FOR AGENDA



SM/83/194

August 19, 1983

To: Members of the Executive Board

From: The Acting Secretary

Subject: Review of the Policy on Access to the Fund's Resources - Legal and Policy Considerations

The attached paper on legal and policy considerations with respect to the review of the policy on access to the Fund's resources has been tentatively scheduled for Executive Board discussion on Wednesday, August 31, 1983.

Att: (1)

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Department Heads

INTERNATIONAL MONETARY FUND

# Review of the Policy on Access to the Fund's Resources - Legal and Policy Considerations

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August 19, 1983

## I. Introduction

1. In the discussion of the memoranda entitled "Review of the Policy on Access to the Fund's Resources - General Considerations" (EBS/83/132, and Correction 1 and Supplement 1), and "Review of the Policy on Access to the Fund's Resources - Financial Considerations" (EBS/83/133), at EBM 83/110 and 111, two proposals were made. The first proposal was that, if the Executive Board decided to reduce the access limits expressed in terms of the Eighth Review quotas, an individual member should not thereby have its present access limit reduced in terms of an absolute amount of SDRs. It was also proposed that if at some future time the access limits were reduced, the reduction should be applied also to the amounts remaining available under arrangements that had been granted prior to the effective date of the reduction. The two following sections discuss the legal aspects of these two proposals and some policy implications.

## II. Maintenance of Access Limits in Absolute Terms

1. The amounts of financial assistance that members are able to obtain from the Fund are determined on the basis of their current quotas. After the effective date of the quota increases under the Eighth Review, the access for all members would normally be determined on the basis of their increased quotas. The first proposition that no member's access limits be reduced in absolute terms would require limits on access that would represent different percentages of quota for different members.

2. The establishment of access limits is a basic policy decision of the Fund and must conform to the requirement of uniformity, which regulates the Fund's relations with its members. The policies of the Fund with respect to members' access to the Fund's resources have reflected the provisions of the Articles that used quotas as the basis for considering the amounts of resources to be made available to members. The original Articles required a waiver for a purchase that would increase the Fund's holdings of a member's currency beyond 25 percent of its quota in any twelve-month period (excluding purchases that only

brought the Fund's holdings up to seventy-five percent of quota), as well as a waiver for a purchase that would raise the Fund's holdings of a member's currency above 200 hundred percent of quota. The latter requirement is still in the Articles. The development of the Fund's policy on the use of its resources reflected these tranches first, in 1952 by adopting the policy that "each member can count on receiving the overwhelming benefit of any doubt respecting drawings which would raise the Fund's holdings of its currency to not more than its quota."1/ Later the general policy on the use of the Fund's resources in the credit tranches established the criteria by which the economic program of a member was to be judged based on the amount of the member's use of Fund resources in relation to the member's quota. 2/ The availability of, or access to, the facilities of the Fund designed to meet special balance of payments problems have been based on fixed percentages of members' quotas. 3/ A uniform access limit of 140 percent was adopted as the limit for arrangements under the Extended Fund Facility and the combined access limits for the use of ordinary and supplementary resources were set under the Supplementary Financing

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1/ Paragraph 3, Executive Board Decision No. 102-(52/11), adopted February 13, 1952.

2/ "The Fund's attitude to requests for transactions within the 'first credit tranche' ... is a liberal one, provided that the member itself is making reasonable efforts to solve its problems. Requests for transactions beyond these limits require substantial justification." See Selected Decisions, Ninth Issue, page 25.

3/ The Compensatory Financing Facility had an initial limit of 25 percent of quota (1963), then 50 percent (1966), 75 percent (1975), and 100 percent (1979). With the 1966 increase to 50 percent a limit was set of 25 percent in any 12-month period, raised to 50 percent in 1975 and abolished in 1979.

There was a joint limit of 75 percent on drawings under the CFF and the Bufferstock Facility (BSF) between 1969 when the BSF was established with a 50 percent limit, until 1975. Upon establishment of the CFF for fluctuations in cost of cereal imports in 1981 with a 100 percent limit another joint limit of 125 percent was introduced on drawings under this facility and the CFF. For a fuller description, see SM/83/131, and Correction 1 (6/16/83), "Compensatory Financing Facility and Bufferstock Financing Facility--Review of Experience with Financing of Fluctuations in the Cost of Cereal Imports and Selected Policy Issues", Annex I.

