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INTERNATIONAL MONETARY FUND

FILES

Minutes of Executive Board Meeting 74/36

3:00 p.m., April 19, 1974

W. B. Dale, Acting Chairman

Executive Directors	Alternate Executive Directors
	C. P. Caranicas
	K. J. M. Andreassen
L. B. Brand	R. van S. Smit
R. Bryce	G. Reynolds
	F. García-Palacios, Temporary
	C. R. Harley
J. de Groote	H. G. Schneider
N. Deif	
	B. Martins
K. Kawaguchi	M. Wakatsuki
B. Kharmawan	
P. Lieftinck	
C. Massad A.	
	H. R. Monday
F. Palamenghi-Crispi	
P. S. N. Prasad	W. M. Tilakaratna
A. K. Rawlinson	P. J. Bull
G. Schleiminger	L. Fuenfgelt
	C. Beaurain
	M. S. Nan Nguema, Temporary

R. V. Anderson, Acting Secretary
J. A. Kay, Assistant

Also Present

European Department: E. Gürgen. Legal Department: J. Gold, General Counsel and Director; A. S. Gerstein, Deputy General Counsel; P. R. Lachman, A. Liuksila, S. A. Silard. Research Department: J. J. Polak, Economic Counsellor and Director; J. M. Fleming, Deputy Director; J. H. Williamson. Secretary's Department: N. K. Humphreys. Treasurer's Department: W. O. Habermeier, Treasurer; R. J. Familton, Deputy Treasurer; R. H. Miller, G. Wittich. Bureau of Language Services: J. S. Haszard, Director. Special Advisor to the Managing Director: F. A. Southard. Information Office: H. M. Koelle. Personal Assistant to the Managing Director: A. D. Crockett. Advisors to Executive Directors: M. Shein, J. B. Zulu. Technical Assistants to Executive Directors: C. J. Batliwalla, D. C. Chessell, J. C. Coleman, J. A. H. de Beaufort Wijnholds, B. P. Eap, M. Garadaghipour, G. E. Heyden Q., V. N. Mudaliar, A. K. Mullei, A. Pipino, Z. Porath, F. Saccomanni, W. Sanner, T. P. Sweeney, A. Takahashi, J. R. Vallet, J. M. G. Vanormelingen, M. A. Wasfy.

1. POSSIBLE CHANGES IN THE GENERAL ACCOUNT

The Executive Directors continued from the previous meeting (EBM/74/35, 4/19/74) their discussion of a staff memorandum on possible changes in the General Account (SM/74/72, 4/3/74).

Mr. Rawlinson said that he welcomed both the staff memorandum and its form. It was a useful survey of various ideas that could reasonably be considered. He regretted that he was in a different camp from Mr. Beaurain, but his authorities favored amending the Articles as part of the interim reform that it was hoped would be completed by summer 1974. He therefore supported the suggestion made by Mr. Kafka, and by others, that there should be active drafting of a legal kind on at least certain of the points set out in the paper. His authorities did not advocate amending the Articles for the pleasure of doing so; but it was clear to them that the Articles in their present form were out of date at a number of points, and that it would clearly be advantageous to amend at least those Articles that were incompatible with present and prospective practice. It might be useful, when the Executive Directors came to discuss the matter again, if the staff would distinguish those actions that were urgent and necessary to put right disorders that were immediately evident, from those that were more in the nature of improvements that could be made some time in the future.

Turning to specific matters, Mr. Rawlinson said that in general terms his authorities supported the staff proposals in relation to a General Account based on special drawing rights. It might be better not to force members to accept special drawing rights too hastily. While his own authorities were prepared to move forward rapidly toward acceptance of special drawing rights, they understood that others had reservations to which some attention should be paid. Member countries should be able to use special drawing rights in repurchases as a right, but his authorities were not so certain that it was necessary for the Fund to have the power to include special drawing rights in drawings without the agreement of the drawing country. At the present stage, they would prefer to continue with the arrangement by which special drawing rights could be used by mutual agreement. They were also in favor of permitting the use of special drawing rights in fulfillment of subscription payments and charges.

Section II of the staff paper (SM/74/72), dealing with gold, raised a number of issues which were, to some extent, being discussed elsewhere, Mr. Rawlinson commented. Nevertheless, his authorities would agree, subject to the discussion in the Committee of Twenty and in other bodies, with the idea of making it permissible for the Fund to sell gold and to invest the proceeds. Such an arrangement might, however, have to come as part of a wider solution to the general problem of gold. In addition, his authorities believed that the maintenance of value provisions in the Articles should be separated from the provisions on gold, so that any changes that might be implemented in the arrangements for gold should not be complicated by having legal consequences in connection with maintenance of value. In Section III, his authorities agreed with the subsections on stand-by arrangements and quantitative limits. In subsection 3 there was an ambiguity which his authorities would like to have cleared up. The subsection read as if it was intended to suggest that the Fund might have powers to specify the currencies to be included in a drawing without consulting either the drawing country or, more importantly, those whose currencies were to be used. His authorities assumed that there was no intent to use currencies in drawings against the wishes of members, but rather that discussions and consultations on a currency budget would continue as in the past. They would, however, like confirmation of that point. He himself also shared some of the misgivings expressed by Mr. Massad about the expression "its reserve currency," which seemed rather difficult.

In Section IV, Mr. Rawlinson explained, his authorities supported the idea of simplifying the repurchase procedures. In Section V, his authorities were rather troubled by the suggestion that a charge should be introduced for gold tranche drawings. While such a proposal might clearly have certain attractions for the management of the Fund, his authorities were not in favor of any action that might seem to prejudice the principle of unimpeded drawings from the gold tranche, or that might call in question the established practice in many countries of treating a gold tranche provision as part of their own reserves. Finally, regarding Section VI, his authorities favored the idea of the Fund having powers to invest part of its assets.

