

MASTER FILES

ROOM C-120

04

INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 84/165

10:00 a.m., November 16, 1984

J. de Larosière, Chairman

Executive Directors

M. Finaish

G. Grosche

J. E. Ismael

A. Kafka

Y. A. Nimatallah

P. Pérez

J. J. Polak

G. Salehkhoul

J. Tvedt

N. Wicks

Zhang Z.

Alternate Executive Directors

w. B. Tshishibmi

M. K. Bush

H. G. Schneider

X. Blandin

T. Alhaimus

T. Yamashita

L. Leonard

C. Robalino

A. S. Jayawardena

A. Abdallah

B. Jensen

J. E. Suraisry

A. V. Romuáldez

O. Kabbaj

T. A. Clark

I. Angeloni, Temporary

Wang E.

L. Van Houtven, Secretary

J. C. Corr, Assistant

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Also Present

African Department: R. J. Bhatia, Deputy Director; G. E. Gondwe, Deputy Director; C. J. Hoban. Central Banking Department: J. B. Zulu, Director. European Department: D. A. Brodsky. Exchange and Trade Relations Department: C. D. Finch, Director; M. Guitián, Deputy Director; C. Brachet. External Relations Department: H. O. Hartmann. IMF Institute: O. B. Makalou. Legal Department: G. P. Nicoletopoulos, Director; W. E. Holder, Ph. Lachman, A. O. Liuksila, S. A. Silard. Middle Eastern Department: M. A. El-Erian. Research Department: R. R. Rhomberg, Deputy Director. Secretary's Department: J. W. Lang, Jr., Deputy Secretary. Treasurer's Department: W. O. Habermeier, Counsellor and Treasurer; Q. Md. Hafiz, T. B. C. Leddy. Personal Assistant to the Managing Director: S. P. Collins. Advisors to Executive Directors: G. Castellanos, S. M. Hassan, G. E. L. Nguyen, P. Péterfalvy, G. W. K. Pickering, M. Z. M. Qureshi, T. Sirivedhin, E. M. Taha, D. C. Templeman, A. Vasudevan. Assistants to Executive Directors: J. R. N. Almeida, W.-R. Bengs, J. Bulloch, M. B. Chatah, Chen J., L. E. J. M. Coene, J. de la Herrán, G. Ercel, V. Govindarajan, G. D. Hodgson, A. K. Juusela, S. Kolb, R. Msadek, K. Murakami, E. Olsen, T. Ramtoolah, M. Rasyid, J. E. Rodríguez, C. A. Salinas, A. A. Scholten, S. Sornyanyontr, A. J. Tregilgas, B. D. White, Z. Ismail.

1. ENLARGED ACCESS POLICY - EXTENSION AND ACCESS LIMITS FOR 1985

The Executive Directors considered a staff paper on the extension of the enlarged access policy and the access limits for 1985 (SM/84/235, 10/24/84; and Cor. 1, 10/25/84).

Mr. Grosche commented that the proposed decision was in concordance with the agreement reached at the September 1984 meeting of the Interim Committee; he could therefore support it.

Mr. Schneider remarked that from the outset his chair had been against a reduction in the access limits, but he could accept the compromise reached in the Interim Committee and, thus, the proposed decision. However, in Executive Board discussions preceding the Interim Committee, the impression had been given that the entire decision required an 85 percent majority for adoption. In SM/84/235, on the other hand, the staff had explained that only the first paragraph of the decision required an 85 percent majority and that the other paragraphs could be adopted with a simple majority of the votes cast. It appeared, therefore, that the enlarged access policy could be extended on the basis of a simple majority if the time limit of three to five years specified in Article V, Section 7(c) were not exceeded and if there were floating of the reserve tranche.

The Director of the Legal Department said that, in the circumstances specified by Mr. Schneider--which could in theory occur--the Executive Board could indeed extend the enlarged access policy by a simple majority of the votes cast. However, the proposed decision reflected the understandings reached in the Interim Committee to extend the policy in the present form.

Mr. Kafka stated that he would have preferred another outcome to the deliberations of the Interim Committee, but, because the proposed decision reflected a compromise, he would not oppose it.

Mr. Suraisry said that he supported the proposed decision as an accurate reflection of the conclusions reached by the Interim Committee. The continuation of the enlarged access policy would allow the Fund to respond effectively to the needs of its members in the period ahead.

Ms. Bush, Mr. Finaish, Mr. Pérez, Mr. Polak, Mr. Tvedt, Mr. Wicks, Mr. Zhang, Mr. Abdallah, Mr. Leonard, Mr. Romuáldez, Mr. Yamashita, and Mr. Angeloni expressed their support for the proposed decision.

Mr. Blandin said that he also supported the proposed decision, although he would have preferred to maintain the present limits.

