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December 2, 1996

To: Members of the Executive Board

From: The Associate Secretary

Subject: **Special Allocation of SDRs - Draft of the Fourth Amendment
of the Articles of Agreement**

Attached for consideration by the Executive Directors is a paper on special allocation of SDRs - draft of the fourth amendment of the Articles of Agreement, which is tentatively scheduled for discussion on Wednesday, December 18, 1996.

Mr. Gianviti (ext. 38329) or Mr. Hagan (ext. 37715) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

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INTERNATIONAL MONETARY FUND

**Special Allocation of SDRs - Draft of the
Fourth Amendment of the Articles of Agreement**

Prepared by the Legal Department
(In consultation with the Research, Treasurer's, and
Policy Development and Review Departments)

Approved by François Gianviti

November 27, 1996

The Interim Committee, in its September 27, 1996 Communique, welcomed the Executive Board's consensus that all members should receive an equitable share of cumulative SDR allocations through an amendment of the Fund's Articles that would provide for a one-time allocation of SDRs, based on a common benchmark ratio of cumulative allocations to present quotas. In addition to endorsing this approach, the Interim Committee requested the Executive Board to finalize its work on the amendment by the time of the Committee's next meeting. It also emphasized that such an amendment of the Articles would not in any way affect the Fund's existing power to allocate SDRs on the basis of a finding of a long-term global need to supplement reserves as and when that need arises.

Attached to this paper is a draft amendment that would provide for the one-time allocation that has been endorsed by the Executive Board and the Interim Committee.^{1/} Set forth below is a description of the features of the draft amendment. This description could serve as the basis of the text of the Executive Board's report that will accompany the proposed resolution to be transmitted to the Board of Governors. As in the past, the Executive Board's report to the Board of Governors would become the official commentary of the amendment.

A. Categories of Recipients

1. Existing Participants

(a) The amount of SDRs that will be allocated to existing participants under the amendment will be an amount that will raise their net cumulative allocations to a level corresponding to a specified benchmark ratio. The level of the benchmark ratio, which has not

^{1/} The text of the draft amendment is derived, in large part, from the draft amendment that was prepared in the context of the discussion of an amendment based on the "Method III" approach, which utilizes a common benchmark; see SM/94/216 (8/10/94).

yet been agreed upon, will determine which existing participants will be eligible to receive a special allocation and the overall size of the special allocation to these participants.

(b) As stated by the Interim Committee in its Communique, the amount to be allocated will be calculated by applying the benchmark ratio to the present quota of each existing participant. Accordingly, the "specified date" to be used for calculation purposes will be a date chosen by the Executive Board that is not later than the date of the transmittal of the proposed amendment resolution to the Board of Governors. The application of the benchmark ratio to quotas as of the specified date has the effect that changes in net cumulative allocations or quotas after the specified date will not affect the size of the special allocation.

(c) For members that continue to have overdue obligations to the General Resources Account as of the specified date and, accordingly, are unable to consent to and pay for their increases in quota under the Ninth General Review by that time, the draft provides that the ratio would be applied to their quotas under the Eighth General Review since those would be the quotas in effect as of the specified date. Alternatively, the draft text could be revised to provide that the benchmark ratio for members in arrears will be applied to their proposed Ninth Review quotas rather than their actual quotas under the Eighth Review.

(e) Each existing participant will receive its special allocation 30 days following the effective date of the amendment unless it has notified the Fund of its desire not to receive the special allocation.

2. Future Participants

The draft amendment also makes provision for special allocations to countries that become members of the Fund and participants in the SDR Department after the specified date ("future participants"). Given the rationale of the amendment, which is, for equity reasons, to allow new participants to "catch up" with prior allocations, future participants could expect to receive the same benefit with respect to allocations made prior to the date of their membership in the Fund.

Regarding the calculation of the amount to be received by future participants, the following should be noted:

(a) The basis for determining the amount to be allocated to future participants has not yet been discussed in detail by the Executive Board. The draft amendment sets forth a formula that attempts to achieve, to the extent possible, comparability of treatment between existing participants and future participants. Specifically, the amendment will give a future participant the opportunity to "catch up" with general allocations made after the specified date but before the date of its participation. Conversely, if there has been a general increase in quotas between the effective date of the amendment and the date of participation of the future participant, the amendment will ensure that the new participant will not receive the unfair advantage of receiving its allocation on the basis of a quota that is larger than what it would

have been had it become a participant prior to the specified date.^{2/} In light of the foregoing, a future participant will receive a special allocation that will result in its ratio of net cumulative allocation-to-quota being equal to the benchmark ratio applied to existing participants, as adjusted (i) downwards, in proportion to the change in the total quotas of existing participants that has occurred since the specified date ^{3/} and (ii) upwards, in proportion to the change in the total net cumulative allocations of existing participants that are attributable to general allocations made after the specified date. ^{4/}

(b) Future participants would receive a special allocation on the 30th day following the later of: (i) the date of their participation or (ii) the effective date of the fourth amendment, unless they notify the Fund of their desire not to receive the allocation.

