INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 89/101

3:00 p.m., July 27, 1989

R. D. Erb, Acting Chairman

Executive Directors	Alternate Executive Directors
	C. Enoch
Dai Q.	
	C. S. Warner
	J. Prader
E. T. El Kogali	S. M. Hassan, Temporary
E. A. Evans	
	R. J. Lombardo
	M. Hepp, Temporary
	G. García, Temporary
	S. Appetiti, Temporary
	S. K. Fayyad, Temporary
M. Fogelholm	
M. R. Ghasimi	
	B. Goos
	E. Kiriwat
	L. E. N. Fernando
A. Kafka	F. A. Quirós, Temporary
	W. N. Engert, Temporary
Mawakani Samba	C. V. Santos
Y. A. Nimatallah	
H. Ploix	
	G. P. J. Hogeweg
	N. Adachi, Temporary

L. Van Houtven, Secretary and Counsellor
B. J. Owen, Assistant

Also Present

African Department: A. B. Taylor. Exchange and Trade Relations Department: L. A. Whittome, Counsellor and Director; J. T. Boorman, Deputy Director; T. Leddy, Deputy Director; S. Tiwari. External Relations Department: S. W. Kane. Legal Department: F. P. Gianviti, General Counsel; W. E. Holder, Deputy General Counsel; H. Elizalde. Middle Eastern Department: L. Alexander. Treasurer's Department: G. Laske, Treasurer; D. Berthet, Z. Farhadian-Lorie, S. J. Fennell, P. S. Ross. Office of the Managing Director: A. K. Sengupta, Special Advisor to the Managing Director; P. Shome. Advisors to Executive Directors: F. E. R. Alfiler, M. Al-Jasser, M. Eran, A. Napky, A. Raza, R. Wenzel. Assistants to Executive Directors: G. Bindley-Taylor, C. Bjorklund, K. Ichikawa, A. Iljas, M. E. F. Jones, K.-H. Kleine, G. Montiel, C. Schioppa, M. J. Shaffrey, Shao Z.

1. OVERDUE FINANCIAL OBLIGATIONS - PROCEDURES FOR DEALING WITH MEMBERS IN ARREARS

The Executive Directors resumed from the previous meeting their consideration of a revision of the statement by the Treasurer on the Fund's procedures for dealing with members with overdue obligations, prepared in light of the discussion at a previous meeting (EBM/89/93 and EBM/89/94, 7/19/89). 1/ They also had before them a staff paper on the legal aspects of censure or declaration of noncooperation (EBS/89/128, 6/26/89), a staff paper on the issue of suspension of membership (SM/89/127, 6/28/89), and the six-monthly report on overdue financial obligations to the Fund (EBS/89/133, 6/29/89).

The Acting Chairman, reverting to the question of which other international institutions the Fund should send a communication to when it communicated with Governors, recalled that a number of Directors had supported the proposal by Mr. Goos to include the World Bank and regional banks. If that was in fact the understanding, the text would be amended accordingly.

Mr. Nimatallah said that that had been his understanding. Nevertheless, he wondered whether it would remain possible to have informal contact with other international institutions, as Mr. Kiriwat had suggested at the previous meeting.

The Acting Chairman suggested that a sentence could be added stating that informal contacts with other international institutions would not be precluded.

Mr. Goos remarked that he had overlooked, at the previous meeting, what seemed to him to be an inappropriate reference in the third test for issuing a declaration of noncooperation to comprehensive adjustment policies as "the basis for embarking on the intensified collaborative approach." Characterizing the appropriateness of the adjustment effort in that way was questionable, especially as the Fund might not wish to embark on the collaborative approach in all cases. The reference should be deleted, if it could not be reworded to qualify the comprehensive adjustment policies as being commensurate with arriving at a solution of the country's problems.