Mr. Jayawardena, Mr. Jensen, and Mr. Tshishimbi stated that they agreed with Mr. Kafka's remarks.

The Executive Board then took the following decision:

The Fund, having reviewed the decisions on the policy on enlarged access and the limits on access to the Fund's resources under that policy and under the special facilities of the Fund (Decision No. 6783-(81/40), Decision No. 7599-(84/3), and Decision No. 7602-(84/3)), decides that:

1. In paragraph a. of Decision No. 7599-(84/3), "1984" shall be replaced by "1985."
2. (a) The following sentence shall be added after the first sentence of paragraph a. of Decision No. 7600-(84/3):
"Access by members to the Fund's general resources under arrangements approved under Decision No. 6783-(81/40) during 1985 shall be subject to annual limits of 95 or 115 percent of quota, three-year limits of 280 or 345 percent of quota, and cumulative limits of 408 or 450 percent of quota net of scheduled repurchases, depending on the seriousness of the member's balance of payments need and the strength of its adjustment effort."

(b) In paragraph b. of Decision No. 7600-(84/3), "1984" shall be replaced by "1985."

Decision No. 7841-(84/165), adopted
November 16, 1984

2. MISREPORTING AND NONCOMPLYING PURCHASES UNDER FUND ARRANGEMENTS -
GUIDELINES ON CORRECTIVE ACTION

The Executive Directors considered a staff paper on guidelines on corrective action relating to misreporting and noncomplying purchases under Fund arrangements (EBS/84/196, 9/13/84; Cor. 1, 9/18/84; Sup. 1, 11/1/84; and Sup. 2, 11/14/84).

Mr. Wicks recalled that at EBM/84/152 and EBM/84/153 (10/17/84) the Executive Board had spent a long time discussing the subject. At that time, the Chairman had noted that it had been difficult to determine the sense of the meeting, although there had been widespread support for certain general principles and for the adoption of guidelines on remedial action. The staff had attempted to capture in the proposed guidelines the wide range of views expressed by Directors. While the proposed text was unsatisfactory in a number of respects, he was willing to refrain from suggesting alternative wording in order to avoid reopening the whole discussion. It was important that the Executive Board should express in a substantive way its collective concern about the problem of misreporting by approving the guidelines. Thus, in a spirit of compromise, he could accept the revised draft of the guidelines put forward by the staff in Supplement 2 to EBS/84/196.

Mr. Jayawardena observed that, during the previous discussion of misreporting and noncomplying purchases, many Directors had suggested that a final decision on a finding of noncomplying purchases should be considered in the Executive Board because it involved a particularly sensitive aspect of relations between the Fund and a member. More important, there could be differences in the interpretation of performance criteria arising, for example, from ambiguity in the wording, and the Board could form a judgment whether the country had genuinely believed that what it had reported had been appropriate or whether the policies adopted to achieve the agreed objective had been adequate. The Executive Director for the country could bring to the attention of the Board additional nuances of interpretation that might assist Directors in coming to a decision. In that respect, the final sentence of paragraph 2 of the proposed guidelines in EBS/84/196, Supplement 1 was worded unsatisfactorily; in particular, the words "the Executive Board shall normally adopt..." gave an impression that the Board was little more than a rubber stamp. He suggested that the guideline could be improved by the deletion of that sentence and the addition to the preceding sentence of the words "...to be approved by the Executive Board on a lapse of time basis."

During the earlier discussion, Mr. Jayawardena continued, Directors had generally favored the establishment of an expectation, not an obligation, to repurchase a noncomplying purchase. He could not support, therefore, paragraph 6 of the proposed guidelines, which provided for the suspension of further purchases under an arrangement whenever a member failed to meet a repurchase expectation pursuant to the guidelines. As his chair had pointed out on the previous occasion, the Fund should not attempt to convert an expectation into an obligation by including sanctions in a stand-by arrangement, because to do so would be manifestly irregular. Furthermore, the inclusion in an arrangement of the possibility of suspension could lead to serious consequences for the program by introducing a large element of uncertainty after agreement on a program had been reached, especially in cases where large-scale debt rescheduling arrangements with commercial banks were tied to Fund programs over long periods. In addition, there was already adequate provision under Article V, Section 5, for the Fund to take independent action whenever a country acted contrary to the Articles of Agreement. Moreover, existing arrangements already contained sufficient provision to suspend purchases, as set out in paragraph 5 of Attachment A to Decision No. 6838-(81/70), adopted April 29, 1981, where it was clearly stated that a member's right to engage in transactions under the existing arrangement could be suspended by the Executive Board either generally or under the limiting procedures. Thus, paragraph 6 of the proposed guidelines was redundant.

