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ATTENTION**

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SM/89/12

January 18, 1989

To: Members of the Executive Board

From: The Secretary

Subject: Multilateral Investment Guarantee Agency (MIGA) - Designation
of Managing Director to Appoint Person to Determine Reference
Rate of Exchange

It is not proposed to bring the attached memorandum to the agenda of the Executive Board for discussion unless an Executive Director so requests by the close of business on Tuesday, January 24, 1989. In the absence of such a request, the draft decision that appears on pages 1 and 2 will be deemed approved by the Executive Board and it will be so recorded in the minutes of the next meeting thereafter.

Mr. Brau (ext. 7854) or Mr. Francotte (ext. 7798) is available to answer technical or factual questions relating to this paper.

Att: (1)

Other Distribution:
Department Heads

INTERNATIONAL MONETARY FUND

Multilateral Investment Guarantee Agency - Designation of Managing
Director to Appoint Person to Determine Reference Rate of Exchange

Prepared by the Exchange and Trade Relations Department
and the Legal Department

Approved by L. A. Whittome and François Gianviti

January 18, 1989

In the annexed letter dated January 13, 1989 (Annex I), the Acting Executive Vice President of the Multilateral Investment Guarantee Agency (MIGA) requests that the Managing Director accept the role of appointing, if the need were to arise, an expert to determine a "reference rate of exchange" under the General Conditions of Guarantee for Equity Investments of MIGA. A draft of these General Conditions has been circulated to MIGA's Board of Directors for approval at a meeting of the Board of Directors scheduled for January 25, 1989.

Article 16 of these draft General Conditions (Annex II) establishes a reference rate of exchange for purposes of converting the local currency of an investment's host country into freely usable currency to determine the amount of compensation to be paid by MIGA to an insured investor in the event of a covered loss. This Article stipulates criteria on the basis of which MIGA and the insured investor shall determine the reference rate of exchange and contemplates that if they fail to agree on the rate, such rate shall be determined by an expert.

It is the role of appointing this expert, if the need arose, that the Managing Director is asked to accept. The acceptance of such a role would be consistent with past practice as well as with the guidance of the Executive Board on the performance of good offices by the Managing Director. 1/ It is therefore recommended that the Executive Board authorize the Managing Director to accept this role, acting in his official capacity.

Accordingly, the following draft decision is proposed for adoption by the Executive Board:

"The Executive Board approves the letter, set out in the Attachment to SM/89/12, from the Managing Director to the Acting

1/ See "The Role of the Fund in the Settlement of Disputes Between Members Relating to External Financial Obligations" SM/84/89 (4/25/84) and the Acting Chairman's Summing Up at EBM/84/99, 6/22/84, Buff 84/107, 7/13/84.

Executive Vice President of the Multilateral Investment Guarantee Agency, stating that the Managing Director has been authorized to appoint an expert to determine the reference rate of exchange in the circumstances described in Article 16 of the draft General Conditions of Guarantee for Equity Investments set out in Annex II of SM/89/12."

Dear Mr. Hollywood,

I refer to your letter dated January 13, 1989 pertaining to the determination of a reference rate of exchange under Article 16 of the General Conditions of Guarantee for Equity Investments of the Multilateral Investment Guarantee Agency.

I am pleased to inform you that the Executive Board of the International Monetary Fund has authorized the Managing Director to appoint an expert to determine the reference rate of exchange in the circumstances described in Article 16 of the draft General Conditions of Guarantee for Equity Investments.

Sincerely yours,

M. Camdessus

Mr. Leigh Hollywood
Acting Executive Vice President
Multilateral Investment Guarantee Agency
Washington, D.C. 20433

MULTILATERAL INVESTMENT GUARANTEE AGENCY
O F F I C E M E M O R A N D U M

DATE: January 13, 1989

TO: Mr. Michel Camdessus, Managing Director, IMF

FROM: /S/ Leigh Hollywood, Acting Executive Vice President, MIGA

EXTENSION: 36168

SUBJECT: MIGA: Reference Rate of Exchange

The Multilateral Investment Guarantee Agency (MIGA) was recently established under the auspices of the World Bank to insure direct investments in developing countries against non-commercial risks. The respective rights and obligations of MIGA and insured investors will be set out in the General Conditions of Guarantee the draft of which awaits the approval of MIGA's Board of Directors at its meeting on January 25, 1989.