Mr. Enoch said that he agreed fully with Mr. Goos. In enumerating the steps to be taken on the remedial side, it seemed unnecessary to refer to action on the other side that was only part of the overall arrears strategy. Moreover, retaining the reference to the intensified collaborative approach in the context of the third criterion would be unnecessarily restrictive. Some countries would manage, by their own efforts, to restore a normal relationship with the Fund, and others would do so

---

1/ Reproduced in Annex I.

through bilateral relations. The intensified collaborative approach was an alternative way. If any reference was to be made to it, it should perhaps be in the preamble to the entire statement.

The Executive Directors agreed to delete the reference to the intensified collaborative approach.

Mr. Fogelholm, reverting to the issue of the declaration of noncooperation, remarked that as its effect was mostly symbolic, and as it was to serve as a signal, he felt that it should be published.

Mr. Nimatallah said that he agreed that the declaration should be published. With that in mind, the amendment to the wording of the declaration itself that he had proposed should be considered.

Mr. Enoch, Mr. Hogeweg, and Mr. Appetiti indicated that the declaration should be published.

Mr. Kiriwat said that he too did not believe that the declaration should be published because that would make it more of a punitive action than a deterrent.

Mr. Dai stated that he was not in favor of publishing the declaration of noncooperation.

Mr. Fernando considered that it was inadvisable not only to propose an amendment of the Fund's Articles of Agreement to allow for the suspension of membership, but even to state that it had already been considered advisable to reconsider the matter in the future. Once sufficient experience had been gained, the entire set of procedures should be reviewed. It was unnecessary to single out one particular aspect, that of suspension, and state that it would be reconsidered.

Mrs. Ploix said that she supported Mr. Fernando's position.

Mr. Goos said that he could accept the paragraph on suspension of membership, as drafted. He could also support publication of the declaration of noncooperation.

The Acting Chairman remarked that although a number of views had been expressed on the question of publication of the declaration of noncooperation, a clearer indication of the weight of opinion of the Board was necessary.

Mr. Nimatallah stated that the whole exercise of issuing declarations of noncooperation would not be useful, without publication. The Fund and its membership had become accustomed to publicizing what were considered to be critical issues. Furthermore, there was a recognition that it was only a few countries in protracted arrears that were creating difficulties for the Fund. Therefore, he saw no reason for not publishing the declaration.

Mr. Warner said that he found Mr. Nimatallah's views to be very sound. As a matter of fact, a decision not to publish the declaration would probably be ineffectual; sooner or later the declaration would work its way into public notice, so that the Fund might just as well publish the declaration of noncooperation as it did the declaration of ineligibility.

Mr. Evans, Mr. Hogeweg, Mr. Prader, Mr. Adachi, Mr. Appetiti, and Mr. Engert stated that they could support publication.

The Executive Directors then turned to the text of the draft declaration on censure or noncooperation in Attachment III to the staff statement. 1/

Mr. Nimatallah recalled that he had asked whether the reference to the lack of preparedness on the part of the member to adopt comprehensive adjustment policies, to which reference had been made in the previous draft of the declaration, could be reinserted, bearing in mind that the intention was to publish the declaration.

The General Counsel explained that the first two paragraphs of the draft declaration of censure were notations of fact by the Fund. The first paragraph noted the existence of arrears to the Fund, and the second the payments to other creditors. The third paragraph was a finding of noncooperation based strictly on the first two paragraphs, and it should be independent of those paragraphs. To meet Mr. Nimatallah's point, he proposed that the third paragraph read "finds that the member is not cooperating with the Fund toward the discharge of its financial obligations to the Fund." The result would be a separate, judgmental aspect, reflecting the substance of the staff statement under discussion by the Board, and following the two factual findings.

Mr. Nimatallah said that he could accept such an amendment.

Mr. Quirós considered that the final paragraph of the draft declaration, calling on all members to cooperate with the Fund toward the solution of the problems created by the member's arrears, suggested that the collaborative approach was being dismissed. Since the possibility of obtaining additional assistance had also been reduced, in his view, by the proposal to communicate with all Governors and most international and regional institutions, he asked what the rationale for such a call was, especially as it would be directed toward 145 out of 151 members, only 6 members being heavily in arrears to the institution.