Paragraph 7 provided that nothing in the guidelines should prevent the Fund from acting under the Articles or the Rules, Mr. Jayawardena noted. He believed that Mr. Polak had made that point during the previous discussion, but he did not believe that Mr. Polak had wished it to be incorporated in the guidelines. Indeed, the paragraph seemed unnecessary; it was well understood that the guidelines could not override

the Articles or the Rules and could not preclude the Fund from taking any action consistent with those agreements.

Mr. Polak said that he agreed with Mr. Jayawardena that paragraph 7 was not strictly necessary from a legal point of view; however, it made a useful point, and he preferred to retain it.

Mr. Suraisry commented that he agreed with Mr. Wicks that it was difficult to encompass fully all the views of Executive Directors in the draft guidelines. However, in a spirit of compromise, he could support the text put forward by the staff and hoped that other Directors would do likewise. In particular, he could endorse the procedure outlined in paragraph 2. The Fund management should have discretion to establish the facts, consult with the member concerned, and attempt to correct problems informally, and the Board should have an opportunity to give its views on the course of action recommended by the Managing Director. The lapse of time procedure appeared appropriate because the Board should have to meet only in very rare cases. He could also accept the expectation to repurchase referred to in paragraph 3, although he would have preferred an obligation to repurchase. The provisions in paragraphs 5 and 6 were most important because they protected the Fund if a member failed to meet its repurchase expectation. Paragraph 7 was also useful: as drafted, it allowed the Fund to use every sanction at its disposal in cases of deliberate misreporting or fraud without explicitly admitting the possibility that some members might engage in such practices.

The third sentence of the preamble to the guidelines envisaged that "...steps should be taken...to define performance criteria and other applicable conditions in a manner that would ensure accurate reporting," Mr. Suraisry continued. The sentence could be taken to mean either that the Fund was not at present defining performance criteria in such a way as to ensure accurate reporting or that poorly defined performance criteria were always the reason for misreporting. Neither interpretation would be correct. Perhaps the addition of the words "if necessary" at an appropriate point in the sentence would clarify the issue.

Mr. Ismael recalled that his chair had earlier expressed a preference for treating misreporting and noncomplying purchases on a case-by-case basis. He continued to believe that the need for a formal procedure, as embodied in the proposed guidelines, was dubious. However, the improvements to the proposed guidelines reflecting Directors' remarks at EBM/84/152 and EBM/84/153 were welcome. Paragraph 2 of the revised draft provided that the Managing Director would submit to the Executive Board a report together with his recommendations, which would normally be adopted on a lapse of time basis. Although such an important and rare decision should, as a rule, merit consideration at a meeting of the Board, the proposed text was acceptable because Directors would be given at least ten days to request that the matter be placed on the agenda for consideration. In paragraph 3, the replacement of an "obligation" with an "expectation" to repurchase was particularly welcome. The proposed 30-day period for repurchase was probably unrealistic; he hoped, therefore, that the Board would be as flexible as possible in that regard.

The provision in Fund arrangements for the suspension of further purchases in case of failure to meet a repurchase expectation, as suggested in paragraph 6, was unnecessary, Mr. Ismael continued. If the member had not met the performance criteria, it would be ineligible for further drawings anyway, whereas, if the situation had been corrected and the member had been able to meet subsequent performance criteria, it would probably have been granted a waiver, and there would have been no repurchase expectation. However, he did not object strongly to the wording in the paragraph. In sum, the proposed guidelines were generally acceptable; he hoped that Directors would exercise flexibility in considering specific cases.

Mr. Jensen remarked that he agreed with Mr. Jayawardena's comments. In addition, paragraph 1 failed to reflect the sense of the previous Board discussion of the subject with regard to the limitation period. At the end of the previous meeting, the Chairman had concluded that the majority of Directors considered a limitation period of two years "rather on the long side," meaning that such a majority had been prepared to accept a shorter period, perhaps one year or, as some Directors had suggested, the period until the next Article IV consultation with the member involved. He would have difficulty in supporting that particular aspect of the proposed decision.

He understood that the effect of the decision would be to correct future, rather than past, noncomplying purchases, Mr. Jensen continued. Cases of misreporting had been rare, and the objective of the decision was to avoid further occurrences by setting out clearly how the Fund would deal with them. That point should be clarified, either in the guidelines or in the preamble to them.

The Director of the Legal Department noted that the point referred to by Mr. Jensen was covered in the final sentence of the preamble to the draft guidelines, which read: "To this end, the Fund adopts the following guidelines, which shall apply to purchases made after the date of this decision...."

Mr. Yamashita recalled that, at the previous discussion of the subject, his chair had expressed its preference for a course of action that would have required a member to repurchase after a finding of misreporting. Nevertheless, his chair had taken the position that an expectation of repurchase was acceptable, provided that additional measures were incorporated to reinforce that expectation. Paragraphs 5 and 6 of the revised draft guidelines provided a sufficient safeguard in that respect. Accordingly, he could support the proposed decision.