Mr. Monday said that, like certain Executive Directors, he considered that the proposals set out in the staff paper should be a "tidying" exercise, and not related to the long-term reform of the international monetary system. He therefore supported Mr. Kafka and others in inviting the staff to draft specific amendments to the Articles in the light of the present discussion for consideration at a future date.

On individual sections of the staff paper, Mr. Monday stated that he gave wholehearted support to the proposal for the use of special drawing rights in the General Account set out in Section I. On Section II he would be grateful if the staff would clarify the meaning of the first sentence. In Section III.1, he saw no reason why the Articles should be amended as proposed; on the contrary, he considered that the present provisions for stand-by arrangements should remain in force. He had no strong views on Section III.2, but on Section III.3, he inquired, like earlier speakers, who would determine a country's reserve currency or currencies. With respect to Section IV.1, he fully supported the proposal to simplify the repurchase provisions, and he had no difficulties with Sections IV.2 or IV.3.

Regarding Section V, Mr. Monday said that he would support the proposal in the paper, although he appreciated the points made by at least two of the Executive Directors from the developed countries that might have to draw on the Fund in the future. He wholeheartedly supported the proposal in Section VI.

Mr. Deif reported that he had received no communication from his constituents. He would therefore speak in a personal capacity. On Section I, he would support the staff proposals in the second paragraph, although with the reservations put forward by Mr. de Groote and Mr. Schleiminger regarding the last sentence. With the third paragraph he had no difficulty although, like Mr. Massad, he would like some explanation as to what was meant by "discharged or undischarged gold obligations." On the fourth paragraph, like Mr. de Groote he would like the proposed authority of the Fund to pay remuneration and distribute net income made subject to agreement of the country concerned.

With respect to Section II, Mr. Deif commented that like other Executive Directors he believed that the issue of gold needed a more extensive discussion before any decision could be taken by the Executive Directors. In connection with Section III.1, he shared Mr. Massad's views regarding the maintenance of the present Fund policies; he was convinced of the desirability of not making express mention of stand-by arrangements in Article V, Section 3. He also shared Mr. Massad's views regarding Section III.2, of the staff paper because of his particular concern with the effects that the proposed change would have on the liquidity of the Fund. Regarding Section IV.1, he could only share the enthusiasm of other Executive Directors for simplification. He also supported the changes proposed in Section IV.2 and Section IV.3. In Section V he sided with the Executive Directors who were against levying a periodic charge on the basic gold tranche. He had nothing to say on Section VI.

Mr. Prasad remarked that his authorities were broadly in sympathy with the thrust of the staff proposals in the staff paper (SM/74/72). While he had some sympathy for Mr. Beaurain's views, it seemed that reform would take place on a piecemeal basis, like it or not. It would therefore surely made little difference if the proposals put forward by the staff were adopted ahead of an overall reform.

His authorities strongly supported the movement in the direction indicated in Section I, Mr. Prasad continued; indeed, the sooner the Fund moved in the direction indicated, the better it would be. Section II he found rather difficult to interpret. For instance, the Fund's present powers to buy gold might be reconsidered; but until more was known about the extent of the powers or for what purposes they would be altered, it would be difficult to have a clear view on the desirability of change. Similarly, the Fund might be authorized to sell gold in the market, or perhaps use gold in exchange for some countries' Treasury Bills, and that might be worth considering, particularly if countries were prepared to allow the Fund to act in that way without actually selling its gold. Mr. de Groote's suggestion with respect to Section III.1--to the effect that since the Fund presently had more than one kind of facility, stand-by arrangements and all the other facilities should be treated equally--appealed to him. His authorities did not wish to see charges imposed on the gold tranche. That was something to be avoided as much as possible. He had no comments on the other sections.

Mr. Harley recalled that the U.S. authorities were generally favorable to amendment of the Articles, and that they were supporting efforts in the Committee of Twenty to develop a package of key amendments for early action. In so acting they were not, he believed, in the opposite camp from Mr. Beaurain, because they were not seeking in any way to prejudge issues of reform. However, because they were interested in obtaining some amendments, they believed that it would be well to be cautious about overloading the package with proposed amendments that might be useful or desirable, but that were certainly not critical or urgent. It might slow legislative approval of the really important amendments if the package were too heavily loaded. The U.S. authorities feared that a number of the changes suggested in the staff paper before them (SM/74/72) might fall into the nonurgent category. They also felt that changes affecting reform should not be made when it was not clear what the outcome of monetary reform would be.

Most of the specific proposals made in the staff paper would need further expansion or clarification before final judgments could be expressed, Mr. Harley considered. In Section I his authorities had noted the proposal that either the Fund or the member could decide to have a transaction carried out in special drawing rights without the agreement of the other party. While such a proposal might not be objectionable, they wondered whether the change was necessary and, if so, why. They felt at first glance that the proposal that special drawing rights should be used in repurchases in lieu of gold or currencies would be satisfactory. With respect to the use of special drawing rights in quota subscriptions, charges, remuneration, and net income, they believed that it would be in order to use special drawing rights for all those items except quota subscriptions. On that topic a great deal more detailed study would be required, and they expected that the work in that connection would be undertaken for the quota review. They were not very sure whether the proposal to eliminate the limitations on replenishment were desirable. Those proposals should perhaps be held over until broader decisions had been made on the characteristics of special drawing rights.

