Operational and Financial Report 2013

December 2014

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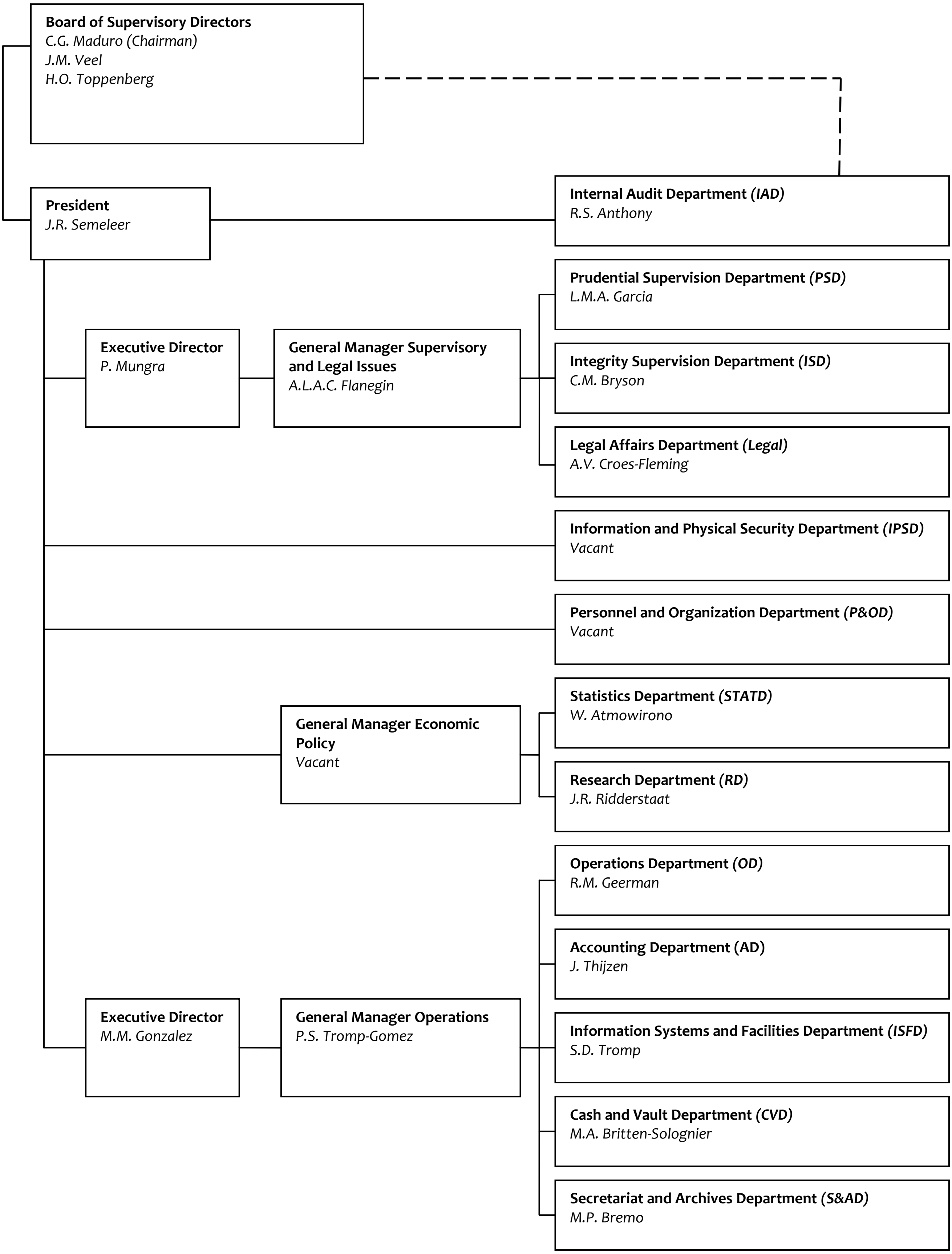
ORGANIZATION CHART

(As of December 1, 2014)



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List of abbreviations

Afl.	Aruban florin
AML/CFT	Anti-money laundering and combating financing of terrorism
ANG	Netherlands Antillean Guilder
APFA	Stichting Algemeen Pensioenfonds Aruba (the civil servants pension fund)
ATA	Aruba Tourism Authority
AVV	Aruba Vrijgestelde Vennootschap (Aruba exempt corporation)
AZV	Algemene Ziektekostenverzekering (the general health insurance)
BoSD	Board of Supervisory Directors
CBA	Centrale Bank van Aruba (the central bank of Aruba)
CBO	Central Bank Ordinance
CBCS	Central Bank of Curaçao and St. Maarten
CMO	Collateralized Mortgage Obligations
DNB	De Nederlandsche Bank N.V.
DNFBP	Designated Non-Financial Businesses and Professions
ECB	European Central Bank
ELMAR	N.V. ELMAR (the government-owned electricity provider)
ESCB	European System of Central Banks
FATF	Financial Action Task Force
FDA	Stichting Fondo Desaroyo Aruba (Foundation Development Fund Aruba)
GDP	Gross Domestic Product
MER	Mutual Evaluation Report
MPC	Monetary Policy Committee
MPI	Minted Photo Image
NDA	Non Disclosure Agreement
ONCS	OnNet Clearing System
RMC	Risk Management Committee
SETAR	Servicio di Telecomunicacion di Aruba (Setar) N.V. (the government-owned telecommunications company)
SIAD	Servicio di Impuesto y Aduana (Aruban Tax & Customs Authority)
SOFEC	State Ordinance Foreign Exchange Commission
SOFET	State Ordinance Foreign Exchange Transactions
SORUT	State Ordinance on the Obligation to Report Unusual Transactions
SOSCS	State Ordinance on the Supervision of the Credit System
SOSIB	State Ordinance on the Supervision of the Insurance Business
SVB	Sociale Verzekeringsbank
U.S.	United States
WEB	Water en Energie Bedrijf Aruba N.V. (the government-owned water and power company)

1 POLICY OBJECTIVES

The Centrale Bank van Aruba (CBA) has a *sui generis* legal status and pursues a number of policy objectives arising from the statutory tasks assigned to it in the Central Bank Ordinance (CBO) (AB 1991, no. GT 32) and other legislation. Achieving these objectives is a fundamental condition for sound economic and financial development. CBA's principal policy objectives are to:

- **Maintain public confidence in the Aruban florin**

The CBA conducts monetary policy to protect the stability of the value of the Aruban florin through the preservation of its fixed exchange rate vis-à-vis the U.S. dollar. To this end, an adequate level of international reserves is maintained at all times.