Mr. Grosche stated that he supported Mr. Wicks, Mr. Suraisry, and Mr. Yamashita in the view that the proposed guidelines were an acceptable compromise solution, although he would have preferred a repurchase obligation rather than an expectation. The guidelines constituted a minimum safeguard to protect the Fund's resources against improper use and to guarantee evenhanded treatment of Fund members. He could support the

clarification introduced in paragraph 3 to the effect that the member's currency could be used in the Fund's transactions and operations as an alternative to repurchasing. In paragraph 2, he would have preferred "a period of normally ten days" for the lapse of time period instead of "at least ten days," in order to help prevent overextension of the period. However, in a spirit of compromise, he could accept paragraph 2 as drafted. Finally, he asked what the words "other action" in paragraph 3 meant. He hoped that the phrase would not be interpreted too broadly; otherwise, the necessary corrective action might be avoided or unduly delayed.

The Director of the Legal Department replied that "other action" might include, for example, a decision by the Executive Board to delay the granting of an outright waiver while it studied certain aspects of the question. Decisions of that nature had been taken in the past.

Mr. Polak said that he could support the guidelines as drafted. However, the proposal in paragraph 3 to allow the use of the member's currency as a way of reducing its debt to the Fund appeared clumsy; there seemed to be no good reason why a member found to have acted wrongly should be given a meaningless option that could only create difficulties for other members. He preferred, therefore, that the second sentence of paragraph 3 should be deleted along with the corresponding reference in the preamble, namely, "either by repurchase or by the use of its currency in transactions and operations of the Fund...."

He agreed with Mr. Jayawardena that the last sentence of paragraph 2 had not been drafted as Directors had intended, Mr. Polak continued. It would be preferable for the sentence to read:

The recommendations of the Managing Director shall normally be submitted to the Executive Board for a decision on a lapse of time basis, allowing a period of at least 10 days during which Executive Directors could ask that the matter be placed on the agenda of the Executive Board for consideration.

He also agreed with Mr. Suraisry that the third sentence of the preamble was poorly drafted. It would not necessarily be appropriate in all cases to admonish the Fund to "define performance criteria and other applicable conditions in a manner that would ensure accurate reporting." Perhaps the sentence could be deleted; alternatively, it could be redrafted to have the effect of a general injunction to the Fund rather than a provision applying "when such a case arises in the future. "Under the latter option, the redrafted sentence would have to be placed elsewhere in the preamble.

Mr. Romuáldez commented that the proposed decision reflected the compromise that his chair had been seeking. He agreed with Mr. Polak's remarks concerning the third sentence of the preamble. The Fund should generally attempt to establish performance criteria that were simple, clear, feasible, and appropriate in the light of the level of statistical

development in the country concerned. Furthermore, it might not always be possible to "ensure" accurate reporting, as stated in the sentence. Perhaps, "facilitate" would be a better term. Finally, with regard to the lapse of time period of at least ten days during which Executive Directors could ask that the matter be placed on the agenda of the Board, was it correct to assume that, if the case were placed on the agenda, Directors would be given the normal four weeks to consult with their authorities? If so, at what point would the four-week period begin?

The Secretary replied that the four-week period would not normally apply. The matter would be placed on the agenda of the Executive Board promptly--two weeks after circulation of the paper containing the Managing Director's recommendation. However, if the Director for the country concerned indicated that there were issues on which his authorities would need more time to prepare their case, existing procedures allowed the Board to grant the member the necessary time on the understanding that the subject should be placed on the agenda as soon as possible.

Mr. Leonard remarked that he was satisfied with the compromise embodied in the guidelines as drafted. He would have preferred an obligation to repurchase rather than an expectation, but paragraphs 5 and 6 provided useful reinforcement in that regard; they should be retained.

Mr. Blandin suggested that the period of two years during which a performance criterion or other condition was open to re-examination seemed somewhat long. A period of one year or 18 months would have been preferable. In paragraph 5, the reference to Article V, Section 5 of the Articles was unnecessary. It could be deleted without affecting the force of the remainder of the paragraph. He agreed with Mr. Jayawardena that paragraph 6 was also redundant. It appeared to cast doubt on the validity of the performance criteria or on the good faith of the member. In addition, paragraph 7 could be deleted; if there were evidence that inaccurate information had been provided deliberately and fraudulently, the Executive Board already had the power to proceed to take actions under Article XXVI, Section 2. Finally, although he would prefer to incorporate the changes that he had just suggested, he could accept the guidelines as drafted.

Ms. Bush commented that she would have preferred the guidelines to include an obligation to repurchase, instead of an expectation, but she could accept the latter. She agreed with Mr. Polak that it might be better to delete the second sentence in paragraph 3, which provided the option of use of a member's currency as an alternative to a repurchase. However, if there were not a consensus in the Board for that proposal, could the staff provide clarification that the period in which the repurchase ought to be made would be 30 days, not 50 days? The paragraph was not clear in that respect.

