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Dutch influence on central banking in the Netherlands Antilles

I. INTRODUCTION AND SUMMARY

I gladly accepted the invitation to say a few words about the Dutch influence on central banking in the Netherlands Antilles. My working experience has been both in the Central Bank of the Netherlands in Amsterdam and in the Central Bank of the Netherlands Antilles in Curaçao, but I must acknowledge that this experience is divided unevenly: 24 years in Amsterdam and 1 year in Curaçao. Nevertheless I will do my best to deliver a balanced speech.

Almost all countries in the world have central banks. There are differences, however, both in the functions that these institutions perform and in their policy independence, especially with regard to their monetary policy. In my view these differences in policy independence are more interesting and relevant for the description of the character of a central bank than the differences in the extent of the functions that they perform.

Therefore I will pay more attention to features which are of relevance for the degree of independence than to the extent of the functions. This paper will deal with a number of interesting features of the Nederlandsche Bank (henceforth: "NB") and of the Bank van de Nederlandse Antillen (henceforth: "BNA"). The conclusion will be that there are rather strong similarities between both central banks, mainly because the legislature in the Netherlands Antilles took the Dutch Bank Act as an example for its own Bank Act. Further a comparison will be made between both central banks at one hand and a number of important

central banks at the other hand. Here the conclusion will be that both central banks have, in comparison with other central banks, a relatively high degree of independence. Finally the paper will enumerate the functions that both central banks perform, the conclusion being that both cover a relatively wide area.

II. LEGAL STRUCTURE AND CONFLICT RESOLUTION

II.1 General

It is widely acknowledged that central banks have a duty to conduct policy at least in consultation with the political authorities, but within that there are varying degrees of independence. Some central banks act merely as an agent of their Government, while others have a high degree of independence. The legal procedures for resolving conflicts between Governments and central banks are of great importance in this respect.

II.2 NB

The NB is a public limited company, whose shares have been held by the Government since 1948. This entails that the Bank's policy cannot be influenced by private interests. The Bank serves the public interest and hence has a public task. Yet the Bank is not a public institution in the narrow sense of a government institution. The Bank Act 1948 provides it with a large measure of independence.

Of great importance in this respect is the article that prescribes the procedure for the solution of a conflict between the Minister of Finance and the Bank. The Minister of Finance is responsible to Parliament for the fiscal and monetary policies. Pursuant to the Bank Act, however, the NB has its own task in the monetary field, which is to maintain the domestic and external purchasing power of the guilder. To ensure coordination of the Bank's monetary policy and the Government's monetary and financial policies, consultations are regularly held by the two monetary authorities, the Minister of Finance and the Bank's resident. The law stipulates how to end possible conflicts which cannot be solved in harmony. In such instances the Minister of Finance has the right to order the Bank to adjust its policy to the monetary and financial policies pursued by the Government. The Bank's Governing Board may appeal against such an order to the Crown, which must then decide whether the order should be followed. In the Netherlands constitutional situation this means that the Government must answer to Parliament for the decision taken. Parliament will either approve or disapprove the Minister's
directive to the Bank. If it approves, thereby taking the side of the Minister against the Bank, the Executive directors of the Bank and by all means the President, will resign. If, however, Parliament disapproves the Minister's directive, thereby taking the Bank's side against the Minister, then the Minister will have to resign. Evidently, the authority of the Minister to give a directive to the Bank entails a heavy procedure, which will only be applied as "ultimum remedium" in a serious conflict. At one hand this procedure was called into existence as a guarantee that the Bank is able to fulfil its statutory tasks in accordance with its own independent judgments. At the other hand the procedure guarantees that ultimately there is a democratic control on the actions of the bank. In practice the procedure has indeed proved to be an ultimum remedium. Since its introduction in the Bank Act 1948 consultations between the Minister of Finance and the Bank's President have always led to an agreement. A directive was never issued.

II.3 BNA

The BNA is a legal entity, called into existence by a National Ordinance (being the Antillean terminology for an Act), which lately has been amended in 1985. These amendments became effective in 1986. Basically BNA's position is equal to that of the NB. Its policy cannot be influenced by private interest, but serves the public interest and the legislature provides it with a large measure of independence.

The procedure laid down in the Act for the solution of a conflict between the Minister of Finance (or more in general: the Government) and the Bank is as follows: "General guidelines for the exercise of the management function can be given in a "Land Decree enacting general measures", after consultation with the management and the Supervisory Board of Directors".

