, while APS has to bear relatively high costs for the administrator. If APS had not introduced a Lease-to-own and Lease option, most of the 44 homes would still be vacant, while APS, regardless of vacancy, would have to pay high fixed costs for the administration of some mortgages. This would have a significant negative effect on the return of Oryx (Oryx would be loss-making) and the total return of APS".

The 2021 and 2022 Financial Statements do not provide a clear indication of how the changes in the business case will affect the projected profits.

2.7 Local Financing

In addition to developing property, APS has funded projects. However, this report highlights two of those; the Rainforest Adventures loan (RFA) and the St. Maarten Investment Agency Loan (SMIA).

2.7.1 Rainforest Adventures St. Maarten Loan

In May 2016, APS entered into a financing agreement with RFA.²⁷ In the 2021 Financial Statements, APS states that although the collateral's assessed value (market value) is higher than the book value of the loan, the Fund recorded an impairment of ANG 2.4 million because of RFA's *non-performance*. While the market and RFA performance improved in 2022, RFA still defaulted. Since then, the parties involved have started discussing restructuring the financing.²⁸

2.7.2 St. Maarten Investment Agency (SMIA)

On April 28, 2020, the SXM Investment Agency (SMIA) was established as a limited liability company (BV) and a subsidiary of APS. SMIA was the recipient of a loan from APS. By 2021, after performing an analysis, APS concluded that costs incurred during the preparation phase of SMIA's establishment (2018-28 April 2020) needed to be excluded from the loan. These charges were excluded from the SMIA loan and recorded as charges to the Fund. Because of the deteriorated economic situation in 2020-2021 (COVID-19 pandemic), SMIA did not generate the expected revenues, which required the Fund to cover additional operating expenditures for SMIA.²⁹

APS considers it unlikely that SMIA will repay the initial investment. Therefore, APS is considering a complete restructuring of the SMIA investment and has recorded the loan as a financing expense as of December 31, 2021. The loan has been fully written off (ANG 1.3 million).³⁰ The 2021 Financial Statements do not specify how this amount was spent, except that it is not considered an investment but an additional expense.³¹

According to the 2022 Financial Statements, the Fund plans to proceed with SMIA, but with some changes in its structure and objective. SMIA will handle APS' local portfolio. However, the initial financial evaluation reveals that SMIA, being a subsidiary, has negative equity, which means its value to APS' is zero. Notably, the 2022 Financial Statements of APS do not indicate the expenses incurred during the year.

²⁴ APS 2022 Financial Statements, page 49: "Oryx Investment Property" (Welgelegen)

²⁵ Response management on the memorandum of findings, dated September 14th, 2023.

²⁶ Idem.

²⁷ Senior Secured Term Loan Facility: loan term of 14 years (later extended by 8 months) at an interest rate of the 2016 LIBOR rate plus a margin of 5.25%, with a fixed minimum interest rate of 6%, 2020 Financial Statements, page 52.

²⁸ APS 2022 Financial Statements, page 15.

²⁹ APS 2021 Financial Statements, page 54.

³⁰ APS 2021 Financial Statements, page 64.

³¹ The APS management's response dated September 27, 2022, to the Memorandum of Findings states that the full impairment of the SMIA loan in 2021 is included as a business loan expense (ANG 1.3 million as part of investment costs).

In response, APS notes:³²

"In 2022, APS did not provide a loan and did not pay any capital to SMIA. In 2022, APS signed a Service Level Agreement (SLA) with SMIA regarding the acquisition of local investments for APS. The total costs that APS paid to SMIA per this SLA in 2022 are ANG 36,575. These costs have been booked as Investment Consultancy Expenses and have therefore been included in APS's 2022 local portfolio return."

On May 1, 2023, APS appointed Curaçao Financial Group (operating in Sint Maarten under the name: Sint Maarten Investment Company - SMIC) as fiduciary manager of the local investment portfolio.³³ The implications for SMIA, the costs incurred, and what SMIA in fact achieved for the participants are not clear to us. A more detailed analysis of SMIA and SMIC may be conducted at a later time.

2.8 Opinion of the 2022 Financial Statements

Based on our audit, we are of the opinion that APS' 2022 Financial Statements provide a true and fair representation of the size and composition of the Fund's assets as of December 31, 2022, and its year-end results.

We also note the following:

The government owed ANG 16.8 million in receivables at the end of 2022, with ANG 11.4 million of that amount being outstanding for over a year, according to APS records. As of 2023, ANG 2.8 million has been successfully settled.³⁴ An amount of ANG 8.6 million in old receivables remains outstanding, which we believe should have been recognized on the balance sheet as long-term receivables.

Of the ANG 8.6 million, ANG 6.0 million relates to the government, and ANG 2.6 million is owed by other employers. The APS has made no provision for bad debt. The explanatory notes for the balance sheet item "Receivables" in the 2022 Financial Statements do not provide information on the age of the receivables, the settlement in 2023, and why the APS chose not to make a provision.³⁵ For example, in our opinion (and that of the auditor), a downward adjustment in the valuation of receivables of approximately ANG 3 million should have been made.

3. LEGAL COMPLIANCE

In this chapter, we answer the following audit question, "Did the APS act in accordance with the National Ordinance APS in 2022?"

3.1 Legislation

In 2022, the APS met all the legal requirements of the Lv APS, except for Article 5, paragraph 1, which mandates that the Board must comprise a chairperson and four members. However, by the end of 2022, two positions on the Board remained vacant.

3.2 Opinion on legal compliance

Given the foregoing, we are of the opinion that the APS has complied with the legislative requirements in 2022, except for the items identified above.

³² Response management on the memorandum of findings, dated September 14th, 2023.

³³ <https://smn-news.com/index.php/st-maarten-st-martin-news/43281-aps-appoints-the-curaçao-financial-group-as-manager-local-investments.html>

³⁴ APS accounts receivable administration as of August 29, 2023.

³⁵ In a response dated September 4, 2023, the acting Director of APS states that no provision has been made because there are no doubts about the collectability.



General Audit Chamber

Algemene Rekenkamer