It was important that paragraph 6 be included in the guidelines because of the seriousness of the subject under discussion, Ms. Bush continued. In the six-monthly report on overdue financial obligations to the Fund (EBS/84/211, 10/11/84), to be discussed at the next two Board meetings (EBM/84/166 and EBM/84/167, 11/19/84), the staff suggested that there were occasions when a member might be in arrears to the Fund yet be able to make purchases under a stand-by arrangement, for example, if the Fund's holdings of that member's currency were less than 25 percent of quota. Would the procedure set out in paragraph 6 of the draft guidelines--that provision would be made in Fund arrangements for the suspension of purchases if a member had not repurchased as expected--apply in the case of overdue obligations?

Mr. Angeloni said that he could accept the proposed guidelines as a compromise solution. He wondered whether the guidelines, particularly paragraph 6, would apply to the special facilities and to other Fund arrangements.

Mr. Salehkhoul stated that he associated himself fully with the remarks by Mr. Jayawardena.

The Director of the Legal Department noted that provision was made in paragraph 3 that the option of use of the member's currency in lieu of a repurchase should be made within the first 20 days, in order to allow an additional 10 days for repurchase if it turned out that that option could not be used. Thus, the applicable period for a repurchase would remain 30 days. With regard to paragraph 6, the intent was to establish the principle that there would be a clause in Fund arrangements providing for the suspension of further purchases whenever a member failed to meet a repurchase expectation, corresponding to the clause that provided for suspension of purchases in cases of overdue obligations. Whether that proposal would apply to the first credit tranche under stand-by arrangements and to special facilities would depend on the outcome of the forthcoming Executive Board discussion of overdue obligations. It would not apply to purchases under the special facilities unless the Board decided otherwise. The staff would formulate specific wording of the relevant clause in the light of the Board's discussion of overdue obligations.

Mr. Kafka suggested that it would be better to postpone a decision to adopt the proposed guidelines until after the discussion of overdue obligations.

The Chairman remarked that paragraph 6 simply provided that there should be a clause in Fund arrangements to the effect that, if a member failed to meet a repurchase expectation, further purchases under the arrangement would be suspended. The question whether a country that had not met the expectation to repurchase could be suspended from drawing on the special facilities was a separate issue that could be considered by the Executive Board in due course.

The Director of the Legal Department added that there were a number of proposals in the paper on overdue obligations that were relevant to the subject under discussion. For example, one proposal in EBS/84/211 was that the suspension of purchases in cases of overdue obligations should be applicable to any purchase under a stand-by arrangement, not only to those above the first credit tranche. If the Executive Board agreed to that proposal, the relevant language putting that decision into effect in arrangements would be similar in the case of overdue obligations and in the case of failure to meet a repurchase expectation. However, it was not being proposed under the guidelines as drafted that failure to meet a repurchase expectation in relation to a noncomplying purchase would make a member ineligible to make purchases under the special facilities.

Mr. Kafka remarked that it appeared that a decision that the Executive Board might adopt on the question of overdue obligations could affect the meaning of paragraph 6 of the proposed guidelines. Therefore, a decision on those guidelines should be postponed until after the discussion of overdue obligations.

Ms. Bush asked whether it was correct to assume that under the proposed guidelines a repurchase expectation would not apply if the noncomplying purchase had been made in the first credit tranche.

The Director of the Legal Department replied that the intent of paragraph 6 was that similar principles would apply in the case of a repurchase expectation as in the case of overdue obligations. If the Executive Board agreed with the proposal that all purchases under a stand-by arrangement should be suspended in cases of overdue obligations--including purchases in the first credit tranche--the staff would draft a clause for insertion in Fund arrangements to put that decision into effect. It would also draft a similar clause in relation to repurchase expectations. However, if the Executive Board did not accept that proposal, the staff would draft the clause on repurchase expectations so that it would not apply to purchases in the first credit tranche under stand-by arrangements.

Mr. Kafka commented that it was an inappropriate drafting technique to have the meaning of one decision dependent on the meaning of another decision not yet taken. Furthermore, it appeared that the essential differences between an expectation to repurchase and an obligation were being eliminated, thereby threatening the compromise reached earlier by Executive Directors.

The Director of the Legal Department said that, as in the past, the staff would put before the Executive Board for its approval specific texts of the relevant clauses. However, the staff had not wished to assume that the Executive Board would wish to make different provisions for overdue obligations than for expectations. Paragraph 6 had been drafted with that consideration in mind, as explained in EBS/84/196. If the Board accepted the proposals in EBS/84/211, the clause in relation to obligations would be similar in scope to that covering expectations.

Mr. Wicks stated that the decision before Executive Directors--on misreporting and noncomplying purchases--stood on its own; the outcome of the Executive Board's discussion of overdue obligations should not be prejudged. The question of how a decision on overdue obligations might affect the decision on repurchase expectations should be considered in due course.