The difference with the above-mentioned procedure in the Netherlands is, that the central bank has no right of appeal against "general measures" given by the Government. The similarity with that procedure is the public procedure. Those "general measures" have to be laid down in a "Land Decree", which is an official regulation that has to be published. The legislator has deliberately chosen for this public procedure in order to promote that the regular consultations between the Minister of Finance and the Central Bank will lead to a compromise. It can be expected that eventual "general measures", will be deemed to be of such a serious nature that they will lead to a discussion in Parliament, although they do not need the formal approval of Parliament. Thus the conclusion is that those "general measures" are an "ultimum remedium" for very serious conflicts. Up to now no "general measures" have been issued.
III. CENTRAL BANK BOARDS, COMPOSITION AND APPOINTMENTS

III. General

The composition and the terms of appointment of central bank boards can have an important influence on the nature of the relationship between central banks and governments. Both in the Netherlands and in the Netherlands Antilles there is basically a two tier structure, one level being decision making (executive) and the other being supervisory.

III.2 NB

The NB’s Executive Board is made up of a President, a Director Secretary and at least three and at most five Executive Directors. So the Executive Board consists of at least five and at most seven members. These are appointed for staggering periods of seven years. In practice Board members whose terms expire, have been reappointed and they usually do not leave the Bank before retirement age. In combination with the fact that many directors were appointed at a relatively young age, this resulted into stable compositions of the Board. For example: since the second world war the NB has been governed by not more than three Presidents. These long governing periods have without doubt strengthened their personal authority.

The Supervisory Board supervises how the Bank is managed and adopts the annual balance sheet and profit and loss account. The Government is represented in this Board by a Royal Commissioner. (Traditionally a professor in economics).

III.3 BNA

Although BNA appears to be oldest central bank in the western hemisphere -being established already in 1828- the Bank Act which has granted the Bank a relatively independent position vis-a-vis the Government is very young. It came into force in 1986.

One of the most important changes in the new Act was that the Bank received the authority to determine its own salary structure, which became independent from the Government's salary structure and rather competitive with that of the commercial banking sector. Needless to say that this measure has improved the average quality of the Bank's staff members.

Similar to the NB, the BNA has a Executive Board ("the Management") and a Supervisory Board. The Management consists of a President assisted by two
Executive Directors. The President is appointed for a period of six years. The other Executive Directors can be appointed for a specific or for an unspecified term. Unspecified means that the appointment will last apart from unforeseen circumstances, until retirement. The members of the Supervisory Board are Appointed for a period of 5 years. The Chairman of this Board is the Government Commissioner.

IV. STATUTORY OBJECTIVES

IV. General

According to an IMF-study\(^1\), generally speaking, central banks which have less formal policy independence tend to have objectives which are more broadly defined in their statutes, covering a range of macro economic goals or making general references to promote welfare. Banks with greater formal independence tend to have a statutory macro economic objective with a somewhat narrower focus, emphasizing stability in the domestic and also the external value of the currency.

IV.2 NB

The Bank Act 1948 stipulates that NB's main task is, to regulate the value of the Netherlands Monetary Unit in such a manner as will be most conducive to the nation's prosperity and welfare and in so doing keep the value as stable as possible.

IV.3 BNA

The Bank Act 1985 formulates the same task in less words: "BNA promotes the value of the monetary unit of the Netherlands Antilles".

IV.4 NB and BNA

Monetary stability is the main task for both central banks. In addition to this they are also entrusted with the issue of banknotes and the supervision of the banking and credit system. In comparison with those other central banks that

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\(^1\) IMF working paper "Central Bank Independence : issues and Experience" by Mark Swinburne and Marta Castello-Branco (June 1991)
have general welfare, economic development or growth etc., among their tasks, both central banks have a relatively narrow legal task.

V. LIMITS ON FINANCING OF GOVERNMENT

V.1 General

A potentially important facet of policy independence of central banks is the presence of legal constraints on their funding of the government.

V.2 NB

The legislation sets a strict, very low, limit on direct central bank credit to Government, but allows government paper to be bought by the central bank. In an agreement between the Minister of Finance and the central bank, it is laid down that when the Government is confronted with seasonal or incidental cash requirements, the central bank is prepared to buy government paper up to maximum of 3% of the Government's budget income in the previous year.

V.3 BNA

According to the legislation the BNA can grant advances to the Government in the case of temporary cash requirements with a seasonal character up to a maximum of 10% of the Government's budget income in the previous year. There is no obligation from the side of the Bank to buy Government paper. In practice the Bank has a rather limited portfolio which enables it to conclude open market transactions.