The General Counsel responded that it had been left deliberately open to all members to determine how they could cooperate with the Fund. It was usual for the membership in general to cooperate without there being any need to specify the form of cooperation. There would be cases in

---

1/ Reproduced in Annex III.

which cooperation took the form of advice to the debtor member, and in other cases, possibly additional financial assistance, or technical assistance. The nature of the assistance would depend on the relationship between the member in default and any other member or members. It would be hard to define in one single declaration the nature of assistance expected from all members of the Fund.

Mr. Quirós remarked that the procedures being set up for dealing with members with overdue obligations to the Fund--an institution for which his chair had the highest regard and which should remain strong and effective--was similar to that followed by commercial enterprises. The problem of arrears was a quantitative one; if countries did not have the money to settle their arrears, they had to borrow it. The purpose of the draft declaration on noncooperation seemed to him to be nothing more than a wish, or "wishful thinking" that some of the Fund's 151 members assist the countries that were currently in arrears; those countries were all at present less developed countries, but in the future, especially after the final integration within the European Community in 1992, other Fund members might wish to use the institution's resources. Throughout the Fund's history, certain members had created safety nets for other members. He hoped that there would be a full understanding of that issue as the tables turned in the years ahead and other countries, including industrial countries, found themselves in need of a safety net as developing countries did at present.

Mr. Fogelholm reiterated his view that there should be no explicit or implicit link in the communications or declaration between arrears and compulsory withdrawal. Not only would the Fund probably not be able to carry out an implied threat, which was therefore completely pointless, but the Fund's flexibility in dealing with such a situation would be restricted by such a reference in the declaration. He proposed that the penultimate paragraph of the declaration be deleted.

Mr. Enoch suggested that the last three paragraphs be deleted. They were all directed at reminding the member of its responsibilities to the Fund and the membership at large, thereby diffusing the point of the draft declaration. The declaration on noncooperation would make a more powerful statement if it were more comparable with the declaration of ineligibility. It could consist simply of the first four paragraphs, excluding the reminders in the subsequent paragraphs.

Mr. Hogeweg said that he would regret the deletion of the reference to compulsory withdrawal, which was the ultimate sanction in the Articles and had its place in the sequence of steps under discussion. Certainly, actual implementation of that final step was highly undesirable and the hope was that it would never have to be applied. But he repeated his view that the whole point of the procedures was to provide a sufficiently strong deterrent to avoid having to apply the provision on compulsory withdrawal. Weakening the declaration would only increase the chance of applying that provision. The existence of the final step of compulsory withdrawal had to be recognized.

Mr. Enoch said that while his preference was for deleting the paragraph, if it was to be retained, he suggested reminding the member of the availability to the Fund of procedures under Section 22 of the By-Laws.

Mr. Nimatallah said that he agreed with Mr. Hogeweg that the declaration must cover the full sequence of events, including the communication and the reference to the provision on compulsory withdrawal. If Mr. Enoch's problem with the final paragraph was with the reference to cooperating with the Fund, he could accept its deletion although he would prefer to retain the entire text, with the amendment proposed by the General Counsel.

Mr. Prader said that he supported Mr. Enoch's proposal, and specifically, the deletion of the reference to compulsory withdrawal. If Mr. Hogeweg's logic was followed to its conclusion, the possibility of bringing the Fund to an end would also have to be included within the context of a sequence of deterrent steps.

