

**Parliamentary Speech on
Constitution of the Republic of Singapore (Amendment) Bill
20 October 2008
By Gautam Banerjee**

Mr Speaker Sir, thank you for allowing me to speak on the Constitution of the Republic of Singapore (Amendment) Bill.

This Bill to amend the Constitution to fundamentally change the basis on which the Government of the day can spend Singapore's reserves has been contemplated, discussed and debated for a number of years. Indeed, every year during the Committee of Supplies debate following the Finance Minister's Budget Statement, this subject has received attention from many MPs asking the government to undertake a review of the hitherto very strict, narrow and limited ways a government can use past reserves for current spending.

The fact that the second reading of this very important Bill is taking place today when we are in the midst of a Global Financial Crisis of unprecedented proportions is entirely a co-incidence. However, the financial meltdown we have experienced over the past few weeks will inevitably influence the discussion and debate we will have in this

house during the second reading of this Bill. But I view the timing of this debate as a positive because it has raised the awareness of how complicated and convoluted the global financial system has become and that we cannot implicitly place trust and reliance in the system, or on venerable and reputable institutions, which for years have been pillars of strength supporting the global financial infrastructure that we have taken for granted. We are fortunate in some ways that we can take on board some basic “dos” and “don’ts” from this present financial crisis that we are embroiled in, as we change our Constitution to allow the use of our hard-earned and precious reserves for current spending.

Sir, before I comment on the Bill itself, let me say that I agree with the Government that a review of the present rules relating to the use of reserves is necessary because of the following reasons:

1. Our present rules only allow the use of:
 - (a) dividends, interest and other income received by the Government during the financial year from investing the reserves of the Government.

- (b) the interest received by the Government during the financial year from loans whenever given by the Government.

Under current rules, all capital gains, realised or unrealised, are not available for spending

Also, the present rules on the spending of our reserves implicitly assumes that all our reserves are invested in fixed income instruments, which clearly they are not. A quick look at the accounts of GIC or Temasek will reveal that a significant portion of the “relevant assets” referred to in the Bill are in asset categories such as Private Equity, Real Estate, Alternative Investment Funds etc, which do not provide regular interest income on dividends. In any case, the concept of total returns should take into account not only the fixed annual income that is received from these assets, but also the change in carrying value of the underlying assets. So unless we update the present rules on spending of reserves, we will have available for current spending only a small proportion of the total returns that are being earned on our reserves.

Under the current rules, most of the returns being generated from our reserves will therefore not be available to the present generation of Singaporeans. So it is necessary to re-calibrate the use of our reserves if we are to be fair to different generations of Singaporeans.

Mr Speaker Sir, allow me now to examine and comment on the main provisions of this Bill.

The amendment bill applies only to relevant assets, which is defined to be assets held by GIC and certain assets held by MAS less certain liabilities. Other assets remain under the current constitution provisions, and all the capital gains therefrom are still considered past reserves.

The Minister will derive and apply an expected long-term real rate of return to the relevant assets. 50% of the amount so computed will form part of current reserves. The actual dividends, interest and other income received from the relevant assets will be ignored (ie they will go into past reserves) to avoid double counting. This “expected long term real rate of return” is forward looking and based on the Minister’s expectations and assumptions. It may not be the same as the

historical realized rate of return. It also may not be the same as the actual realized returns each year. The only check and balance is the President's concurrence. This is a completely different basis from the current constitution which is based on actual returns.

The inclusion of capital gain will ensure consistency in the treatment of asset classes with different proportion of yield vs capital gains. Returns from investment take the form of dividend/interest or capital gains upon disposal. Often the 2 element are inter-related. For the same investment, a lower dividend/interest distribution will in theory result in higher eventual capital gains, and vice versa. For example, high growth companies. Hence, it is inconsistent to include only the dividend/interest but not the capital gains.

The "expected long term real rate of return" entails the use of various assumptions and expectations about the future. These are subjective so the Bill seeks to incorporate certain safeguards into the Proposed Amendment:

1. Firstly, only 50% of the long term return is allowed to be used. This provides some buffer against uncertainties, which are inherent in any forward looking assumption and expectation.
2. Secondly, the Minister is required to review the long-term real rate of return each year. This ensures that current market conditions and outlook are taken into account, and the rate revised if necessary.
3. Thirdly, the President has to concur on the long-term real rate of return each year. This allows a process of check and balance on the assumptions and expectations adopted. This is very important given the subjectivity and judgment involved in deriving the rate.

I believe the checks and balances in the Bill have been well thought through, but my main concern is that they must not only work but be seen to work by Singaporeans at large. We have to step up transparency and communication compared to what we do now. Unlike the present system, which is based on historical earned income, the proposed new system will be based on assumptions of

future trends and outcomes – and requires a great degree of judgement. So we should discuss and embellish the checks and balances. I have the following suggestions, which I would like the Minister to consider:

1. The “expected long term real rate of return” used for the computation should be capped by the actual historical long-term real rate of return of the components of the relevant assets. While the past is not necessary an indication of future investment performance, a cap based on historical actual return provides a sanity check on the assumptions and expectations adopted. In the long run, the historical cap will be automatically revised upwards if the actual returns consistently turn out to be higher.
2. Both the “expected long term real rate of return” used in the computation and the “actual historical long term real rate of return” should be published

3. The basis of computing “expected long term real rate of return”, including assumptions to be made, should be set out and consistently applied from year to year.

4. As part of His annual concurrence with the “expected long term real rate of return”, the President should have powers to review the assumptions and expectations adopted, the application and any change in the basis used, and the computation. This review should be carried out independently of the government. A process for this review, including the resources and expertise that will be required to support the President should be clearly set out, discussed and debated in this house.

Given the very significant changes and their implications for the future, it is worth spending time satisfying ourselves in this house that we not only have a robust system of checks and balances, but there is also good communication and transparency.

Sir, at the end of the day, we can have all the checks and balances in place but as the financial crisis has clearly demonstrated, that unless the people in charge are competent, honest and have the interests of all Singaporeans at heart, the system will fail. By amending the Constitution with this Bill, we are raising the stakes and the demands on the Government of the day. So the clear message to all Singaporeans is that we should continue to have the best, brightest and honest amongst us to be in charge of the Government and the finances of the nation.

Before I conclude, I would like a clarification from the Minister. Given that the expected rate of return includes both realised and unrealised investments, how is the government proposing to fund the amount available for current use if the long-term expected rate of return exceeds the realized dividend/interest and capital gains each year? Sir, put in another way, how do we manage the liquidity issue because the expected long-term rate of return is based on assumptions and expected outcomes, not actual cash that has been earned.

Sir, thank you for giving me this opportunity to speak on this Bill.