The Chairman said that he agreed with Mr. Wicks. If a member had mistakenly purchased under an arrangement with the Fund, that mistake had to be corrected, and if the expectation that it would be corrected was not met, the member would not be eligible to make further purchases under a stand-by or extended arrangement. That was the intent of paragraph 6. Whether the member would be precluded from making purchases in the first credit tranche was a separate issue and would depend on the outcome of the Executive Board's discussion of overdue obligations. However, in that discussion, Executive Directors could take into account all relevant considerations, including the decision--if it were adopted--before them at present.

Mr. Kafka remarked that he continued to believe that it would be better to postpone the decision before the Executive Board until after the discussion of overdue obligations, when the meaning of the decision would become clear.

Mr. Wicks commented that the meaning of the decision before the Executive Board was clear. If a decision on overdue obligations had implications for the decision on expectations, the Executive Board would undoubtedly bear that consideration in mind in its discussion of obligations. However, it could not be assumed beforehand that such implications would in fact exist.

Mr. Suraisry observed that paragraph 6 reflected agreement already reached in the Executive Board; in effect, it could have been embodied in a decision several weeks earlier. The relevance of a decision on overdue obligations to the decision on expectations was a matter that could be considered at the appropriate time, namely, in the discussion of overdue obligations.

Mr. Tvedt stated that he supported the proposed guidelines. He agreed with the view that noncomplying purchases should be dealt with within a period not exceeding two years from the date on which the purchases were made. If the period were significantly shorter than two years, it could hamper the effectiveness of the guidelines. He also supported the procedures set out in paragraphs 2 and 3.

Mr. Zhang said that he supported Mr. Jayawardena's remarks with respect to paragraph 6.

Mr. Schneider said that he could accept the proposed guidelines in a spirit of compromise. However, he agreed with the comments by Mr. Polak and Mr. Suraisry regarding the third sentence of the preamble. It would

be overoptimistic to expect that the Fund could "ensure" accurate reporting by taking certain measures. He also agreed with their comments on paragraph 2; the present wording was too strict and left little leeway to the Board in its actions. He shared the opinion of Mr. Jensen and Mr. Blandin that the two-year period referred to in paragraph 1 was on the long side; a period of one year or 18 months would have been preferable. Although he sympathized with Mr. Kafka's interpretation of paragraph 6, his own understanding was that the paragraph was intended to prevent further purchases under an arrangement in the event of a failure to meet a repurchase expectation, but to have no other implications. It would be preferable to take a decision on the matter at the present meeting and bear that decision in mind in the course of the discussion of overdue obligations. He had no strong preference as to whether paragraph 7 remained; the Board would always be free to take appropriate action within the Articles of Agreement and the Rules.

Mr. Tshishimbi remarked that, in the light of the comments of other Directors, he believed that it would be preferable to postpone a decision, particularly with regard to paragraph 6, until after the Executive Board discussion of overdue obligations, or at least to consider the two subjects together.

Mr. Angeloni said that he would prefer that the Board take a decision on the guidelines at the present meeting. The implications for purchases outside a stand-by or extended arrangement should be discussed in due course, although the discussion of overdue obligations might not be the most appropriate occasion to discuss purchases under the special facilities.

Ms. Bush stated that she agreed with those speakers who favored taking a decision on repurchase expectations at the present meeting; if a decision on overdue obligations had implications for that issue, the Executive Board might have to take up the question again at a later date.

Mr. Tshishimbi asked whether the effect of paragraph 6 of the proposed guidelines applied to purchases in the first credit tranche.

The Director of the Legal Department replied that the staff had drafted paragraph 6 in the context of current policy. The effect of the paragraph would be to include in Fund arrangements a clause providing for suspension of further purchases whenever a member failed to meet a repurchase expectation; the clause would be similar to that currently included in arrangements with respect to overdue obligations. If, however, the Executive Board decided at the conclusion of its discussion of overdue obligations to include purchases in the first credit tranche under a stand-by arrangement among the purchases that would be suspended in cases of overdue obligations, the staff would draft the clause referring to repurchase expectations in light of that decision.

The Chairman observed that the position was clear. Paragraph 6 of the proposed guidelines, as drafted, established the principle of how the Fund would act if a member failed to meet a repurchase expectation. The

precise wording of the clause giving effect to that principle in Fund arrangements would depend to an extent on the outcome of the Executive Board's decision with respect to overdue obligations. However, it was intended that the clauses on overdue obligations and on repurchase expectation should be similar in scope. Executive Directors could bear those considerations in mind in the course of their discussion of overdue obligations. At the present stage of the discussion, it might be useful to consider the draft decision on a paragraph-by-paragraph basis.