With respect to Section II, the U.S. authorities had no objection to reconsidering the Fund's powers to buy gold, Mr. Harley explained, but they would like to know what the Fund intended to do thereafter. It was not necessarily desirable merely to generalize the powers of the Fund without knowing in what direction they might be used. They had no objection in principle to the Fund selling gold on the market and investing the proceeds as it might desire, but there again they would like to know what principles and safeguards would be adopted.

The proposal in Section III.1 to insert an express provision for stand-by arrangements in the Articles looked unexceptionable to the U.S. authorities, Mr. Harley commented. It was, however, not clear that such an action was needed, and it was certainly not urgent. Concerning Section III.2, the U.S. authorities were prepared to consider waiving the 25 per cent limit on drawings, but they had not yet come to a clear conclusion. They believed that the 200 per cent of quota limit should be retained, as should the tranche conditionality policy. They would not object to an alternative legal form for ensuring tranche conditionality, but if the 25 per cent per year limit were withdrawn, they would not wish to lôse conditionality. In Section III.3, the suggestion that the Fund should say which currencies were to be drawn, and the elimination of any reference to the need for "that currency" in making payments, would require additional study and thought. His authorities understood the desire to make additional currencies usable in practice by the Fund, but they would like to see a staff paper as an aid to clarifying their views.

On Section IV, his authorities felt that the proposal would give the Fund rather broad authority without informing members just how it would be used, and they would wish to consider it more carefully, Mr. Harley stated. They had no objection to increasing the flexibility of the Fund's operations, but they would like to be sure that they knew how the flexibility would be exercised. On the topic of allowing the Fund to decide the proportion of quota increases to be paid in gold or special drawing rights--with the difference between the portion and 25 per cent subject to repurchase with gold or special drawing rights at a later date--the U.S. authorities understood that the proposal would not apply to subscriptions connected with a general increase in quota. While the proposal was probably satisfactory in itself, since installment payments by less developed countries had been permitted in the past, the matter did require further study, and he would join those Executive Directors who had asked for more work to be done on the topic before coming to a conclusion. Elimination of the complex rules on the media of repurchase was very desirable.

The U.S. authorities assumed that Sections V and VI were aimed at producing more earnings for the Fund, Mr. Harley continued; they were by no means certain that additional earnings would be required within the foreseeable future. In any event, charges on gold tranche drawings needed further study. They would have no difficulty with the alternative suggestion of a small one-time service charge.

Mr. Lieftinck wondered whether the staff paper covered sufficient ground to enable Executive Directors to come to meaningful conclusions.

In strongly favoring an early amendment of the Articles of Agreement, he had two objectives in mind: first, to bring about an early return to legality; second, to safeguard the financial integrity of the Fund. While it was true that the Fund still had sufficient reserves, it would reflect on its position if for a number of years it were to operate in deficit and reduce its reserves each year. A third objective of reform could be to create a broader facility than provided for in the present Article XIV, which the Fund would use in emergency conditions.

Dealing with the return to legality, Mr. Lieftinck remarked that the subject had been discussed by the Deputies of the Committee of Twenty and, in that connection, he regretted that there had been no proposal to legalize floating. If there was anything that he considered urgent, and which would not prejudice reform, it was the legalization of floating in certain conditions. With respect to the financial integrity of the Fund, he noted that when difficulties arose with respect to the equal value principle, Article XXV provided that any change required unanimous agreement among the Executive Directors and an 80 per cent majority in the Board of Governors. He wondered whether it would not be desirable, in the unsettled times through which the Fund was passing, to avoid the need for such near unanimity. He would therefore welcome a change from unanimity to a 75 per cent vote among the Executive Directors, while maintaining the 80 per cent vote for the Board of Governors.

The immediate amendment of the Articles presently under discussion could be used to make the special drawing rights a better instrument and pave the way for their playing a larger role in the future, Mr. Lieftinck considered. Section I of the staff paper was, therefore, a step in the right direction. The discharge of repurchase obligations in special drawing rights would be particularly helpful. With respect to the use of special drawing rights in purchases, he had similar reservations to those voiced by Mr. Rawlinson. Further work should certainly be done on enabling both the member and the Fund to have options to use special drawing rights under the General Account, and more particularly to enable the Fund to sell and the member to buy special drawing rights instead of currencies in accordance with the Articles. He was rather dubious as to whether it would be proper, if a member were anxious to have currencies, for the Fund to be able to compel it to receive special drawing rights. Similarly, he wondered whether it would be satisfactory if a member were entitled to require that the Fund sell nothing but special drawing rights. He was therefore unable to support the proposal to do away with the agreement of the other party. However, the real danger in the second paragraph of Section I lay in the last sentence, where it was proposed that the option would be limited by the amount of special drawing rights held in the General Account unless the Fund had powers to issue them to finance transactions and cancel them on repurchase. He had no trouble with the cancellation of special drawing rights, but the creation of special drawing rights in the cases mentioned by the staff went beyond what he considered sound.

He would have no objection to permitting members to discharge part of the subscription payable on an increase in quota or to pay all charges with special drawing rights, and the Fund could be authorized to pay remuneration and to distribute net income in the form of special drawing rights, Mr. Lieftinck remarked. He had, however, an open mind about whether limitations on replenishment should be eliminated under the Articles. A more important point was the question of the acceptance limit. He himself did not believe that the SDR was yet sufficiently firmly established to eliminate the limit, but he would be open-minded in considering whether perhaps the limit was too low.