- **Contribute to financial stability**

The CBO also assigns the CBA the responsibility to promote the stability and integrity of the financial system. The supervisory-related activities are carried out mainly via ongoing off-site surveillance and periodic risk-based on-site examinations to assess soundness of the supervised institutions and/or their compliance with relevant laws and regulations.

- **Ensure smooth circulation of the Aruban florin**

The CBA is the sole issuer of florin bank notes. In accordance with the CBO, the CBA is responsible for the design and printing of secure and safe bank notes. The CBA withdraws from circulation and destroys damaged or worn florin bills. Furthermore, it contributes to an efficient domestic payment system by managing the OnNet Clearing System (ONCS).

In line with its policy objectives, the CBA performs the following tasks and related activities :

Tasks	Related activities
a. Conduct monetary policy.	Formulate and implement measures to, inter alia, maintain the adequacy of the international reserves.
b. Supervise the financial system.	Perform risk-based supervision of financial institutions to protect the interests of depositors and policy-holders and promote the stability and integrity of the supervised sectors.
c. Issue florin bank notes.	Bring safe and secure bank notes into circulation to meet the needs of the public.
d. Issue coins on behalf of the government.	Bring safe and secure coins into circulation to meet the needs of the public.
e. Promote efficiency in settling domestic payments.	Operate an automated clearing system between the CBA, commercial banks, and a number of government-related institutions.
f. Act as the banker for the government.	Execute payment orders and intermediate in the issuance of government debt paper.

Tasks	Related activities
g. Regulate the flow of international payments.	Regulate payments between residents and nonresidents and collect foreign exchange commission on behalf of the government.
h. Manage Aruba's official reserves, consisting of gold and foreign currency holdings.	Invest CBA's foreign currency reserves in accordance with prudent guidelines, aimed at preserving these reserves and thus confidence in the Aruban florin peg with the U.S. dollar.
i. Advise the Minister of Finance on financial matters.	Produce relevant macroeconomic, financial, and monetary analysis and provide expert policy advice.
j. Monitor economic and financial developments.	Collect and analyze financial and economic data for the purpose of monitoring, policymaking, and dissemination through the publication of regular reports, as well as by giving presentations.

2 A QUICK LOOK AT THE YEAR 2013

- In conducting monetary policy, the CBA applies the reserve requirement as its main instrument. During 2013, the reserve requirement rate was maintained at 11 percent, while the advance rate was kept at 1 percent. Although a downward trend had been observed, the international reserves remained adequate when benchmarked against Gross Domestic Product (GDP), the money supply, and, most importantly, the current account payments, supportive of the fixed exchange rate regime of the Aruban florin with the US dollar and the resulting relative price stability objective. Consequently, the legal interest rate, which equals the advance rate plus two percentage points, was also kept unchanged at 3 percent. The legal interest rate is the interest rate that can be charged in case of default of payment. However, parties are free to enter into a contract in which the penalty fee in case of default of payment could deviate from the legal interest rate.

- During 2013, further strengthening of the regulatory framework of the CBA continued. As of January 1, 2013, the scope of the State Ordinance on the Supervision of the Credit System (SOSCS) was broadened to include, among others, electronic money institutions, while that of the State Ordinance on the Supervision of Trust Service Providers (SOSTSP) was widened to include trust companies providing trust services to local companies. Moreover, all sectoral supervisory laws were amended to enhance the possibilities for cooperation and information exchange with foreign supervisors and to harmonize and strengthen the requirements in the sectoral supervisory laws with regard to fit and proper testing. In addition, a uniform requirement in the area of sound and controlled business operations was introduced in all sectoral supervisory laws.

- For 2013, the 12-month average of the consumer price index reached -2.4 percent, down from 0.6 percent in 2012. This development was induced by the reductions of water and electricity tariffs in August and November 2012, respectively, which continued to impact the CPI in 2013.

Financial highlights for 2013

- At year-end 2013, CBA's total assets amounted to Afl. 1,213.5 million, i.e. Afl. 215.7 million or 15.1 percent lower when compared to year-end 2012. This decrease was due to an Afl. 124.4 million (11.5 percent) drop in the foreign currency assets of the CBA and an Afl. 92.1 million (27.8 percent) decline in the value of its gold holdings. The decrease in the foreign currency assets was mainly related to a decline in the value of the investment portfolios, largely caused by a sudden rise in the demand for foreign currency by the commercial banks in particular as well as the restructuring of the investment portfolios. The aim of the latter was to reduce interest rate risk. Furthermore, the market value of the gold holdings of the CBA dropped by USD 462.50 (Afl. 827.87) per troy ounce or 27.8 percent at the end of 2013, thereby causing a decline in the CBA's gold holdings at year-end 2013, which in turn negatively impacted the revaluation account on the liability side of the balance sheet of the CBA.

- On the liability side, the deposits of residents decreased by Afl. 86.9 million (9.8 percent) in 2013, largely the result of the purchase of foreign currency by the commercial banks, which was partially offset by an increase in the government's deposits. The aforementioned rise stems from the loan proceeds received by the government in 2013 in the amount of Afl. 285.5 million, which were partially offset by payments to abroad mostly related to repayment of principal and interest on maturing foreign loans.

- Total gross income (net of interest expenses) decreased in 2013 by Afl. 2.1 million or 9.1 percent to Afl. 20.6 million (December 2012: Afl. 22.6 million). This decrease was associated mainly with a drop in net interest revenues of Afl. 3.8 million or 23.7 percent resulting from lower foreign investment revenues. However, these lower foreign investment revenues were offset by increased foreign exchange revenues following the receipt of the funds related to the aforementioned bond issue on the international capital market by the government of Aruba. Furthermore, various other revenues surged during 2013, mainly attributed to incidental revenues stemming from administrative fines imposed by the CBA on several supervised institutions.

- Total expenses went up by 0.2 percent or Afl. 44.2 thousand to Afl. 18.9 million at end-2013 (December 2012: Afl. 18.9 million), mostly owed to an increase of Afl. 237.5 thousand (17.1 percent) in depreciation expenses and an Afl. 206.9 thousand (60.5 percent) surge in amortization costs of banknotes. On the other hand, personnel expenses went down by Afl. 442 thousand (-3.4 percent), attributable to lower pension contributions in 2013 based on new actuarial calculations.

- At end-2013, net profit amounted to Afl. 1.6 million, i.e., Afl. 2.1 million or 56.2 percent lower than in 2012. This reduction in the net profit was caused mainly by a decline in foreign currency investment revenue.