Preamble

Mr. Polak commented that the meaning of the paragraph would be clearer if that part of the third sentence beginning with the words "steps should also be taken..." became the penultimate sentence of the preamble, with the word "ensure" replaced by the word "facilitate." The opening phrase of the final sentence--"to this end"--could also be eliminated.

The Executive Directors agreed to the revised wording.

Paragraph 1

Mr. Wicks, Mr. Grosche, Mr. Suraisry, Mr. Angeloni, Mr. Tvedt, Mr. Yamashita, Mr. Polak, and Ms. Bush stated that they preferred a limitation period of two years.

Mr. Blandin, Mr. Schneider, Mr. Jensen, Mr. Finaish, and Mr. Kafka said that they preferred a period shorter than two years.

Mr. Tshishimbi, Mr. Pérez, Mr. Jayawardena, Mr. Zhang, Mr. Robalino, and Mr. Abdallah expressed support for a one-year period.

The Chairman noted that the sense of the meeting was in favor of two years.

Paragraph 2

The Chairman recalled that Mr. Jayawardena had suggested that at the end of the second sentence the words "to be approved by the Executive Board on a lapse of time basis" could be added, while Mr. Polak had preferred wording to the effect that the recommendations of the Managing Director should normally be submitted to the Board on a lapse of time basis.

Mr. Polak said that either variant was acceptable to him.

Mr. Leonard commented that Mr. Polak's formulation was preferable.

Mr. Jayawardena said that he could support Mr. Polak's formulation.

The Executive Directors agreed that the paragraph should be revised to reflect Mr. Polak's suggestion.

Paragraph 3

The Director of the Legal Department observed that, as Mr. Polak had remarked, the probability that a member would take up the option to use its currency in lieu of repurchase was quite low. However, there were circumstances in which it might be advantageous.

The Deputy Treasurer noted that the staff had drafted the paragraph to keep it in conformity with the guidelines for early repurchase agreed to in 1979, which contained the option that a member could reduce its liabilities through Fund use of its currency. Furthermore, on occasion, a member preferred for domestic reasons to take the initiative in reducing its holdings in the Fund through a sale of its currency rather than have the Fund ask it to reduce them through a repurchase. Finally, the option provided additional, albeit minor, flexibility to the Fund in managing its currency holdings, which might enhance Fund liquidity.

The Executive Directors agreed to retain paragraph 3 unchanged.

Paragraph 4

The Executive Directors agreed to retain paragraph 4 unchanged.

Paragraph 5

The Chairman recalled that Mr. Blandin had suggested that the words "in which he may recommend that the Fund initiate action under Article V, Section 5 of the Articles" should be deleted from the end of the paragraph.

Mr. Grosche, Mr. Leonard, Mr. Suraisry, Mr. Jayawardena, and Ms. Bush said that they preferred that the paragraph remain unchanged.

The Executive Directors agreed to retain paragraph 5 unchanged.

Paragraph 6

The Director of the Legal Department noted that Mr. Jayawardena had suggested that paragraph 6 could be deleted because the Fund already had the power under paragraph 5 of the standard text of stand-by arrangements to bring about the suspension of further purchases. However, there was an important difference between the action that could be taken under paragraph 5 of a stand-by arrangement and under paragraph 6 of the proposed guidelines. In the former case, a decision of the Executive Board was required, whereas, under the guidelines, suspension would be automatic.

The Executive Directors agreed to retain paragraph 6 unchanged.

Paragraph 7

The Director of the Legal Department commented that, as several Executive Directors had remarked, the paragraph was not strictly necessary from a legal point of view. Even if the paragraph were eliminated, the Executive Board would be free to take appropriate action under the Fund's Articles and Rules. However, the paragraph served the particular purpose of stressing that, in the unlikely case of deliberate misreporting, the adoption of the guidelines did not preclude the Fund from taking any action consistent with the Articles and Rules. There had been general agreement in the Board that cases of deliberate misreporting, if they arose, should be dealt with severely.

Mr. Polak remarked that he would prefer to retain the paragraph. If, for example, a case of deliberate misreporting were discovered more than two years after it had occurred, the Fund might wish to take certain actions. Similarly, although the guidelines were intended to apply to future cases of misreporting or noncomplying purchases, if a past case came to light that in the Executive Board's judgment required action, the paragraph would serve as a reminder that the Board was free to take appropriate action under the Articles.

The Executive Directors agreed to retain paragraph 7 unchanged.

The Chairman invited Directors to state their preferences on the question whether a decision to adopt the guidelines should be taken at the present meeting or should be postponed to a later meeting.

Mr. Kafka, Mr. Jayawardena, Mr. Salehkhrou, Mr. Jensen, and Mr. Pérez indicated that they would prefer to postpone the decision.

The Chairman observed that the sense of the meeting was in favor of a decision at the present meeting.