Mr. Warner said that if his recollection was correct, the Board had been willing throughout its many discussions on arrears to recognize the existence of compulsory withdrawal, which was the Fund's longest-standing remedial landmark. He understood the point of view of Mr. Enoch and several other Directors, namely, that every Fund member was aware of the existence of the provision in the Articles and by deduction realized that it could be subject to it at some juncture--but as the debates on the issue proceeded, he had been drawing the conclusion that too many assumptions had been made about what Governors of the Fund or heads of state knew. Therefore, although there was merit in some of the drafting suggestions that had been made, he would be reluctant to delete the reference to compulsory withdrawal. Like Mr. Hogeweg and Mr. Nimatallah, he considered that the Fund, to be consistent, had to mention all of the relevant provisions relating to its remedial functions. Perhaps the wording could be amended simply to refer to the relevant provisions in the Articles and By-Laws. To omit any reference to those provisions would send a signal that the Fund had already decided that the step was so impractical that it would never be taken. He recognized that the provisions had important impractical characteristics, particularly in the cooperative environment of the Fund. But if the Fund never intended to give serious consideration to compulsory withdrawal, then it should admit it. He did not think that it could, and nor could its Governors. Therefore, the reference to compulsory withdrawal would have to be retained.

Mr. Nimatallah remarked that the statement in the draft declaration simply informed the member that, unless its arrears to the Fund were fully settled within a reasonable period, the procedures under Section 22 of the By-Laws leading to compulsory withdrawal could be considered. The wording seemed to be very flexible and in fact to be the minimum necessary.

Mr. Engert said that as he had mentioned at the previous meeting, the preference of his authorities was to delete the reference to compulsory

withdrawal, although the proposed wording was milder than the original version. While he recognized the logic of Mr. Hogeweg's position on the usefulness of making such a threat, he shared the view of Mr. Fogelholm and others that the threat would need to be credible, but it would be very difficult, if not impossible, to carry out such a threat. Notwithstanding those remarks, he believed that Mr. Warner had made a useful suggestion for finding even more benign wording to note that the procedure for compulsory withdrawal existed.

Mr. Enoch said that he too could go along if there was a consensus on the suggestion by Mr. Warner. As it stood, the wording in the draft declaration was so weak and so conditional that compulsory withdrawal did not appear to be much of a threat. After all, the Board would have to hold a series of discussions and take various decisions before it embarked on such a course. Once the Board had decided to consider moving ahead with compulsory withdrawal, then it could make a stronger statement. For the time being, he joined Mr. Engert in suggesting that it would be sufficient to remind the member of the existence of procedures under Section 22 of the By-Laws leading to compulsory withdrawal.

In response to a question by the Acting Chairman, Mr. Enoch said that he had in mind reverting to the issue after the Board had had experience, in individual cases, of the frequency with which the issue of invoking compulsory withdrawal had arisen.

Mr. Warner remarked that his concern was to close the declaration of noncooperation with a clear indication that one final step--the provisions leading to compulsory withdrawal--was left, and that the member would be subject to those provisions if it did not settle its arrears.

Mr. Goos said that he agreed fully with Mr. Warner and with the logic underlying the positions of Mr. Hogeweg and Mr. Nimatallah. Whatever form it took, there should be a reference to compulsory withdrawal as the last step of the procedures.

The Acting Chairman commented that the two positions were not necessarily inconsistent, if, as Mr. Enoch had suggested, it was indicated in the declaration, by including an appropriate reference in square brackets, that the decision to apply the provisions leading to compulsory withdrawal would be decided in the light of developments.

Mr. Goos stated that his preference was for a standard, comprehensive clause, which would in any event open up the discussion on the specific cases as they arose. Otherwise, there would never be enough support for moving toward the final step in the whole strategy at which the point of withdrawal might be reached. Placing the reference to that provision in square brackets, for use or not depending on the case in question, would lead to the loss of the deterrent effect.