Under the oil facilities maximum access was determined as the smaller of two amounts namely: 75 percent of quota under the 1974 Facility, raised to 125 percent under the 1975 Facility, and an amount calculated on the basis of a formula taking mainly into account the increase in oil import cost (Executive Board Decision No. 4241-(74/67), adopted June 13, 1974, and Executive Board Decision No. 4634-(75/47), adopted April 4, 1975, as amended. Selected Decisions, Ninth Issue, pp. 69-77).

Facility at 202.5 percent for stand-by arrangements and 280 percent for extended arrangements.

3. While the policy to be adopted must provide for consideration of members' requests in terms of quotas as they exist, the adoption of access limits in terms of quotas does not mean that the Fund cannot grant greater access to a member that demonstrates a greater balance of payments need and presents a program that supports the greater use of resources. The authority to grant further access in particular cases was contained in the original Articles, which, as mentioned above, provided that both the 25 and the 200 percent limits could be waived when the Fund judged this action to be appropriate in the circumstances and against the considerations set forth in Article V, Section 4. 1/ In considering whether to grant a waiver the Fund must take into consideration, together with other aspects of the member's request, the exceptional requirements of the member.

4. Thus the requirement of uniformity of treatment of members does not mean and has not been understood to mean that all members be treated in exactly the same manner regardless of their different circumstances and needs. The Fund has taken account of different circumstances and permitted members with balance of payments difficulties arising from special problems that did not affect all members to make purchases to meet these special problems, as well as permitted members with balance of payments needs that were large in relation to their quotas to purchase amounts larger in relation to quota than otherwise might have been provided. This latter proposition is expressly recognized in paragraph 5(f) of the decision on the Supplementary Financing Facility, 2/ which provides, in special cases, for use of Fund resources in amounts above the access limits otherwise set forth in the provisions of the decision.

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1/ The present Article V, Section 4 states:

> "The Fund may in its discretion, and on terms which safeguard its interests, waive any of the conditions prescribed in Section 3(b)(iii) and (iv) of this Article, especially in the case of members with a record of avoiding large or continuous use of the Fund's general resources. In making a waiver it shall take into consideration periodic or exceptional requirements of the member requesting the waiver. The Fund shall also take into consideration a member's willingness to pledge as collateral security acceptable assets having a value sufficient in the opinion of the Fund to protect its interests and may require as a condition of waiver the pledge of such collateral security."

2/ Executive Board Decision No. 5508-(77/127), adopted August 29, 1977, Selected Decisions, Ninth Issue, pp. 31, 34.

5. While it would not be consistent with the principle of uniform treatment for the Fund to adopt a policy under which access limits in terms of new quotas would apply to one category of members, while access limits for others were determined on some other criterion, there would be no legal impediment to the adoption of a policy whereby the Fund would assure members of sympathetic consideration, on an individual basis, of their requests for use of the Fund's resources in excess of the established access limit if their requirements were exceptionally large and the requests were supported by appropriate measures and otherwise met the considerations of Article V, Section 4.

## III. Reduction in the Amount of Existing Stand-by and Extended Arrangements

1. The proposition that the Fund should decide that, in the event of a reduction of access limits, the amounts still to be purchased under existing stand-by and extended arrangements would be reduced accordingly must be viewed against a fundamental legal principle that has been observed by the Fund in all its decisions, i.e., the Fund cannot make changes in its decisions or rules if the change would have an adverse effect on the position of members that had relied on the previous decision or rules. In terms of this principle it would not be permissible for the Fund to reduce the specified amounts in existing arrangements unless notice of the possibility had been given in the decision granting the arrangement.

2. A similar application of this principle is familiar from the Fund's treatment of the changes in the rate of periodic charges. It was concluded long ago that the Fund cannot increase the rates in a schedule of periodic charges to be levied on outstanding balances of currency above the rates in existence when the purchases were made, unless the member is on notice at the time of the purchase that the rate of charge that will be levied may be changed from time to time. In order to permit future changes in the rates of charge on the Fund's holdings of members' currencies to apply to outstanding balances the Fund had to take a decision that such changes, including increases, would apply to existing holdings if the holdings were obtained by the Fund after the date of the decision that future changes shall so apply (Executive Board Decision No. 4239-(74/67), June 30, 1974, Selected Decisions, Ninth Issue, page 99).

3. The proposal to make a reduction in access limits applicable to amounts available under arrangements in existence when the decision is taken would not be inconsistent with the legal principle referred to if members had been given appropriate notice that such a change would be made applicable to the amounts under the arrangement.