Article 16 of the said General Conditions establishes a reference rate of exchange for the purpose of converting local currency of an investment's host country into freely usable currency in the context of determining the amount of compensation which MIGA may pay to an insured investor. To avoid arbitration in case of disagreement between MIGA and an insured investor on the applicable exchange rate, it is provided that the rate be determined by an independent expert designated by an impartial authority at either party's request.

In view of the Fund's authority and expertise in this area it would appear most appropriate if its Managing Director acted as designatory authority. I, therefore, request your advice whether you would kindly be prepared to assume this role.

I should note that the Managing Director's authority would be based on a contractual agreement between MIGA and its insured investors and that the Managing Director would in no case have to take a position in a dispute between MIGA and an insured investor. Also, instances where the Managing Director would be called upon can be expected to occur extremely infrequently, if at all.

Attached is the text of Article 16 of MIGA'S General Conditions, as revised with the benefit of advice from the Fund's Legal Department. The provision establishing the Managing Director's designatory authority is underlined.

Your cooperation on this matter is appreciated.

Attachment

Article 16. Reference Rate of Exchange

16.1 Under this Chapter, all conversions of Local Currency into Guarantee Currency shall be made on the basis of the Reference Rate of Exchange. Subject to Sections 16.2 through 16.4 below, such rate shall be the effective average rate of exchange applied by the central bank or other foreign exchange regulatory authority of the Host Country (hereinafter referred to as the "central bank") for the exchange rate category concerned on the Date of Loss to conversion of the Local Currency into Guarantee Currency.

16.2 If on the Date of Loss the central bank has not freely executed conversions into the Guarantee Currency or has applied multiple exchange rate categories with respect to such conversions, the Reference Rate of Exchange shall be computed on the basis of one of the following exchange rate categories for the conversion of Local Currency into Guarantee Currency in the following order of priority:

- (a) first, the exchange rate category generally applied by the central bank on the Date of Loss to earnings remitted on account of foreign equity investments;
- (b) second, the exchange rate category generally applied by the central bank on the Date of Loss for purposes of servicing private foreign debt;
- (c) third, the most depreciated (that is, requiring the greatest amount of Local Currency per Guarantee Currency unit) exchange rate category applied by the central bank on the Date of Loss for the sale of Guarantee Currency monies to private residents of the Host Country;

- (d) fourth, the most representative clearing rate on the Date of Loss legally used by commercial banks or any other private market in the Host Country; and
- (e) fifth, the clearing rate used on the Date of Loss outside the Host Country in the most active market for conversion of Local Currency into the Guarantee Currency.

16.3 If MIGA is unable to determine the Reference Rate of Exchange according to the above-mentioned method or the Guarantee Holder objects within thirty days of his notification to the determination made by MIGA, the Reference Rate of Exchange shall, with the approval of the Guarantee Holder, be determined by applying Section 16.2 to any freely usable currency other than the Guarantee Currency. If no such approval is obtained by MIGA within thirty days from the date of its request, either party may request the Managing Director of the International Monetary Fund to designate an expert to make a final decision on the applicable Reference Rate of Exchange. The cost of determining the Reference Rate of Exchange by such expert shall be equally shared by the parties.

16.4 For the purposes of this Article, the Reference Rate of Exchange shall represent the average of the high and low for the applicable exchange rate category on the Date of Loss. Any payment by MIGA shall be computed net of all charges and expenses due in case of conversions and transfers by or on behalf of the Guarantee Holder under the prevailing laws, regulations and business practices of the host country.

16.5 The provisions of this Article for the conversion of Local Currency into Guarantee Currency shall be applied mutatis mutandis to any other conversion of one currency into another for the purposes of the Contract.