With respect to gold, Mr. Lieftinck observed, he would favor extending the powers of the Fund from being able to buy gold to being able also to sell gold. Such an amendment would certainly represent a change in the role of gold, but prudent and cautious steps in that direction were called for because the gold problem had become quite out of hand. If the Fund did not establish some provisions with respect to gold, members would flout their obligations to the Fund, and it was desirable to try to prevent the emergence of illegal actions. In that connection, he had been rather surprised that no mention had been made in the staff paper of Article V, Section 6, which dealt with purchases of currencies from the Fund for gold. That section contained the "equal advantage" clause, on which there had been a clear difference of opinion among Executive Directors. In the first place, the opportunity might be taken to clarify the meaning of the clause. Second, if the Executive Directors were trying to expand the role of special drawing rights, he wondered whether it would not be possible to introduce provisions for special drawing rights similar to those contained in Article V, Section 6, in respect to gold. If that were done, any member desiring to obtain, directly or indirectly, the currency of another member would be able to acquire it by the sale of special drawing rights to the Fund. A change in Article V, Section 6 was certainly desirable if the intention was to minimize the role of gold.

The proposal to give legal status to stand-by arrangements was not of great significance, Mr. Lieftinck considered. He was greatly attached to stand-by arrangements, which had not given rise to any legal problems so far. To give them legal status might reduce their flexibility; in any event, he did not consider the matter to be at all urgent. With respect to the quantitative limits on the use of the Fund's resources, he saw no reason to abolish the waiver requirement for the use of over 25 per cent of quota for purchases within 12 months. The Executive Directors had been quite generous with the use of the waiver, and he had understood that it had not created any real difficulties; he would certainly maintain the 200 per cent of quota limit. He also did not believe that the use of currencies in transactions and repurchases had created difficulties. Still, the reference to "that currency" could perhaps be modified.

While he agreed with the comments that had been made regarding the use of the term "its reserve currency" in the paragraph dealing with conversion, Mr. Lieftinck continued, he would favor the establishment of a conversion obligation. However, it would certainly be necessary to know what the obligation involved, and to do so would require clarification of the meaning of "reserve currency." Moreover, if exchange rate was to be determined in accordance with new provisions, those should be worked out before a conversion obligation was introduced.

He was a strong supporter of Article V, Section 7(b), Mr. Lieftinck stated. While it was true that it made for difficult reading as presently worded, and could therefore be simplified, he would wish to maintain the concept of need and the revolving character of the Fund's resources. He would be prepared to accept a simplification of the wording, provided that the substance was not changed.

Dealing with the question of monetary reserves, set out in Section IV.2, Mr. Lieftinck considered that some definition of "reserves" was absolutely essential. It would be very dangerous to leave it to the Fund to define the term on an ad hoc basis from time to time. There were so many references to the reserves and to the volume of reserves in the Articles of Agreement that the concept should be clarified. While he was generally in favor of flexibility, he would not apply that attitude to the meaning of "reserves." On that point it was essential for all concerned to know clearly what was involved. When it came to the use of reserves in defining repurchase obligations, he would favor more flexibility than was permitted under the present arrangements for the distribution of repurchase obligations among the types of monetary reserve. Nevertheless, the principle should be maintained of enabling the Fund to give guidance with respect to the distribution of repurchase obligations among the types of monetary reserves, and he would have great hesitation in agreeing that currencies might be acceptable by the Fund even though they were not convertible within the meaning of the Articles.

The whole question of charges on transactions in the gold tranche was a very controversial one, Mr. Lieftinck considered. His attitude was to some extent determined by his belief that the financial integrity of the Fund must be safeguarded. The best way of achieving that result would perhaps be to break the link between remuneration and the rate of interest on special drawing rights. That was a point which, although not mentioned in the staff paper, ought to be seriously considered as an urgent matter requiring amendment of the Articles. The imposition of a service charge was already permitted by the Articles; but the introduction of greater flexibility in order to permit a differentiation between the rate of interest on special drawing rights and that on the super gold tranche was essential if the financial position of the Fund was to be maintained.

He had been rather disappointed to hear from Mr. Schleiminger that the German authorities were against any charge on transactions in the gold tranche and that they did not favor investment, Mr. Lieftinck commented. If the two elements were not taken together, the Fund could hardly cover its expenditures and maintain its reserves; the only possibility might be a considerable increase in charges on all tranches. The three topics of charges on transactions in the gold tranche, a loosening of the link between remuneration and the rate of interest on special drawing rights, and authorization to invest reserves were each of such importance that they ought to receive special consideration.

Mr. Reynolds commented that, while he favored the drafting of amendments, it might be premature to do so forthwith. A more practicable timetable might be to prepare a general report by June 1974 prior to the meeting of the Committee of Twenty, with a view to having possible amendments to the Articles by the time of the 1974 Annual Meeting.

Before making points of detail, Mr. Reynolds said that he attached a great deal of importance to conditional liquidity, which had a significant role to play both in helping members with their balance of payments problems and in assisting in the adjustment process. If there was to be a healthy and viable General Account, it was almost essential to have the two assets "Reserve Position in the Fund" and "Special Drawing Rights" as similar as possible, with respect to both their value and to their yield or rate of interest. He feared that a substantial difference between the two assets would result in a continuous built-in tension that would be manifested by a marked preference for one asset over the other. Indeed, his enthusiasm for some of the recommendations set out by the staff in its paper (SM/74/72) rested, in part, on the assumption that there would be a close similarity between the two assets.

Dealing with specific points in the staff document, Mr. Reynolds said that he had no problems with Section I. However, like Mr. Schleiminger and Mr. Lieftinck, he considered that it would be premature to make allocations of special drawing rights to the General Account. Some improvement in the existing arrangements could perhaps be made if the General Account were in a position to obtain special drawing rights from members in exchange for their currency. Such an arrangement would be the reverse of the present replenishment procedure.