3 THE BUSINESS OF THE CBA

3.1 Domestic payment system

3.1.1 Currency operations

The CBA has the sole mandate to issue bank notes and coins in Aruba. In carrying out this mandate, the CBA determines the quantity, denomination, substrate, and characteristics of the notes and coins. With respect to the issuing of coins, the CBA executes this task on behalf of the Minister of Finance. The CBA provides bank notes and coins to the commercial banks, which in turn meet the public's demand for currency. The CBA redeems surplus bank notes from commercial banks and withdraws them from circulation. The CBA processes the redeemed notes, destroying the unfit ones via an environmentally friendly bank note destruction machine. The aim of the CBA is to have only high quality bank notes in circulation.

Bank notes in circulation

Table 3.1 provides an overview of the bank notes in circulation per denomination. As can be derived from this table, the total amount of bank notes brought into circulation has increased by 4.9 percent in 2013 compared to 2012. Consequently, the total value of bank notes in circulation experienced a growth, increasing by 5.6 percent compared to a year earlier to Afl. 237.7 million at the end of 2013. Despite the widespread use of payment cards, including debit and credit cards, and electronic payments through online banking, the use of florin bank notes to make payments continued to grow in 2013. The Afl. 100 denomination still represents the largest share of all bank notes issued, comprising 47.5 percent of the total bank notes in circulation, while the Afl. 500 bank note remained underused. The Afl. 5 bank note was replaced by a Afl. 5 coin in 1996.

Table 3.1: Bank notes in circulation (in numbers)

Denomination	2009	2010	2011	2012	2013
500	11,424	10,521	10,130	10,157	9,391
100	1,554,223	1,536,933	1,595,866	1,766,549	1,881,641
50	316,754	309,424	301,808	341,701	350,926
25	635,320	618,046	632,727	701,902	734,241
10	692,393	703,778	754,701	774,928	805,516
5	176,768	176,555	176,424	176,338	176,318
Total	**3,386,882**	**3,355,257**	**3,471,656**	**3,771,575**	**3,958,033**

Source: CBA.

As also shown in chart 3.1, the 100 florin bill remained by far the most commonly used denomination.

Chart 3.1: Bank notes in circulation by denomination

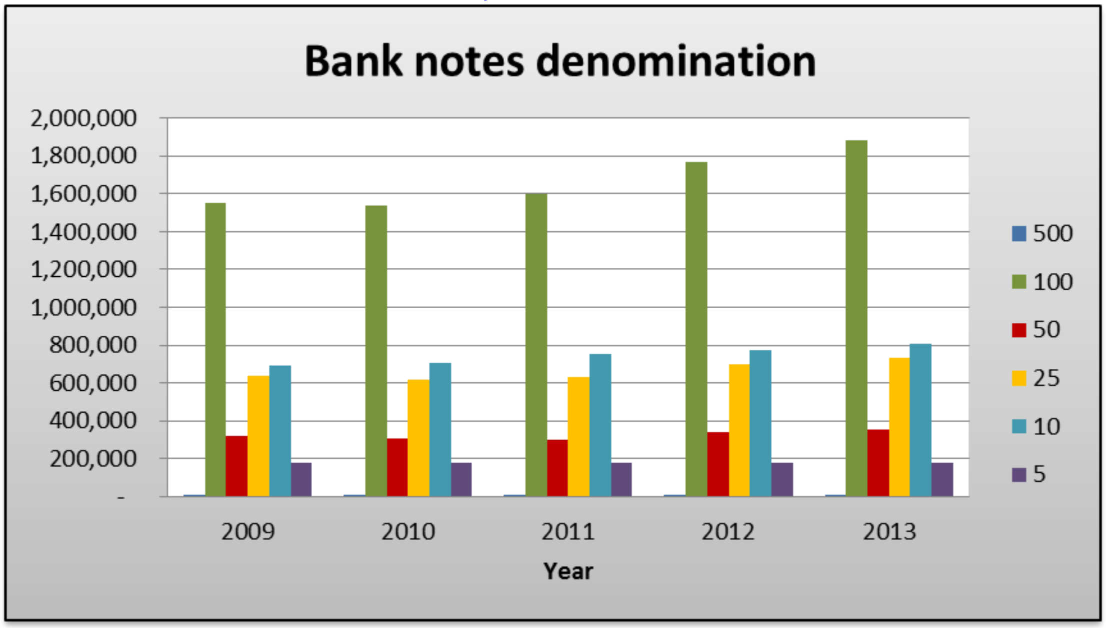


Chart 3.1: The Afl. 100 denomination continues to be the most used bank note.

Counterfeit florin bank notes

The number of counterfeit florin bank notes has been quite low over the years. The CBA provides extensive information on its website, and via the commercial banks through brochures, to assist the public in verifying the authenticity of the florin bank notes. Nonetheless, in 2013, a few cases of counterfeit florin bank notes were registered. The CBA then immediately initiated a media campaign to remind the public of the security features of the florin bank notes to counteract the circulation of counterfeit bank notes.

Coins in circulation

The CBA is also entrusted with issuing coins on behalf of the government. The total value of coins in circulation in 2013, excluding commemorative coins, increased by Afl. 1.5 million (5.2%) to Afl. 30.2 million (2012: Afl. 28.7 million). As depicted in Table 3.2, the two smallest coin denominations, the 5 and 10 cent coins, are the largest in circulation, followed closely by the 25 cent coin.

Table 3.2: Coins in circulation (in number)
(in thousands)

Denomination	2009	2010	2011	2012	2013
5.00	1,587	1,633	1,739	1,787	1,873
2.50	81	84	91	92	94
1.00	7,909	8,269	8,675	9,104	9,586
0.50	6,187	6,559	6,928	7,141	7,605
0.25	11,946	12,576	13,286	14,231	14,979
0.10	18,825	19,822	20,925	21,733	23,138
0.05	19,080	19,957	21,108	22,450	23,313
Total	**65,615**	**68,900**	**72,752**	**76,538**	**80,588**

Source: CBA

Chart 3.2 illustrates graphically the number of coins in circulation by denomination.