Mr. Jayawardena asked whether the proposed decision would in effect convert an expectation to repurchase into an obligation. If so, what was the nature of that obligation? Would such a decision require an 85 percent majority of the Board?

The Director of the Legal Department replied that the proposed decision would not convert an expectation to repurchase into an obligation. The decision, which would require a simple majority of votes cast, would establish a repurchase expectation with certain consequences arising from the understandings embodied in stand-by arrangements. If, however, "expectation" were replaced by "obligation," an 85 percent majority of the Executive Board would be required for adoption of the decision. Legally, an expectation differed from an obligation in a number of ways; for example, if a member failed to meet an expectation, the Fund could not take action against the member pursuant to Article XXVI, which applied only to cases of violation of obligations.

The Executive Board then took the following decision:

Misreporting and Noncomplying Purchases Under Fund
Arrangements - Guidelines on Corrective Action

In a few cases, it has been found that a member has made a purchase under a stand-by or extended arrangement which it was not entitled to make by the terms of the arrangement (a "noncomplying purchase"). The purchase was permitted because, on the basis of the information available to it at the time, the Fund was satisfied that all performance criteria that were applicable to the purchase under the arrangement, or other conditions applicable to purchases under the terms of the decisions on the arrangement, had been observed, but this information later proved to be incorrect. When such a case arises in the future, the member will be called upon to take corrective action regarding a noncomplying purchase, to the extent that it is still outstanding, either by repurchase or by the use of its currency in transactions and operations of the Fund, unless the Fund decides that the circumstances justify the member's continued use of the purchased resources. Steps should also be taken to improve the accuracy and completeness of the information to be reported to the Fund by the member under the arrangement and to define performance criteria and other applicable conditions in a manner that would facilitate accurate reporting. The Fund adopts the following guidelines, which shall apply to purchases made after the date of this decision:

1. Whenever evidence comes to the attention of the Fund indicating that a performance criterion or other condition applicable to an outstanding purchase made within the previous two years under a stand-by or extended arrangement may not have been observed, the Managing Director shall promptly inform the member concerned.
2. If, after consultation with the member, the Managing Director finds that, in fact, the criterion or condition was not observed, he shall promptly notify the member of his finding. At the same time, he shall submit a report to the Executive Board together with his recommendations, which may include a recommendation that the member be called upon to take corrective action pursuant to paragraph 3 or that the nonobservance be waived pursuant to paragraph 4. The recommendations of the Managing Director shall be submitted to the Executive Board on a lapse of time basis giving Executive Directors a period of at least ten days during which they could ask that the matter be placed on the agenda of the Executive Board for consideration.
3. Unless the decision of the Executive Board is to grant a waiver pursuant to paragraph 4 or to take other action, the member shall be expected to repurchase from the Fund the outstanding amount of its currency resulting from the noncomplying purchase normally within a period of 30 days from the date of the Executive Board decision

referred to in paragraph 2. Instead of repurchasing, the member may request the Fund to use an equivalent amount of its holdings of the member's currency in the Fund's transactions and operations, but if such use cannot be made within 20 days from the date of the Executive Board decision the member shall be expected to make a repurchase in accordance with this paragraph.

4. A waiver will normally be granted only if the deviation from the relevant performance criterion or other condition was minor or temporary, or if subsequent to the purchase the member had adopted additional policy measures appropriate to achieving the objectives of the program supported by the arrangement under which the purchase was made.

5. If a repurchase pursuant to the expectation under paragraph 3 has not been effected, the Managing Director shall submit promptly a report to the Executive Board accompanied by a proposal on how to deal with this matter, in which he may recommend that the Fund initiate action under Article V, Section 5 of the Articles.

6. Provision shall be made in Fund arrangements for the suspension of further purchases under an arrangement whenever a member fails to meet a repurchase expectation pursuant to these guidelines.

7. Nothing in these guidelines shall limit the power of the Fund to take, in case of noncomplying purchases, other action that could be taken pursuant to the Fund's Articles and Rules.

Decision No. 7842-(84/165), adopted
November 16, 1984

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board in the period between EBM/84/164 (11/9/84) and EBM/84/165 (11/16/84).

3. ARAB REPUBLIC OF EGYPT - TECHNICAL ASSISTANCE

In response to a request from the Egyptian authorities for technical assistance, the Executive Board approves the proposal set forth in EBD/84/285 (11/8/84).

Adopted November 9, 1984

4. APPROVAL OF MINUTES

a. The minutes of Executive Board Meetings 84/76 and 84/77 are approved.

Adopted November 14, 1984

b. The minutes of Executive Board Meetings 84/78 and 84/79 are approved.

Adopted November 15, 1984

5. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors as set forth in EBAP/84/241 (11/8/84) and EBAP/84/242 (11/9/84) is approved.

APPROVED: August 21, 1985

JOSEPH W. LANG, JR.
Acting Secretary