If all members were participants in the Special Drawing Account, Mr. Reynolds remarked, he would be inclined to make the 25 per cent subscription payment obligatory in special drawing rights rather than in gold. However, all members were not participants, and it might be worth considering whether those members that were not participants should pay the 25 per cent "in currencies convertible in fact"--other than their own respective currencies--instead of in special drawing rights. As such an arrangement would involve greater expense to the members converned, in the sense that their interest foregone on those currencies would be somewhat higher than the interest that would be lost by paying subscriptions in special drawing rights, it might be an incentive for them to become participants in the Special Drawing Account.

The limit on acceptance laid down in Article XXV, Section 4, should be maintained, Mr. Reynolds considered, though he doubted the need for any extensive consultations regarding alternative means of replenishment. On the question of gold, he had been puzzled by the reference to the Fund's present powers to buy gold. However, if the reference was to Article V, Section 6(a), a section that had in the past been very controversial, he felt that that particular provision might well be reconsidered. He would favor the Fund selling gold, and he would like it to be authorized to do so by a simple majority vote of members. He would also favor the Fund investing the proceeds.

On the question of making specific mention in the Articles of stand-by arrangements, Mr. Reynolds said that he had no strong views. However, if stand-by arrangements were to be mentioned in the Articles, consideration should also be given to mentioning other Fund facilities. He would also be rather indifferent as to whether or not the 25 per cent of quota limit on purchases in one year should be abandoned. However, there was the consideration that for the next year or two it might be useful to retain the limit as a means of rationing whatever resources the Fund might have to distribute among drawers. He would favor increasing the cumulative limit from 200 per cent of quota to say 300 per cent of quota and would accept the staff's suggestions on the use of currencies in transactions and repurchases. For information, he inquired what, in Fund parlance, was the difference between "transactions" and "operations." It seemed to him that in present circumstances, Article V, Section 3(a)(i) was probably obsolete.

He had always found Article V, Section 7(b) a complicated provision, Mr. Reynolds noted. While the principles mentioned by the staff at the end of Section IV.1 of the staff paper were laudable and desirable, it should be possible to devise a less complicated way of achieving the objectives. Like Mr. Lieftinck, he considered it important for all Fund members to know what the Fund meant when it referred to "reserves." Noting that the staff appeared to have in mind several concepts of reserves, he hoped that one concept or definition would prove to be sufficient. While he had no difficulty with the suggestions regarding the media of repurchase, he would not favor having a periodic charge on transactions in the basic gold tranche.

Saying that such a charge would be quite unfair, Mr. Reynolds expressed the belief that it would not be in the best interest of the General Account or of the whole scheme for providing conditional liquidity. Such an arrangement would in fact involve a double cost, namely, the cost--in the form of income foregone--in acquiring a basic gold tranche position in the first place and, second, in the proposed periodic charge that would be incurred in using it.

Finally, Mr. Reynolds believed that the Fund should be empowered to invest assets equivalent in amount to its reserves for the purpose of meeting deficits or augmenting its reserves in order to cover prospective deficits.

Mr. Kharmawan remarked that he had not received instructions or comments from all his constituents; he would therefore be making largely provisional remarks. In general terms, his constituency welcomed attempts to make special drawing rights more meaningful and to introduce them gradually into the monetary system. However, if amendments were required for the greater use of SDRs in the General Account, he would not consider them to be directly connected with monetary reform. While references had of course been made to the General Account in the Committee of Twenty, he could not accept the position that every amendment should be considered as related to monetary reform. They would rather, for the time being, constitute a "tidying up" operation. The less developed countries were naturally concerned about the piecemeal approach to reform that had been adopted; but they considered the staff paper (SM/74/72) as only indirectly related to the work of the Committee of Twenty.

Speaking on the use of special drawing rights in the General Account, Mr. Kharmawan said that he failed to understand the advantage of the Fund offering special drawing rights to members that came to the Fund for assistance. A member that was short of reserves would surely need to convert the special drawing rights into currency immediately. On the question of gold, he would not comment until he had heard the staff explanation of the first sentence of Section II. So far as the second sentence was concerned, as members had the right to sell gold in the market, he saw no objection to the Fund having the same right. Section III.1 and Section III.2 seemed to him superfluous, as he saw no need either to legalize stand-by arrangements or to change the 25 per cent of quota provision. Regarding the use of currencies in transactions and repurchases, he would like to see the matter studied further; the obligation to convert currency into a reserve currency seemed obscure, quite apart from the meaning of the term "reserve currency" in the present context. For instance, what would be the obligation of an Article XIV country under Section III.3?

With respect to Section IV, Mr. Kharmawan believed that some clarification of the meaning of the term "monetary reserves" would be desirable. He welcomed the proposal to make it possible for countries to pay subscriptions in connection with a general review of quotas, or with an adjustment of individual quotas, in special drawing rights. That was indeed an urgent matter that ought to be settled as soon as possible. He did not feel that charges should be imposed on transactions in the gold tranche. A great deal of difficulty had been encountered in establishing that the gold tranche belonged to a member's reserves, and it would not be desirable to risk engaging in such lengthy debates again. He certainly agreed with the proposal to give the Fund power to invest its assets.

Mr. Andreassen stated that the Nordic countries considered that most of the issues raised in the staff document (SM/74/72) needed further study and consideration. They did, however, think that it would be desirable to streamline and simplify the rules for the General Account. In so doing, they took the position that the provisions should be formulated in such a way that it would be possible to change details without going through the cumbersome process of amending the Articles of Agreement. Furthermore, they would in principle support the idea of broadening the role of special drawing rights in the General Account. However, before taking any position on the various changes proposed in Section I, they wished to have the technical problems relating to the changes, and the implications thereof, spelled out in greater detail.