3. The Federal Republic of Yugoslavia (Serbia/Montenegro)

If, by the specified date, the Federal Republic of Yugoslavia (Serbia/Montenegro) (the "FRY") fulfills the conditions of membership set forth in the decision of the Executive Board dated December 14, 1992, it will be eligible to receive a special allocation as an existing participant. If, however, it fulfills these conditions after the specified date, it will not be eligible to receive an allocation as a future participant because, upon meeting these conditions, it will have succeeded retroactively to the former Socialist Federal Republic of Yugoslavia's (the "SFRY") membership in the Fund and participation in the SDR Department, along with the four other successor states of the SFRY. Accordingly, in the event that the FRY had not

^{2/} In principle, such an adjustment is similar to the one that may be made in the context of a general allocation to a participant that joined the SDR Department after the commencement of the basic period in which the allocation is being made. In circumstances where there had been a general quota increase after the general allocation decision but before the date of membership of the new participant, the legislative history of Article XVIII, Section 2(d) reveals that the amount allocated to the new participant would be based on a notional quota that would be equal to the quota which the member would have received had there been no general quota increase in the interim.

^{3/} Changes arising from: (i) the additional quotas of new members and (ii) increases of quotas under the Ninth Review that enter into effect after the specified date, will not cause an adjustment.

^{4/} The category of existing participants that would be used for purposes of determining the adjustment to be made would be limited to existing participants that have decided to receive all allocations made by the Fund since the specified date. This would ensure that a future participant would not be adversely affected by a decision taken by an existing participant to opt out of a allocation (which would reduce the amount by which the total of net cumulative allocations of participants would have otherwise increased and, accordingly, would also reduce the extent of the upwards adjustment).

become a participant of the SDR Department by the specified date, the text of the amendment would include a provision that would enable the FRY to also receive a special allocation once it becomes a participant, calculated on the same basis as that applicable to future participants. 5/

B. General Features

1. The special allocation made pursuant to the amendment will not be made on the basis of a finding of "long term global need". Rather, a sentence will be added to Article XV to provide for a one-time allocation of SDRs to existing and future participants in accordance with the provisions of Schedule M.
2. The one-time special allocation will not in any way affect the Fund's existing power to allocate SDRs on the basis of a finding of "long term global need" in accordance with Article XVIII. The text of Article XVIII will not be modified. Moreover, a specific reference will be added to the first sentence of Article XV for the purpose of emphasizing that allocations made on the basis of "long term global need" will continue to be made exclusively in accordance with the provisions of Article XVIII.
3. Participants will receive only one allocation under the amendment. Accordingly, the amendment will not establish a permanent mechanism for periodic harmonization of cumulative net allocation-to-quota ratios.
4. Unlike Article XVIII, the special allocation provision will operate without the necessity of a decision by an organ of the Fund; conversely, an organ of the Fund will have no authority to modify the operation of the provision. 6/
5. The characteristics of SDRs allocated pursuant to a special allocation will be the same as those of SDRs allocated under Article XVIII. For operational purposes, therefore, SDRs received from a special allocation will not be distinguished from those received under general allocations. For example, the allocation received by a participant pursuant to the amendment will be taken into consideration for purposes of calculating the acceptance limits under

5/ If the quota of the FRY is increased pursuant to the Ninth General Review on the same day that the Fund determines that the FRY has satisfied all of the conditions for membership in the Fund and participation in the SDR Department, the quota of the FRY to be used for purposes of calculating the amount of SDRs it would receive under the proposed amendment would be its quota under the Ninth General Review.

6/ However, the general provisions on the liquidation of the SDR Department will apply: allocations made under the amendment will be suspended if the Executive Board decides that the liquidation of the SDR Department may be necessary and will cease after a decision of the Board of Governors to liquidate the SDR Department or the Fund.

Article XIX, Section 4; i.e., the limits with respect to the amount of currency which this participant would have to provide if it were designated pursuant to Article XIX, Section 5. Similarly, if a reconstitution requirement were introduced, it would apply to all SDR allocations, whether special or general.

6. The amendment will also be without prejudice to the application of Article XVIII, Section 2(d), which sets forth the rules regarding the receipt of regular allocations by members that become participants after the commencement of a basic period. Under that provision, the Fund may authorize a new participant to receive regular allocations made during the remainder of the basic period. ^{7/} Accordingly, if a future member becomes a participant during a basic period when allocations are being made, it may be authorized to receive a regular allocation in addition to its special allocation.

^{7/} A member that becomes a participant after the commencement of a basic period during which regular allocations are being made may receive such allocations during the remainder of the period only if the Fund so decides. In the past, the Fund has always authorized the receipt of allocations in these cases.