Chart 3.2: Coins in circulation by denomination

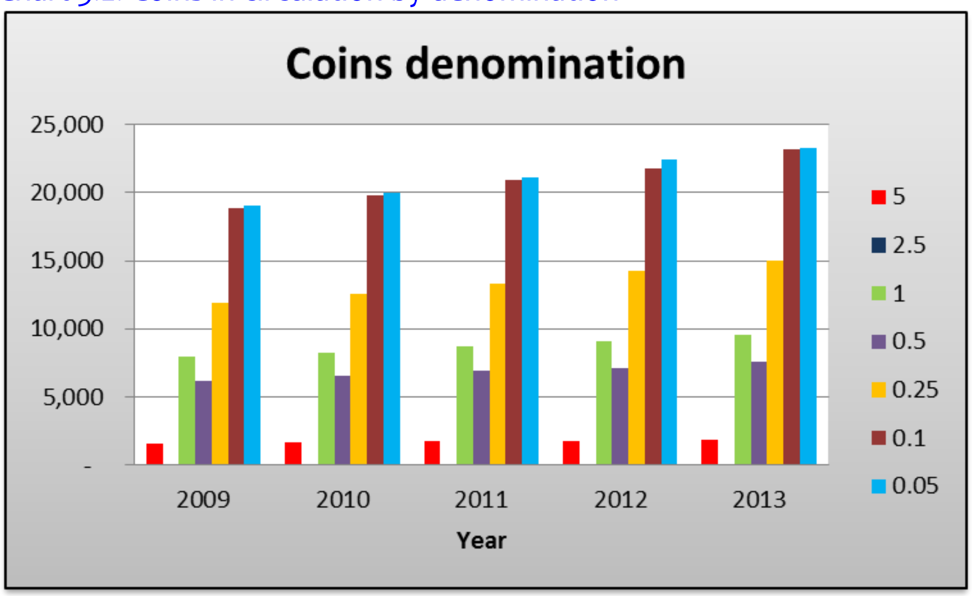


Chart 3.2: The 5 cent and 10 cent denominations remain the most used coins.

Commemorative coins

In 2013, on behalf of the government, the CBA issued two silver commemorative proof quality coins with a nominal face value of Afl. 5, one gold commemorative proof quality coin with a nominal face value of Afl. 10 and one special edition Afl. 5 circulation coin (in color). The Afl. 5 special edition circulation coin (in color) was issued to commemorate the announcement of the abdication of Queen Beatrix, containing a double portrait of Prince Willem Alexander and Queen Beatrix. The gold and one silver commemorative coin were issued to commemorate the change in throne, whereby Prince Willem Alexander was crowned as the new King of the Dutch Kingdom. The other silver commemorative coin was issued on the occasion of the first official visit of King Willem Alexander and Queen Maxima.

Coin sets

The 2013 coin set carried the theme 'Flowers of Aruba' to illustrate that despite its dry climate, various types of beautiful flowers grow in Aruba. A distinguishing feature is the striking difference between flowers and plants that grow during the rainy season, from October to December, and those that grow during the dry season, from January to September.

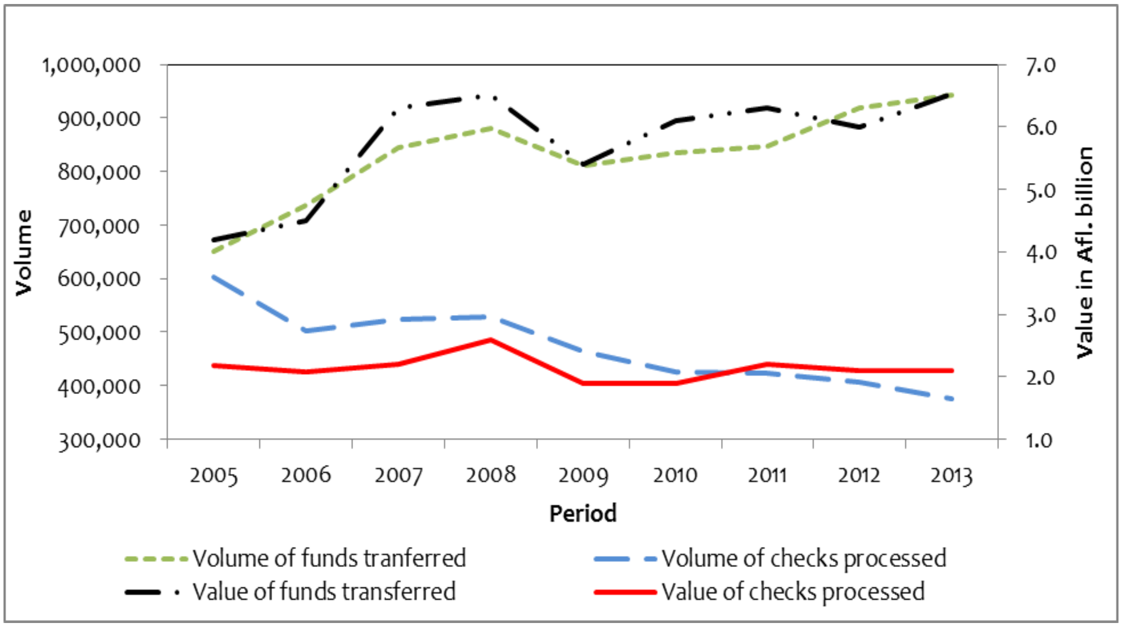
3.1.2 Clearing system

To contribute to a safe, secure, and efficient payment system that allows the public to complete transactions smoothly, the CBA operates a computer network system called the OnNet Clearing System (ONCS) (previously known as the Goldnet Clearing System). This batch-clearing electronic payment system processes payments between the commercial banks, the Department of Finance, a number of government-related institutions, such as the Water en Energie Bedrijf Aruba N.V. (WEB), the N.V. ELMAR (ELMAR), the Servicio di

Telecomunicacion di Aruba N.V. (SETAR), the Stichting Algemeen Pensioenfonds Aruba (APFA), and the CBA. This system is based on a secured web-client solution through which local interbank checks and fund transfers are settled.

The ONCS continued to operate smoothly in 2013. The volume as well as the value of funds transferred through ONCS increased in 2013 by approximately 22,847 transactions (2.5 percent) to 942,814 transactions and by Afl. 0.5 billion (8.3 percent) to Afl. 6.5 billion respectively, compared to the previous year. On the other hand, the volume of checks processed fell further in 2013 by approximately 31,256 checks (7.7 percent) to 376,457 checks (2012: 407,713 checks), while the value of checks processed remained unchanged at Afl. 2.1 billion, compared to 2012 (see Chart 3.3).

Chart 3.3: Transactions processed by the CBA Clearing System



3.1.3 Banker to the government

Within the scope of the CBO, the CBA also functions as the banker for the government and advisor to the Minister of Finance. As part of its treasury services to the government, the CBA accepts deposits from the government and carries out its foreign payment instructions as well as a small part of its local payments. The CBA additionally provides services regarding the issuance and settlement of government securities.