The proposal to change the Fund's powers to buy and sell gold would raise many problems that were difficult at present to foresee with any degree of clarity, Mr. Andreassen felt. The Nordic countries doubted whether changes in the Fund's gold policy should be undertaken before a general agreement on the role of gold in the monetary system had been reached. They also had doubts about the proposal that the Fund should be given power to invest part of its assets. In any event, the proposals he had mentioned required fuller consideration. In conclusion, he stressed the tentative nature of his remarks and the need for further Board deliberation on the important issues raised in the staff paper.

Mr. Palamenghi-Crispi commented that he had long taken the position that Mr. Andreassen indicated was held by the Nordic countries, namely, that any amendment that might be introduced should make it possible to vary agreed limits without going through the cumbersome exercise of amendment and ratification. He also agreed with Mr. Harley that there were urgent matters and nonurgent matters, even though there might be disagreement on what was urgent and what was not urgent. In that connection, Mr. Kharmawan had referred to Article XIV and, though it might not be urgent for the salvation of the monetary system, there were certain words in Article XIV, Section 2 that ought rationally to be amended. That Section referred, for instance, to "the postwar transitional period" and to "the case of members whose territories had been occupied by the enemy." Surely the "transitional period" was long past, and the time had come to consider whether the distinction between Article XIV and Article VIII made sense any longer. In practice, the only difference between the two categories of obligation seemed to be that Article XIV countries were able to act without authorization from the Fund in ways that, for Article VIII countries, required Fund authorization. In the present circumstances, he would be interested either in abandoning the distinction or making it more meaningful. In passing, it was perhaps paradoxical that the countries for which Article XIV had been designed were, for the most part, currently fulfilling the obligations of Article VIII, and that those countries that were fulfilling the obligations of Article XIV were not those that had been envisaged when Article XIV had been drafted.

Mr. Kharmawan explained that, while he would be interested in discussing in the Executive Board whether it was worthwhile or not to maintain the distinction between Article XIV and Article VIII, he was more concerned with the obligation for members to convert their currency if it was included in the currency budget. Mr. Lieftinck had recently observed that it was rather strange that the Fund had to pay remuneration on the super gold tranche, which was really part of the Fund's own assets. If it was in fact the case that the subscription paid by a member country was the property of the Fund, then no member, whether adhering to the obligations of Article XIV or to those of Article VIII, could object to the inclusion of its currency in a currency budget, because that currency belonged to the Fund. However, the question of conversion was a rather different one because, by definition, the currencies of Article XIV countries were not convertible. Even for certain Article VIII countries, whose currencies were legally convertible, there had been difficulties in the past. If that were so for Article VIII countries, it would surely be more difficult for Article XIV countries to accept the obligation of convertibility. He would be interested to hear the comments of the General Counsel on that matter.

Mr. Prasad considered that the Executive Directors should take up the point made by Mr. Palamenghi-Crispi at more leisure. The question of convertibility was no longer related to the conditions referred to in Article XIV, but to the need for seeking equilibrium in a situation where there was likely to be a continuous balance of payments deficit arising out of development programs. While he agreed with Mr. Palamenghi-Crispi that the matter ought to be dealt with separately at an appropriate time, the beliefs of his chair were likely to prove somewhat different from those that might be expressed by Mr. Palamenghi-Crispi.

Mr. Caranicas remarked that, not having heard from members of his constituency, he would comment very briefly on a purely personal basis. In so doing, he would adopt the line put forward by Mr. Wahl; he did not believe that the Executive Directors ought to be undertaking a minor reform of the monetary system nor should they be overzealous in bringing law and order into the General Account by proposing changes in the Articles of Agreement or urgently reviewing the regulations and decisions on which the General Account was based. In general, he shared the views made by the Executive Directors from developing countries, even though he noted that there were some differences in their positions.

While avoiding examination of each particular item in the staff paper (SM/74/72), Mr. Caranicas thought in general that there was agreement for the special drawing rights to become the focus of the international monetary system, and all efforts should be made in order to enable them to play a greater role. He would, therefore, made no comment on Section I in the staff paper while he considered that Section II was rather premature. It had been proved that gold was a complicated and touchy question, during recent discussions by the Deputies of the Committee of Twenty.

On Section III.1, Mr. Caranicas felt that there was no need to proceed with a revision of the Articles of Agreement because the Fund had been operating stand-by arrangements successfully without any mention of them occurring in the Articles.

There were some points in the staff paper that he did not understand, Mr. Caranicas commented. For instance, the definition of "monetary reserves" was likely to be a long and difficult task. He observed, in passing, that it had taken the United Nations 48 years to agree on the definition of "aggression." While it might not take so long to define "monetary reserves," that was certainly not one of the most pressing activities facing the Executive Directors. Many other points in the paper, although interesting, and representing a checklist of possible modifications, were also not of great urgency; nor was there much agreement on them. The staff should therefore be given more time to gather additional information before the subject came back to the Executive Board.

With respect to Mr. Lieftinck's suggestion that the Fund should take steps to legalize floating, Mr. Caranicas wondered whether it was necessary to do so. After all, the Committee of Twenty would no doubt endorse the rules for floating on which it had been working, and in two years' time it might perhaps prove unnecessary to have legal provisions for floating. That was certainly the ardent desire of the developing countries. Their hope for a return to a monetary system based on stable but adjustable exchange rates was not likely to be advanced if floating were legalized.