V.4 NB and BNA

A comparison between the Dutch and the Netherlands Antillean system leads to the conclusion that there are no differences of a principle character. There is a practical difference, however, as the maximum for Government funding is higher in the Netherlands Antilles than in the Netherlands.
I. COMPARISON WITH OTHER CENTRAL BANKS

After this description of some important characteristics of the BNA and the NB it may be interesting to see what their position is in comparison with other central banks. Any composition is somewhat arbitrary and in order to avoid a bias from my side concerning the position of the NB and the BNA, I will closely follow a study entitled "Policy and monetary institutions and public financial policies in the industrial countries", by Grill, Masciandaro and Tabellini\(^2\)). In this study, published in 1991, a comparison was made between 18 industrial countries. In a chapter on central banks a table was displayed on the political independence of central banks and an other one on the economic independence of central banks. For the purpose of this speech I deleted 12 of the original 18 countries, maintaining only the (economically) biggest three (U.S.A. Japan and Germany) and the three which are of special importance for this Caribbean conference (Spain, U.K. and the Netherlands). Further the Netherlands Antilles was inserted into the tables.

VI.1 Political independence

In the table on political independence 8 different features which contribute to independence are mentioned, whereby a cross indicates that the country in question possesses that feature.

These features are:

1. Governor not appointed by Government
2. Governor appointed for more than 5 years
3. All the Board not appointed by Government
4. Board appointed for more than 5 years
5. No mandatory participation of government representative in the Board
6. No government approval of monetary policy formulation is required
7. Statutory requirements that central bank pursues monetary stability among its goals
8. Legal provisions that strengthen the central bank's position in conflicts with the government are present

\(^2\) "Policy and monetary institutions and public financial policies in the industrial countries" by Grill, Masciandaro and Tabellini (1991)
This brings us to the following table

<table>
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<tr>
<th>Political independence of central banks</th>
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<td>Germ.</td>
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<td>1. Governor's app.</td>
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<td>2. Governor's term</td>
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<td>3. Board's app.</td>
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<td>4. Board's term</td>
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<td>5. No represent.</td>
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<td>6. No policy appr.</td>
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<td>7. Monet.Stabil.goal</td>
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<td>8. Prov.for conflict</td>
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<tr>
<td>Total score</td>
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From the total score at the bottom of the table it can be concluded that both the Netherlands at the Netherlands Antilles have high rankings in this table of political independence (together with Germany and the USA).

VI.2 Economic independence

In a similar way a table on economic independence has been construed, which is based on 7 different features. These features are:

1. No automatic credit facility to Government
2. Market interest rate on such facility
3. Temporary access to such facility
4. Limited amount for such facility
5. No central bank participation in primary market for public debt
6. Discount rate set by central bank
7. Banking supervision not entrusted to central bank or not entrusted to central bank alone

This leads to the following table
### Economic independence of central banks

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<th>Germ.</th>
<th>Japan</th>
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<th>Spain</th>
<th>UK</th>
<th>USA</th>
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<tbody>
<tr>
<td>1. Credit not Autom.</td>
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<td>2. Credit market rate</td>
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<td></td>
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<td>X</td>
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<td>3. Credit temporary</td>
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<td>4. Credit limited</td>
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<tr>
<td>6. Discount rate</td>
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<td>7. No banking superv</td>
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<td>Total score</td>
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<td>3</td>
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The conclusion is that, contrary to the first table, both the Netherlands and the Antilles have relatively low rankings. Again there are no substantial differences between these two countries. When we take the political and the economic features together the Netherlands and the Netherlands Antilles have a middle position between the central banks of Germany and USA which have a higher degree of independence and the other central banks which have a lower degree.

### VII. EXTENT OF THE FUNCTIONS

The following overview displays the similarities and the differences between both central banks.

### VII.1 Functions performed by both the BNA and the NB

- Management of the currency issue
- Monetary policy
- Bankers' bank
- Borrowing facilities for banks
  (Actual borrowing at BNA normally is zero)
- Participation in clearing and settlement systems
- Exchange rate policy
- Managing international reserves
- Supervision of banks
VII.2 Functions performed by the BNA but not by the NB

- Exchange control
  (The NB also performed this function until the abolition of exchange control in the Netherlands)
- Fiscal agent/management of domestic public debt
  (In the Netherlands this function is performed by a special agency of the Minister of Finance)
- Supervision of insurance companies and pension funds
  (In the Netherlands this function is performed by a separate legal entity)

VII.3 Function performed by the NB but not by the BNA

- Deposit insurance based on guarantees of commercial banks
  (In the Netherlands Antilles there is no deposit insurance)

VII.4 Functions performed by neither the BNA nor the NB

- Quasi-fiscal functions such as subsidization of specific sector's; equity participation in financial institutions, etc.

VII.5 Summary

Both central banks have a wide scope of functions. The similarities as shown under 7.1 and 7.4 are considerable more important than the differences as shown under 7.2 and 7.3.

VIII. CONCLUSION

With regard to both the legal position (esp. the degree of independence) and the extent of functions that they perform, there appears to be a strong similarity between the central bank of the Netherlands Antilles and the central bank of the Netherlands. This must be attributed to the Dutch influence in the Netherlands Antilles.