In conformity with the CBO, the CBA does not charge any fee on the domestic and foreign payments carried out on behalf of the government. These payments are cleared through the accounts of the Department of Finance and the Servicio di Impuesto y Aduana (SIAD), including its earmarked accounts held at the CBA. The total balance of these accounts amounted to Afl. 74.8 million at the end of 2013. Government deposits held in earmarked accounts increased to Afl. 22.7 million at the end of 2013 (2012: Afl. 21.3 million). In addition, the development fund account, managed by the Stichting Fondo Desaroyo Aruba (FDA), fell by Afl. 6.1 million to Afl. 7.7 million at the end of 2013, mostly due to payments made related to ongoing projects of the FDA.

In 2013, the CBA assisted with the renewal of four 3-month treasury bills in tranches of Afl. 45 million and Afl. 20 million at each issuance. Furthermore, the CBA assisted with the issuance of one 6-month cash loan certificates and the renewal of one 6-month cash loan certificates in the amount of Afl. 8 million in both cases. The yield on the 3-month treasury bills fluctuated between 1.72 percent and 2.01 percent, compared to fluctuations in the yield in 2012 between 1.43 percent and 2.01 percent. The weighted average yield on the 3-month treasury bills was 1.98 percent in 2013 and was slightly higher compared to the previous year (2012: 1.95 percent), reflecting the limited available liquidity on the domestic money market.

The CBA did not intermediate on behalf of the government with respect to the issuance of government bonds on the domestic market in 2013 as the government covered its financing needs via domestic loans as well as placement of bonds on the international capital market.

3.2 International payment system

3.2.1 Daily exchange rate fixing

The CBA's official buying and selling rates for the U.S. dollar from and to the commercial banks remained fixed at Afl. 1.7895 and Afl. 1.7905, respectively. Besides the U.S. dollar, and in accordance with article 12, section 3 of the CBO, the CBA publishes daily quotations for eight other foreign currencies based on data provided by the European Central Bank (ECB).

These rates are published on a daily basis on the CBA's website and are valid for amounts up to Afl. 100,000. For transactions greater than Afl. 100,000, the commercial banks can set other exchange rates. In 2013, the selling rate of the euro against the Aruban florin varied between Afl. 2.29 and Afl. 2.47, while the buying rate fluctuated between Afl. 2.28 and Afl. 2.47. At the end of December 2013, the euro appreciated slightly against the florin, pushing the selling rate up by 4.6 percent or Afl. 0.11 to Afl. 2.48 at the end of 2013, when compared to the corresponding period of 2012.

3.2.2 Foreign exchange transactions

In 2013, foreign exchange transactions settled through the CBA led to a net sale of Afl. 75.0 million of foreign exchange reserves compared to a net purchase of Afl. 118.4 million in foreign exchange reserves in 2012. This turnaround resulted from decreases in the net purchase of foreign exchange reserves from the government and other clients of, respectively, Afl. 175.8 million and Afl. 10.7 million, and an increase in net sale of foreign exchange reserves to commercial banks of Afl. 6.9 million when compared to 2012.

Overall, the contraction in the net purchase of foreign exchange reserves from the government related to the foreign exchange transactions carried out by the CBA in 2013 on its behalf was brought about by an Afl. 67.7 million drop in foreign exchange purchases and an Afl. 108.1 million rise in foreign exchange sales. The fall in foreign exchange purchases from the government was attributed mainly to lower receipts of funds from the bond issuance by the government on the international capital market during 2013, while the growth in foreign exchange sales to the government was caused by an increase in its foreign exchange spending.

The CBA's total gross foreign exchange purchases grew by Afl. 22.1 million or 2.2 percent to Afl. 1,038.3 million in 2013, stemming mainly from an Afl. 99.8 million or 18.9 percent increase in foreign exchange purchases from the commercial banks. This expansion was partially offset by the earlier mentioned fall in foreign exchange purchases from the government and an Afl. 10.0 million decline in foreign exchange purchases from other clients, including CBA's interest earnings. On the other hand, a total amount of Afl. 20.5 million was received by the government in 2013, including an amount of Afl. 18.3 million associated with the final contribution of the Dutch government in the development fund foundation of Aruba (FDA).

Total gross foreign exchange sales of the CBA expanded by Afl. 215.5 million or 24.0 percent to Afl. 1,113.3 million in 2013, reflecting rises in the foreign exchange sales to the commercial banks and the government of, respectively, Afl. 106.7 million or 17.1 percent and Afl. 108.1 million or 40.7 percent. The latter increase was largely related to higher payments for foreign debt servicing and the governments' representatives abroad in 2013 of Afl. 93.9 million and Afl. 3.8 million, respectively.

Table 3.3 Foreign exchange transactions */
(in Afl. million)

	2011	2012	2013
Net purchases/sales (-) from/to commercial banks	47.6	-94.2	-101.1
Net purchases/sales (-) from/to government	-142.7	190.7	14.9
of which government's foreign exchange spending	*-147.6*	*-265.9*	*-374.0*
Net purchases/sales (-) from/to others	24.9	21.9	11.2
Net purchase/sale (-) of foreign exchange	-70.2	118.4	-75.0

Source: CBA.
*/ Including adjustments for statistical differences.

3.2.3 Foreign exchange regulations

In April 2013, the foreign exchange regulations concerning transfers to and from foreign bank accounts and foreign intercompany accounts were revised. The Notice concerning Foreign Exchange Transactions RV 2009/1 was revoked and replaced by a Decree on Foreign Exchange Transactions 2013/K.2. This Decree entails a general foreign exchange license for executing transfers to and from notified foreign bank accounts and foreign intercompany accounts. The holders of foreign bank accounts and foreign intercompany accounts, who have notified the CBA of these accounts and who comply with the reporting requirements laid down in the aforementioned Decree, are included in the CBA's quarterly list of compliant holders of foreign bank accounts and foreign intercompany accounts. The companies and persons mentioned in this list may execute transfers to and from these accounts without a special foreign exchange license of the CBA.

No other changes have been made to the foreign exchange license regulations during 2013. Pursuant to the SOFET, no restrictions are imposed on payments related to current account transactions, while capital transactions above a certain threshold do require a special foreign exchange license from the CBA. The annual upper limit for executing capital transactions without any administrative restrictions was kept at Afl. 300,000 for resident natural persons and Afl. 750,000 for resident legal entities (excluding commercial banks). Also, dividend distributions to nonresident shareholders require a declaration from the CBA in order to transfer the dividend amount.