The General Counsel, after some discussion on questions of procedure, explained that the staff paper (SM/74/72), which had been commissioned both by the Executive Directors and by the Deputies of the Committee of Twenty, was to be a paper dealing with the amendment of provisions relating to transactions and operations of the General Account. In reply to Mr. Reynolds, he explained that a "transaction" was intended to be the exchange of one asset for another, while an "operation" was the discharge of an obligation not involving an exchange of assets. Hence, an exchange transaction with the Fund, meaning the sale of one currency for another, was the most important transaction referred to in the paper. Clearly, as the paper was intended to deal with transactions and operations of the General Account, it did not deal with any of the regulatory provisions of the Articles. It was for that reason that it did not cover floating or the distinction between Article VIII and Article XIV. There was, however, no implication that other amendments were not overdue or desirable. Similarly, the reason for the absence of any mention of the possibility of breaking the link between the rate of remuneration and the interest rate on special drawing rights was that that particular provision related to the Special Drawing Account and not to the General Account. The distinction between Article VIII and Article XIV, touched upon by Mr. Palamenghi-Crispi, was a complicated issue on which a great deal could be said.

The discussion had raised two general categories of topics, the General Counsel considered, namely, specific amendments that could be made, and the technique of amendment. With respect to technique, he believed that the basic issue would be how flexible the new provisions ought to be. That, in turn, led to the twofold question: whether very specific formulas, such as now existed, should be eliminated from the Articles on the grounds that they tended to become hampering to the Fund and members; and whether, if any more or less specific formulas were retained, provisions ought not to be introduced to make it possible to revise or supplement these formulas or elements of them without the need for amendment. In that connection, he would recall that there were already nine provisions in the Articles under which there was a power to vary provisions without the need for amendment.

Moving from general comments to explanations of questions that had been raised by Executive Directors on individual sections of the staff paper, the General Counsel explained that in Section I the reference to "repurchase obligations in gold, whether discharged or undischarged," referred to the fact that there were certain outstanding repurchase obligations that had accrued in gold but that had been postponed. There was no obvious method at the moment of disposing of those obligations. Constant postponement was clearly a very dubious course; hence, if the opportunity arose to eliminate those outstanding obligations--in the sense that they would be settled in another medium--it ought to be taken. However, if undischarged obligations that had accrued after a given date were treated in that way, equity would clearly demand that similar obligations that had already been discharged in gold should be the subject of the same treatment under the amendment.

Section II, the General Counsel explained, had deliberately been written in vague form. The first sentence referred to the only provision under which the Fund could buy gold, apart from the acceptance of gold in the discharge of repurchases. That provision--Article V, Section 6--was a narrow and obscure provision that had been the subject of considerable contention. It could be improved, but what was desirable was an extention of the powers of the Fund in connection with the purchase and sale of gold, and not merely a "tidying up" of Article V, Section 6 and Article VII, Section 2.

The reference to stand-by arrangements in Section III.1 had been proposed in SM/74/72, the General Counsel remarked, because it had been thought that the Articles ought to mention what had become the main financial technique of the Fund for making its resources available. In that connection, he would distinguish between techniques for making the Fund's resources available, and policies for so doing. If that distinction were accepted, the mention of stand-by arrangements in the Articles would not lead to the mention of the particular policies under which the Fund made its resources available. He would propose that the second sentence of

Article V, Section 3(c) should be enlarged to read "The Fund shall adopt policies on the use of its resources, including use under stand-by arrangements, that will assist members to solve their balance of payments problems... ." That reference would involve no loss of flexibility in the adaptation of stand-by arrangements.

There were two separate points to be made in the case for amending the quantitative limit of 25 per cent of quota for purchases within 12 months, referred to in Section III.2, the General Counsel stated. First, it had become a matter of almost daily routine to grant waivers under Article V, Section 4. And yet, the Section in question referred only to granting waivers after taking into consideration periodic or exceptional requirements, and to granting them especially in the case of members with a record of avoiding large or continuous use of the Fund's resources. Article V, Section 4 had not been the basis for the Fund's adoption of conditionality policies. It had been employed mainly to make repurchases obligatory. Policies on conditionality had been extrapolated from the explicit and implicit provisions of the Articles requiring the Fund to have policies on the use of its resources. Incidentally, there had been no explicit mention of the need for the Fund to have policies on the use of its resources until the amendment of 1968. The amendment had been adopted precisely because there had been no clear reference to policies. The reason was similar to the one that led to the suggestion that stand-by arrangements should be mentioned.

With respect to the use of the term "its reserve currency" in Section III.3, the General Counsel remarked that he had understood those words to be an echo of the words in the present policy on the use of currencies in purchases and repurchases, which would in effect become statutory if the suggestion in Section III.3 was adopted. The words in that policy meant the currency normally held by a member in its reserves. The language had been inserted in the policy in order to avoid compelling a member to provide or acquire a currency other than the one that it normally held in its reserves. In connection with the same section, Executive Directors had mentioned the difference between Article VIII and Article XIV countries, with the suggestion that the conversion obligation ought not to extend to Article XIV countries. It was perhaps worth mentioning that the duty to convert currency drawn from the Fund, even by an Article VIII country, had never been satisfactorily settled in principle. The problem was related to some extent to the words "in that currency" in Article V, Section 3(a)(i). The drafters of the Articles had assumed that, in most instances perhaps, conversion would not be necessary, because normally members would draw from the Fund the currency in which they or their residents wished to make payments. The world had of course changed since then, and so had the Fund's policies. What was really under discussion was the extent to which in the changed world some of the Fund's policies should be made statutory.

Commenting on the remarks made by Executive Directors on the proposal to replace Article V, Section 7(b), the General Counsel recalled that that provision, which had been enormously troublesome, was the source of no more than approximately 25 per cent of repurchases at the present time. What had happened was that a system of repurchase had grown up as a supplement to statutory provisions that were unsatisfactory for various reasons. The issue, therefore, was whether the Executive Directors wished to retain a system that had little practical effect. It should not be overlooked that the supplementary system was effective. The proposal for replacement was not concerned so much with language as with the very concept of the provision.