4. The Fund is expected under Article V, Section 3(a) 1/, to adopt policies on the use of the general resources, including policies on stand-by and similar arrangements. The term "stand-by arrangement" is included among the concepts explained in Article XXX, which states:

> "In interpreting the provisions of this Agreement the Fund and its members shall be guided by the following provisions:
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> '(b) Stand-by arrangement means a decision of the Fund by which a member is assured that it will be able to make purchases from the General Resources Account in accordance with the terms of the decision during a specified period and up to a specified amount.'"

5. The appropriate form of notice would thus appear to be a statement in each decision granting the arrangement that the amount specified would be reduced in accordance with any new decision on access limits. Thus, the policy on stand-by and other arrangements would establish as one of the "terms of the decision" granting the arrangement that any reduction in the amounts available to members under a future change in the policy on access limits would be applicable to and govern the extent that the member may make purchases under the arrangement.

6. It is of interest in this connection to recall that stand-by decisions at one time contained what was called a "prior notice clause" in addition to the other type of protective clause formulated as performance criteria. Under the "prior notice clause" a member's right to make further purchases under the arrangement could be interrupted if, pursuant to a decision of the Executive Board, the Fund gave the member notice to that effect. The criteria for such notices were not usually made explicit although it had been tacitly assumed that they were

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1/ Article V, Section 3(a) states:

> "The Fund shall adopt policies on the use of its general resources, including policies on stand-by or similar arrangements, and may adopt special policies for special balance of payments problems, that will assist members to solve their balance of payments problems in a manner consistent with the provisions of this Agreement and that will establish adequate safeguards for the temporary use of the general resources of the Fund."

the observance of the policies and intentions that had prompted the Fund to grant the stand-by arrangement. The clause came under criticism on the grounds that it was not incorporated in all decisions but also because of the uncertainty created by the lack of clarity as to the circumstances in which it would be invoked. The proposal to include a clause to the effect that the amounts initially made available may be reduced by subsequent decisions of the Executive Board might be seen as reintroducing a similar uncertainty, a consideration discussed further below.

7. In addition to the correct legal formulation of such a provision, policy decisions would have to be made for its application. These policy decisions would need to encompass, as a minimum, guidance with respect to the timing and extent of any reduction that would be made to the initial amounts available under the arrangements. In principle, any reduction would have to apply to all existing arrangements under which amounts could still be purchased and inevitably problems of application will arise, in part because of the considerable variation in the length of existing arrangements. One procedure would be to bring the total amount of any arrangement exceeding the new limits down to those limits by reducing the amounts available in the present and future years. This procedure would, of course, have the disadvantage of affecting all large arrangements regardless of how long they had been in effect and how much had already been drawn: it might also result in the elimination of further purchases well before the scheduled end of the arrangement. Another procedure that would reduce the undrawn amounts of all arrangements on a given date by a specified percentage, while uniform with respect to the amounts outstanding as available under the arrangements, could result in reductions that would be inconsistent with the uniform application of new cumulative access limits and would reduce the yearly amounts regardless of whether these amounts were near the limits or not. Another possible approach would be to attempt to develop some standards that could be used to determine, on a case by case basis, how much the available amounts should be reduced. Thus, for example, the type of principles that might be applied might be the prospective balance of payments need, reliance on the program amount for other financing, or that purchases would not be reduced below repurchases during the remaining life of the arrangement. But even though standards could be devised to take account of specific problems, it is questionable whether the application of the standards would appear to be equitable in all cases.

8. In addition to problems of application, an important policy issue needs to be considered. Current practice has been based on a principle that the Fund would make a firm commitment of a stated amount of resources if the policies of the member were sufficient to warrant financial support. This understanding is not only part of the process of negotiation, but it also affects the relationship between the degree

of adjustment and the extent of financing of an imbalance. These principles have been followed in the past with changes in the policy on access limits, even though all of them involved the potential of absolute increases. To date, all such increases or augmentations of Fund resources have been submitted to the Board on an individual basis so that the consistency of the adjustment program with the newly available financing could be assessed. A new provision in favor of automatic and across-the-board variations in the amount of available Fund resources without review of the policies and circumstances of the member would break with this past policy. A related aspect of possible adjustments to the amount of Fund financing in the context of multi-year arrangements is discussed in the forthcoming paper reviewing conditionality.

9. In summary, the proposal to apply any future policy decision under which a reduction in access limits is to be applied to amounts available under outstanding stand-by and extended arrangements may and can be accomplished by including in the decisions granting the respective arrangements a provision to that effect. But the staff doubts the appropriateness of such an action in view of its consequences for the balance required between adjustment and financing.