Pursuant to the Notice concerning Foreign Exchange Transactions AW 2005/1, commercial banks also require a special foreign exchange license when granting loans to nonresidents that exceed Afl. 1,000,000 per annum per individual or group of nonresident borrowers, as well as for certain transfers or sales of financial instruments such as bonds and notes to nonresidents.

In 2013, the number of special foreign exchange licenses granted by the CBA rose by 89 (29.2 percent) to 394 compared to 2012 (see Table 3.4). This surge was mainly caused by increases in the number of special foreign exchange licenses granted for transfers to and from notified foreign accounts, selling/buying of real estate, other capital transactions and portfolio investments abroad. This increase was partially offset by a decrease in the number of the licenses granted in the category lending/borrowing abroad. In 2013, the total value of the transactions for which licenses were granted expanded by Afl. 621.0 million (129.8 percent) to Afl. 1,099.6 million, caused mainly by increases of Afl. 385.6 million (726.2 percent) in the amount of transactions related to the category other capital transactions, Afl. 135.6 million (65.1 percent) related to lending/borrowing abroad, which includes an infrastructural project, and Afl. 110.3 million (392.5 percent) related to investments abroad. On the other hand, the total value of transactions related to selling/buying of real estate declined by Afl. 24.6 million (20.9 percent) to Afl. 93.3 million in 2013.

In 2013, the number of declarations for dividend distributions to nonresident shareholders decreased by 2 (4.7 percent) to 41. However, the total amount of dividend distributions increased by Afl. 67.9 million (92.9 percent) to Afl. 140.9 million when compared to 2012.

Table 3.4 Overview of special foreign exchange licenses issued
(Amounts in Afl. million)

	2012		2013	
Description	**Number**	**Amount in Afl.**	**Number**	**Amount in Afl.**
1. Lending / Borrowing abroad				
a. Refinancing	3	41.5	4	70.6
b. Other	48	166.8	38	273.3
2. Portfolio investment abroad	9	28.1	24	138.4
3. Selling / Buying real estate	76	117.9	98	93.3
4. Transfers to and from notified foreign accounts	152	71.2	195	85.3
5. Other capital transactions				
a. Participation in local companies by nonresidents	4	6.1	13	35.3
b. Participation residents in companies abroad	1	4.2	2	1.2
c. Granting of guarantees to nonresidents	7	34.9	3	363.5
d. Other	5	7.9	17	38.7
Total	**305**	**478.6**	**394**	**1,099.6**

Source: CBA.

3.2.4 Foreign exchange commission

Based on article 2, paragraph 1, of the SOFEC, residents must pay a 1.3 percent foreign exchange commission on their payments to nonresidents. These payments may be effectuated through, inter alia, domestic commercial banks or via foreign accounts reported to and approved by the CBA.

However, based on the State Decree Regulation Exemption Foreign Exchange Commission some of the transactions conducted by certain groups of companies (including government-related companies) are exempted from the payment of the foreign exchange commission.

Pursuant to article 12 of the State Ordinance on the Free Zone, free-zone companies may request an exemption from the payment of foreign exchange commission on foreign payments for the import of goods and services for the purpose of re-export.

Also, offshore companies, which have obtained an exemption based on article 19 of the SOFET, as well as Aruba Exempt Corporations, the so-called AVVs, which were incorporated before January 1, 2006, and, by virtue of law, are considered nonresidents, are not subject to the payment of foreign exchange commission.

The government of Aruba is responsible for determining the policy concerning the foreign exchange commission, while the CBA, pursuant to article 5 of the SOFEC, is entrusted with the levy and collection thereof. In 2013, the total amount of foreign exchange commission collected grew by Afl. 2.1 million (4.5 percent) to Afl. 48.8 million compared to 2012**.** In that year, the CBA transferred Afl. 48.2 million to the Treasury (2012: Afl. 45.4 million). This amount included the amount accrued by the end of 2012.

3.3 Managing the foreign exchange reserves

The CBA manages Aruba's net foreign assets as laid down in article 12, sub 1, of the CBO and applies, among other things, the B-9 rule for commercial banks and the 40-60 percent investment rule for institutional investors. The B-9 rule allows commercial banks to hold a certain level of foreign exchange reserves as working balances and to settle the foreign transactions of their clients. The 40-60 percent investment rule requires institutional investors to maintain a certain amount of their investments domestically.

The CBA's policy regarding the management of the official reserve remained unchanged in 2013. The CBA continues to pursue a prudent investment policy to minimize potential losses and aiming at preserving its capital (minimum A rates). The official foreign exchange reserves are invested by the CBA predominantly in U.S. dollars and in government and U.S. agency securities (incl. mortgage backed securities), securities issued by qualifying supranational financial institutions, and money-market instruments comprising mostly certificates of deposits, time deposits, treasury bills, and corporate bonds. The latter investment option is limited to the financial services industry, specifically banks and financial institutions.

3.4 Monetary policy

In 2013, the reserve requirement remained the CBA's main tool of monetary policy. The Monetary Policy Committee (MPC) of the CBA met six times during 2013 to review monetary developments and the economic outlook. The more frequent assessments of the adequacy of the monetary policy allow the CBA to react swiftly to deviating monetary and/or economic conditions. The MPC considered several indicators, including the level of net foreign assets (and official reserves), (core) inflation, and banking sector credit. The reviewed economic indicators remained adequate throughout the year. Consequently, the MPC decided to uphold the reserve requirement at 11 percent and the advance rate at 1 percent.

Aruba's economy expanded by 4.8 percent in real terms during 2013, due mainly to the strong performance of the tourism sector. Domestic credit also grew by 4.0 percent, mainly because of higher net claims of the banking sector on the private sector. This increase was driven chiefly by an expansion in business loans (7.5 percent). Based on the results of the business perception survey, businesses were positive on both current and short-term future economic conditions. Furthermore, housing mortgages rose by 5. percent in 2013 and consumer credit decreased slightly by 0.1 percent. The latter signaled that consumers were cautious about borrowing as consumer confidence remained negative throughout 2013. Net claims on the public sector decreased in 2013 compared to 2012 largely related to the receipt of funds stemming from the placement of government bonds on the international capital market in that year. Government deposits increased by 40.0 percent or Afl. 28.5 million.

3.5 Financial sector supervision

The CBA is the sole supervisory authority in Aruba with respect to the financial sector, aiming primarily at safeguarding the confidence in the financial system of Aruba by promoting the (financial) soundness and integrity of the supervised sectors and institutions. Currently, it is entrusted with the regulation and supervision of the credit system, insurance sector, company pension funds, money transfer companies, and trust service providers pursuant to the sectoral supervisory state ordinances. Furthermore, the CBA is tasked with overseeing compliance with the AML/CFT State Ordinance and with the Sanction State Ordinance 2006. Consequently, the CBA also has AML/CFT oversight responsibility over all sectors subject to the AML/CFT State Ordinance and Sanction Decree Combat Terrorism and Financing Terrorism.