On Section VI, the General Counsel commented that a certain power to invest had been found by interpretation; there was some question whether there could be a different power of investment. His own feeling was that only a limited possibility existed under the Articles, and that even if it did exist, there was still the question of how the power to invest should be implemented. The case for amendment, therefore, rested not simply on the recognition and establishment of an express power of investment but also on the regulation of the mode in which investment might be made.

The Economic Counsellor noted that the tentative suggestion in the second paragraph of Section I--that the General Account could impose the receipt of special drawing rights on a drawer from the Fund, or that a drawer could insist on receiving special drawing rights even if the other party did not agree--had not found much favor. So far as the desire of the General Account to sell special drawing rights was concerned, it seemed unlikely that the drawer would object. It would only mean that the drawer would have to go through the designation process to receive currencies if it wished to do so. In view of that, a provision of the sort suggested was probably not necessary for the Fund. If it was true that the drawer would normally be happy to accept special drawing rights, whether it wished to keep them or exchange them for currencies, perhaps the proposal that the Fund should be able to replenish its holdings of special drawing rights without the consent of the other party was also less important than might appear at first sight. If the Fund wished to use special drawing rights, it could use them in the transaction itself; that would ensure, incidentally, that the use would be subject to the rules for acceptance and the principle of designation. Mr. Lieftinck had inquired whether members should not have a right to obtain currency from the General Account for special drawing rights. He did not believe that such a right was desirable. Members could obtain currency for special drawing rights through designation, subject only to need. If they did not have a need, presumably the Fund would not wish to offer them another method of obtaining currency. If they did have a need, the Fund would not wish them to draw what might be relatively scarce currencies from the General Account.

With respect to Section III, the Economic Counsellor commented that it seemed to him important that the Articles should provide all the assurance they could that the Fund would be able to sell the currencies it held. If currencies were not readily usable in the exchange market, some obligation would be needed on the issuer, i.e. the member acquiring a reserve position in the Fund, to make available an asset that was readily convertible. It would not make very much difference whether the provision stated that the asset was to be converted into the member's reserve currency or into a currency convertible in fact. But if the Fund wished to sell minor currencies, there would have to be a conversion provision. He did not believe that the proposal would introduce any particular hardship; both Article XIV and Article VIII members were already obliged to acquire special drawing rights against a convertible currency.

Regarding the replacement of Article V, Section 7(b), the Economic Counsellor recalled that the staff had explained at the top of page 4 of the staff paper (SM/74/72) that if there were satisfactory provisions regarding the sale of all currencies, the Fund would, in fact, have the power to reduce a member's indebtedness to the Fund by selling its currency. In those circumstances, it would be less necessary than in the past to rely on the provisions of Article V, Section 7(b).

With respect to Section IV.2 of the staff paper, the Economic Counsellor explained that the definition of monetary reserves was only significant in the provisions on repurchase, on paying charges in a member's own currency, and on paying 25 per cent in gold in connection with a quota increase. If those three provisions were considered no longer worth retaining, it would not be necessary to have a definition of monetary reserves either. The Fund could probably operate quite satisfactorily with a concept of reserves that was not sharply defined. Designation was based, not on monetary reserves, but on "reserves," and that arrangement had caused no difficulty.

Executive Directors seemed to feel it undesirable to levy a charge on transactions in the gold tranche, the Economic Counsellor commented, because to do so would interfere with the reserve character of the gold tranche itself. However, to levy a charge of that sort would have a real merit in equity, as the staff had mentioned previously. The gold tranche was the only slice of a member's access to the Fund's resources that could be used at no cost to the member. As the access would consume resources for which the Fund would have to pay remuneration, if the cost was not borne by the member using the resources, it would have to be borne by other members. Since Executive Directors in general disliked the idea of levying a charge on the gold tranche, the staff would return to the idea mentioned by the Managing Director some months ago that would have the same net effect, namely, that the Fund should levy a charge on all members on the equivalent of their gold tranche, and remunerate the basic gold tranche as well as the remainder of the gold tranches.

The Acting Chairman recalled that it had been intended that the present discussion should be preliminary and exploratory. It had certinaly been useful in that respect. Two general points could be made: first, aside from Mr. Beaurain--and perhaps Mr. Caranicas in a personal capacity--Executive Directors had indicated that they either favored an interim amendment or that they would not be averse to one. Second, Executive Directors had asked for elucidation on several of the individual suggestions, and many of them had indicated that they would like further written material for subsequent discussion at a later date. The staff would of course do its best to provide that material.

Mr. Lieftinck noted that the intention of the staff in preparing its paper (SM/74/72) had been to deal only with problems arising from the transactions and operations of the General Account. He had allowed himself a limited number of observations on other possible changes in the General Account that did not refer to transactions and operations. He hoped that the staff, in meeting the requests for further material, would take into account changes in the General Account other than those discussed in SM/74/72.

The General Counsel remarked that not all the provisions of the Articles were divisible between the General Account and the Special Drawing Account. There were many other provisions in the Articles that dealt with the Fund or with the obligations of members other than in relation to those two Accounts. The study that had been requested had related to the General Account only.

The Executive Directors then concluded their preliminary exchange of views on possible changes in the General Account.

APPROVED BY THE EXECUTIVE BOARD:
Meeting 74/131, October 21, 1974

WILLIAM B. DALE
Acting Chairman

W. LAWRENCE HEBBARD
Secretary