Mr. Enoch recalled that as M.. Posthumus had mentioned in a previous discussion, the Board needed to undertake a further investigation of the

provisions on compulsory withdrawal, including the financial and other implications. His concern with the paragraph under discussion was its double conditional: unless its arrears were fully settled, the procedures leading to compulsory withdrawal could be considered. No doubt the Board would consider the concept of compulsory withdrawal in detail at a later stage, when it would be able to introduce wording in the declaration on noncooperation along the lines proposed in Attachment III. Indeed, the Board might even be able to agree on stronger wording, in keeping with the point made earlier by Mr. Hogeweg that empty threats were worse than no threats at all. But it seemed to him to be premature to include reference to the provisions on compulsory withdrawal until there was a consensus that invoking them would be useful. He was not suggesting that the issue be raised in individual country cases.

On a final point of drafting, Mr. Enoch suggested that the reference to a member having to fully settle its arrears was not consistent with the Fund's policy, which was to ask the country to embark on cooperation with the Fund.

Mr. Kiriwat stated that the reference to compulsory withdrawal should be deleted, especially if the declaration was to be published. It was not yet clear how the Fund would proceed with steps leading to compulsory withdrawal.

Mr. Warner said that Mr. Enoch's concern about the conditional wording of the paragraph could be met by modifying it to state directly that members that failed to cooperate with the Fund were subject to the provisions of Section 22 of the By-Laws.

Mr. Nimatallah suggested that the penultimate paragraph of the draft declaration could, like the preceding paragraph, remind the member that it would face the consequences of Section 22 of the By-Laws if it did not cooperate with the Fund. There was no need to refer to fully settling its arrears, as Mr. Enoch had suggested, or to mention that that be done within a reasonable period of time.

Mr. Evans asked the staff whether it was possible to define the circumstances under which the procedures of Section 22 of the By-Laws would be considered, if they were not already defined, and specifically, with respect to the settlement of arrears as opposed to cooperation with the Fund.

The General Counsel responded that the ground for compulsory withdrawal had to be a breach of obligation to the Fund. The nondischarge of financial obligations was such a breach and therefore could give rise to compulsory withdrawal. Noncooperation as such was not a breach of obligation. The meaning of the declaration was that if, in addition to not discharging its obligations, the member did not cooperate, then compulsory withdrawal might be considered. But noncooperation could not be a substitute for a breach of obligation. An acceptable formulation would be to

remind the member that unless it resumed cooperation with the Fund, the procedures under Section 22 of the By-Laws could be considered.

Mr. Appetiti remarked that his chair was in favor of maintaining a reference to compulsory withdrawal in the declaration.

Mr. Fogelholm said that he maintained his view that it would be better not to refer to compulsory withdrawal, for the reasons explained by Mr. Enoch. The only acceptable language would be that suggested by Mr. Enoch, namely, to refer to the existence of the procedures.

Mr. Nimatallah remarked that he had simply been suggesting that the reference in the earlier paragraphs to the member not cooperating and urging it to cooperate with the Fund should be succeeded by a reminder that the failure to do so would have certain consequences.

Mr. Goos remarked that some reference to compulsory withdrawal would be needed because, if the declaration was to be published, a reference to certain sections of the By-Laws would be meaningless to the public at large.

Mr. Engert said that he agreed with Mr. Goos.

The General Counsel said that there were two ways of formulating the final paragraph. First, the Fund could remind the member that members in breach of their obligations to the Fund may be subject to the procedures under Section 22 of the By-Laws leading to compulsory withdrawal. Second, in line with Mr. Enoch's suggestion, the Fund could remind the member of the availability to the Fund of procedures under Section 22 of the By-Laws on compulsory withdrawal. The main difference would be the absence of any reference to breach of obligation.

Mr. Enoch and Mr. Warner said that they could accept the wording proposed by the General Counsel.

Mr. Appetiti and Mr. Engert said that they too could accept the General Counsel's proposals.

Mrs. Ploix asked whether the skepticism that had been expressed about the approach would be reflected anywhere, for instance, in a summing up.

The Acting Chairman observed that the record would show where Directors had expressed reservations about certain issues.