Prudential supervision is focused on monitoring the financial soundness of the supervised institutions (*inter alia* solvency, liquidity, risk management, corporate governance, and technical provisions), while integrity supervision concentrates on integrity aspects (*inter alia* money laundering, terrorist financing, breaches of law or acting contrary to generally accepted standards, promotion of ethical behavior, and ethical corporate culture).

Ongoing off-site surveillance and periodic risk-based on-site examinations are carried out by the CBA to assess compliance with the supervisory laws and regulations governing the mentioned supervised institutions. In addition, the CBA holds regular bilateral meetings with the supervised institutions and their representative organizations.

As part of the Kingdom of the Netherlands, Aruba is a member of the Financial Action Task Force (FATF), the internationally recognized standard-setter for anti-money laundering and combating terrorist financing. The government of Aruba has committed itself to implement the FATF recommendations and, thus, bring its AML/CFT framework in line with FATF standards. Since the adoption of the FATF Mutual Evaluation Report (MER) on Aruba on October 16, 2009, Aruba has made significant progress in eliminating the deficiencies mentioned in the MER. On February 12, 2014, the FATF Plenary acknowledged that Aruba had made significant progress in addressing the deficiencies identified in the 2009 MER. It concluded that Aruba is now largely compliant with the FATF Core and Key Recommendations and, thus, could exit the regular follow-up process. The report prepared by the FATF, based on Aruba's 8th follow-up report, contains a detailed description and analysis of the actions taken by Aruba since the MER of October 2009. This report can be found on the website of the FATF (www.fatf-gafi.org).

Aruba is also a member of the Caribbean Action Task Force (CFATF), a FATF-style regional body in the Caribbean whose main objective is to achieve effective implementation of and compliance with the FATF recommendations. On May 28, 2014, the CFATF also decided to remove Aruba from its follow-up process.

As of January 1, 2013, the reach of the existing sectoral supervisory laws was extended. The scope of the State Ordinance on the Supervision of the Credit System (SOSCS) was broadened to include, among others, electronic money institutions, while that of the State Ordinance on the Supervision of Trust Service Providers was widened to include trust companies providing trust services to local companies. Moreover, all sectoral supervisory laws were amended to enhance the possibilities for cooperation and information exchange with foreign supervisors and to harmonize and strengthen the requirements in the sectoral supervisory laws with regard to fit and proper testing. In addition, a uniform requirement in the area of sound and controlled business operations was introduced in all sectoral supervisory laws. The amendments made to the State Ordinance on the Insurance Business (SOSIB) introduced the possibility to place insurance brokers under the CBA's supervision.

In June 2013, the CBA submitted a draft State Ordinance on the Supervision of the Securities Business to the Minister of Finance for approval. This draft state ordinance introduces a licensing obligation for securities brokers, portfolio managers, investment schemes, and operators of a stock exchange and ongoing supervision on the same. This state ordinance will most likely be discussed in Parliament soon.

On April 1, 2012 the CBA issued a dispensation policy for pawnshops operating in Aruba and guidelines on the conduct of the business of pawnshops / "compra y benta" companies. Pawnshops already active in Aruba on April 1, 2012 were granted a transition period of one year (ending on March 31, 2013) to submit a dispensation request. Meanwhile, the CBA has granted three (conditional) dispensations to pawnshops.

3.6 Organizational affairs

At the end of December 2013, the CBA employed 83 persons full-time compared to 88 in 2012. During 2013, four new employees were hired, seven employees' labour contracts were terminated by mutual agreement, the secondment period of one employee from De Nederlandsche Bank N.V. (DNB) ended, and one employee retired from the CBA. The management of the CBA would like to thank its staff members for their loyalty and ongoing commitment and dedication to the CBA during 2013.

For the third consecutive year, the CBA's external auditor completed an audited review of CBA's mid-year financial figures. The CBA also achieved its goal of having the external auditor complete the year-end audit by early 2014. On February 27, 2014, the Auditors of the CBA issued an unqualified opinion with respect to the 2013 financial statements of the CBA, which subsequently was adopted by the BoSD.

In 2013, the CBA published its first edition of the art collection book, thus promoting the work of the Aruban talents.

3.6.1 Training, courses, and seminars

During 2013, as part of upgrading skills and knowledge sharing, the CBA staff participated in a number of courses, seminars, and conferences held locally and abroad.

3.6.2 Internal organization

In 2013, the Internal Audit Department (IAD) enhanced its tasks, procedures, and activities. In addition, the processes and procedures of a number of departments, including the Cash and Vault Department and the Legal Affairs Department, were reviewed and updated.

During 2013, the Information Systems and Facilities Department (ISFD) executed a project in which the data storage capability of the CBA was increased twofold in order to suit the continuously growing amount of data within the organization. In other efforts to promote mobility and increase productivity, a set of secured iPhones replaced the outdated Blackberry devices used by management.

Furthermore in 2013, several preparations took place for the upgrade of the IBS Banking Application (IBS) scheduled for mid-2014. A new AS400 server that will be the production host was purchased and installed within the datacenter.

An additional number of virtual servers were configured to support enhanced IBS functionalities such as on-demand reporting.

In collaboration with the Information & Physical Security Department (IPSD), the ISFD successfully executed the yearly IT disaster recovery exercise in 2013 in Sterling Forest, NY in which the critical IT infrastructure was restored and tested. In addition to the exercise, the IPSD executed an enterprise-wide business continuity planning project that entailed the documentation of business continuity for all departments.

In the field of information security, the IPSD has been constantly engaged in designing, implementing, and evaluating processes and procedures. The IPSD performed audits and reviews on selected software applications within CBA's IT environment. Furthermore, in 2013 the IPSD addressed and resolved all the previous year IT audit findings identified by the external accountants.

In its effort to continue executing the recommendations in the report "Structuring the information management at the CBA", the Secretariat & Archives Department (S&AD) selected two work processes in 2013, namely the recruitment process and the process of weekly statements, to be pilot tested in the workflow module. Intensive sessions were conducted together with the related departments and an external consultancy bureau to gather the necessary information for this module.

Furthermore, in 2013 the S&AD in close cooperation with the Human Resources (HR) department started with the restructuring of the HR archive. The S&A department will support the HR department in the areas of recordkeeping, policies, procedures, systems, and processes as well as the retention management.