Draft of the Proposed Fourth Amendment

1. The text of Article XV, Section 1 shall be amended to read as follows:
 - (a) To meet the need, as and when it arises, for a supplement to existing reserve assets, the Fund is authorized to allocate special drawing rights in accordance with the provisions of Article XVIII to members that are participants in the Special Drawing Rights Department.
 - (b) In addition, the Fund shall allocate special drawing rights to members that are participants in the Special Drawing Rights Department in accordance with the provisions of Schedule M.
2. A new Schedule M shall be added to the Articles, to read as follows:

SCHEDULE M

Special Allocations of Special Drawing Rights

1. Subject to 5 below, each member that, as of [specified date], is a participant in the Special Drawing Rights Department [and has a net cumulative allocation of special drawing rights that is less than [] percent of its quota]^{8/} shall, on the 30th day following the effective date of the fourth amendment of this Agreement, receive an allocation of special drawing rights in an amount that will result in its net cumulative allocation of special drawing rights being equal to [] percent of its quota as of [specified date].
2. Subject to 5 below, each country that becomes a member of the Fund and a participant in the Special Drawing Rights Department after [specified date] shall receive an allocation of special drawing rights in an amount calculated in accordance with 4 below on the 30th day following the later of: (i) the date on which the new member becomes a participant in the Special Drawing Rights Department, or (ii) the effective date of the fourth amendment of this Agreement.
- [3. Subject to 5 below, if the Federal Republic of Yugoslavia (Serbia/Montenegro) succeeds to the membership in the Fund and the participation in the Special Drawing Rights Department of the former Socialist Federal Republic of Yugoslavia in accordance with the terms and conditions of the decision of the Fund dated December 14, 1992, it shall receive an allocation of special drawing rights in an amount calculated in accordance with 4 below on the 30th day following the later of: (i) the date on which the Fund determines that the Federal Republic of Yugoslavia (Serbia/Montenegro) has met all of the terms and conditions of the

^{8/} The square-bracketed language will be eliminated if the benchmark is sufficiently high to ensure that all existing participants will receive a special allocation.

decision of the Fund dated December 14, 1992, or (ii) the effective date of the fourth amendment of this Agreement.]^{9/}

4. (a) For the purposes of 2 and 3 above, each participant shall receive an amount of special drawing rights that will result in such participant's ratio of net cumulative allocation to quota being equal to [] percent of its quota as of the date determined under (c) below, as adjusted:

(i) first, by multiplying [] percent by the ratio of the total of quotas as of [specified date] of the participants described in (b) below to the total of quotas of such participants as of the date determined under (c) below, excluding amounts attributable to increases in quotas after [specified date] under decisions of the Fund adopted before [specified date], and

(ii) second, by multiplying the product of (i) above by the ratio of the total of the sum of the net cumulative allocations of special drawing rights received under Article XVIII of the participants described in (b) below as of the date determined under (c) below and the allocations received by such participants under 1 above to the total of the sum of the net cumulative allocations of special drawing rights received under Article XVIII of such participants as of [specified date] and the allocations received by such participants under 1 above.

(b) For the purposes of the adjustments to be made under (a) above, the participants in the Special Drawing Rights Department shall be those participants that [(i) have ratios of net cumulative allocation to quota that are equal to or less than [] percent as of [specified date]]^{10/}, (ii) continue to be participants in the Special Drawing Rights Department as of the date determined under (c) below, and (iii) have received all allocations made by the Fund after [specified date].

(c) Except as otherwise specified in (a) and (b) above,

[(i)] calculations made for the purposes of 2 above shall be made on the basis of the net cumulative allocations and quotas in existence as of the date on which the member becomes a participant in the Special Drawing Rights Department, [and]

[(ii)] calculations made for the purposes of 3 above shall be made on the basis of the net cumulative allocations and quotas in existence as of the date on which the

^{9/} This square-bracketed paragraph will be eliminated if the Fund determines that the Federal Republic of Yugoslavia (Serbia/Montenegro) has met the conditions of membership in the Fund and participation in the SDR Department prior to the specified date.

^{10/} The square-bracketed language will be eliminated if the benchmark is at least as high as the highest net cumulative allocation to quota ratio currently in existence.

Fund determines that the Federal Republic of Yugoslavia (Serbia/Montenegro) has met all of the terms and conditions specified in the decision of December 14, 1992 of the Fund.]^{11/}

5. The Fund shall not allocate special drawing rights under this Schedule to those participants that have notified the Fund in writing prior to the date of the allocation of their desire not to receive the allocation.

^{11/} This square bracketed paragraph will only be necessary if, by the specified date, the Fund has not determined that the Federal Republic of Yugoslavia (Serbia/Montenegro) has met the conditions for membership in the Fund and participation in the Special Drawing Rights Department.