4 GOVERNANCE AND ACCOUNTABILITY

The financial year 2013 was characterized by various important developments. The focus in this section is on corporate governance and risk management with special attention to investments and financial risks.

4.1 Governance structure

The CBA is a public corporate body incorporated under Aruban law. Its independence is laid down in article 2, paragraph 2 of the CBO and it is a bearer of rights and duties. While its principal tasks are stipulated in the CBO and other rules and regulations, the CBA strives to have a sound corporate governance system in place that supports proper and effective decision making, through the incorporation of appropriate checks and balances to ensure accountability, fairness and transparency.

Management structure

The CBA is managed by a President and two Executive Directors, who together form the Executive Committee. The members of the Executive Committee are appointed and dismissed by the Governor of Aruba. This committee operates according to the general regulations set out in the State Decree giving directives to the President, the Executive Directors, and the BoSD.

The management team of the CBA consists of the President, the two Executive Directors, three General Managers, of which one position is still vacant, and 13 Department Managers. In addition, the CBA has an Investment Committee that advises on matters related to investment strategy, policy, and instruments, a Budget Committee responsible for preparing and submitting CBA's budget to the BoSD for approval, a Foreign Exchange Committee that coordinates all works of the departments of the CBA which are involved in implementing the regulations concerning foreign exchange transactions and foreign exchange commission, a Monetary Policy Committee that convenes regularly to evaluate and determine the CBA's monetary policy, and a Risk Management Committee responsible for ensuring that sound policies, procedures and practices are in place for the enterprise-wide management of the CBA's material risks.

Board of Supervisory Directors (BoSD)

The BoSD of the CBA consists of at least three and at most five members. The Government Commissioner is the Chairman of the BoSD and is appointed and dismissed by the Governor of Aruba. The members of the BoSD are nominated for a term of five years. At the end of 2013, the BoSD consisted of four members (including the chairman). The BoSD supervises the CBA's operations and oversees the management of its property as well as the funds entrusted to it. On request of the BoSD, the Executive Committee reports on policies implemented, as well as on administration and management. The BoSD meets with the Executive Committee at least four times a year and exercises its duties according to the rules set forth in the State Decree giving directives to the President, Executive Directors and the BoSD. Its tasks include, among other things, the approval of the budget and the adoption of the financial statements. After approval by the BoSD, the budget is sent to the Minister of Finance and the Chairman of the Aruban Parliament, while the financial statements are submitted to the Minister of Finance. The adoption of the financial statements by the BoSD also serves to discharge the President and the Executive Directors from liability. The BoSD is also responsible for appointing the CBA's external auditor.

In 2013, the BoSD and the Executive Committee held 13 scheduled meetings to discuss several ongoing issues, including the annual report 2012, the mid-year review 2013, and the budget 2014. In addition, the Chairman of the BoSD held weekly meetings with the President to discuss matters related to the CBA.

The employment conditions for the staff, including pension provisions, are determined by the BoSD and the President after consulting with the Minister of Finance. The remuneration of the BoSD is determined by the Minister of Finance, after consulting with the members of said Board and the President. Also, additions to the general reserve and the forming of earmarked reserves are determined by the Executive Committee following prior written approval of the Minister of Finance.

4.2 Risk management

The CBA faces a number of risks with respect to the performance of its (main) tasks. Some of these risks are general, while others are unique to central banks. Risk management is integral to the CBA's daily operations, with management's efforts directed towards ensuring that detailed procedure manuals, proper segregation of duties, and clear delineation of roles and responsibilities are in place and integrated in departmental processes.

The Risk Management Committee is tasked with establishing a standardized risk management system for the CBA. This committee monitors and provides advice on all material risks and recommends the steps needed to mitigate these risks. In 2013, the CBA developed an overall risk matrix that includes a broad range of risks. In 2014, the CBA will review these risks and conduct another risk assessment to identify the 10 most significant risks per department.

The most fundamental risks are legal and reputational risks. Reputational risk results when policy errors occur regarding monetary policy or supervision of the financial system that could negatively impact the economy in general and the

CBA's reputation in particular. Other risks include, but are not limited to, the following:

- Risk associated with the holding of foreign currency reserves (market, credit, and counterparty risks). The steps taken to mitigate these risks are further elaborated in paragraph 4.3.
- Risk associated with processing and storing currency, including risk of theft and robbery.
- Risk related to bringing into circulation bank notes and coins that are not adequately guarded against counterfeit.
- Risk associated with the operations of the local payment system, which could arise from technical faults.
- Risk related to noncompliance with the prevailing laws and regulations (compliance risk).
- Risk associated with the dissemination of confidential information.
- Risks of publishing inaccurate data.

The CBA views risk management as an integral part of the day-to-day responsibility of the President, Executive Directors, General Managers, and Department Managers. The CBA has an Internal Audit Department (IAD) that independently supports the Executive Committee in matters related to the evaluation of the effectiveness of internal controls, risk management, and governance processes.

To guarantee the continuity and safeguarding of its IT systems and processes, the IPSD is responsible for protecting business information and information systems of the CBA. In addition, this department is in charge of the physical security of CBA property. The IPSD, in close cooperation with the ISFD and the IAD, formulates policy, rules, and procedures concerning both the information and physical security of the CBA.

4.3 Investment and financial risks

Management of the official reserve impacts the size and structure of the CBA's balance sheet, as well as its financial performance. To minimize the associated risks, the CBA implements a prudent investment policy strategy, which is fully fixed income based. Against this background, the CBA invests in financial instruments that meet high standards in terms of credit quality and liquidity. Within these strict parameters, the CBA seeks to diversify and optimize its return.

The Investment Committee meets weekly to discuss, among other things, matters related to current market trends and economic developments that could impact its official reserve as well as investment performance and related risks. Once a month, the committee discusses the performance report of each asset manager, providing information for strategic or tactical changes in the investment policy.

Implementation of the strategic decisions is delegated to the asset managers. The portfolios are further categorized by a duration ladder, which consists of a medium-term portfolio with an average duration of 0-3 years that is managed by an external asset manager, and a medium-term portfolio with an average duration of 0-3 years and a long-term portfolio with an average duration of 0-10 years that are managed internally.

Strict investment guidelines have been established for asset managers; any deviation from these guidelines requires prior written approval of the President. The IAD verifies that investments are executed according to the stipulated guidelines.

In 2013, the Investment Committee further revised CBA's investment guidelines to include other asset classes (*inter alia* corporates and collateralized mortgage obligations (CMO)) and to adjust the existing price constraints. The CBA also reviewed its investment policy and strategy in light of the changing international investment environment.