The General Counsel, in response to a question by Mr. Kafka, said that it was his understanding that the Board had agreed that the declaration could be published, if Directors having a majority of the votes so decided. That agreement had been reached during the Board's discussion of the two staff papers on the legal aspects of censure or declaration of noncooperation (EBS/89/128, 6/26/89) and the issue of suspension of membership (SM/89/127, 6/28/89).

The Acting Chairman inquired whether Mr. Enoch's proposal to delete the final paragraph of the draft declaration was acceptable.

Mr. Warner considered that Mr. Enoch's suggestion had been constructive because the declaration was directed to the member in breach, whereas the final paragraph was making a universal appeal to all members that was not appropriate in such a declaration.

The Executive Directors agreed to delete the last paragraph of the draft declaration.

Mr. Hogeweg noted that there seemed to be some inconsistency between the first and the second halves of the second paragraph of the declaration, which mentioned, respectively, payments to other creditors but not to the Fund--or not to the same extent--and subsequently to the member ignoring the preferred creditor status of the Fund. The question in his mind was whether equal payments to the Fund and to other creditors implied equal creditor status rather than preferred creditor status. Perhaps reference could be made to the member having made payments to other creditors while not discharging its obligations to the Fund in conformity with the preferred creditor status that members are expected to give to the Fund.

Mr. Warner recalled that the same drafting problem had arisen in a different context, namely, that of how to define preferred creditor status for the Fund. The Fund's standing relative to that of the World Bank, and potentially other international institutions, had been raised, and it had been agreed that the Fund was a preferred creditor, not the preferred creditor.

The General Counsel noted that the second paragraph of the draft declaration was indeed worded in a somewhat guarded fashion because the Fund was not the preferred creditor but a preferred creditor. There were two cases in which the Fund's preferred creditor status was clearly disregarded. The first was when payments were made to other creditors and no payments were made to the Fund. In the second case, higher payments were made to other creditors than to the Fund. If those distinctions were not made, and it was stated simply that payments were being made to other creditors inconsistent with the Fund's preferred creditor status, there would be no factual basis for determining the Fund's preferred creditor status, other than on an ad hoc, case-by-case basis.

Mr. Goos said that he wondered whether it would not be preferable to place the entire paragraph in square brackets, because appropriate wording would have to be sought depending on the particular circumstances of the country in arrears.

The Director of the Exchange and Trade Relations Department said that the suggestion of Mr. Goos was constructive, especially as it might be necessary to discuss a country's situation with the World Bank in order to take parallel action.

The Acting Chairman noted that the statements of fact underlying the first two paragraphs would thus be determined in individual cases.

Mr. Evans asked whether it would then be sufficient simply to note that the member had ignored the preferred creditor status that members were expected to give to the Fund.

Mr. Goos commented that such a statement might not apply to all cases. For instance, a member might have discharged all its obligations to creditors, including the Fund, at the same rate. But that would not mean that the Fund's preferred creditor status had been respected. Similarly, if no payments at all were made within a certain period to any creditor, the Fund's preferred creditor status would not be respected. But that would not prevent the Fund from finding that a member was not cooperating with it, and it would have to make a decision on the basis of the specific circumstances.

Mr. Evans remarked that the entire paragraph should thus be placed in square brackets.

Mr. Enoch remarked that presumably preferred creditor status in its purest form meant that the preferred creditor received full payment before any payments were made to a nonpreferred creditor. The idea was not to achieve equality of treatment for the Fund, but primacy for its full claims. Certainly, he agreed with Mr. Goos that the matter might be easier to deal with if the entire paragraph was placed in square brackets. At the same time, the concept of preferred creditor status must not be relegated to second place.

Mr. Goos said that he agreed fully with Mr. Enoch's remarks.

The Director of the Exchange and Trade Relations Department recalled that the Board had decided in its earlier discussions that the concept of preferred creditor status was not a legal but a practical concept, which it was wise not to try to define with great precision. Indeed, there could be circumstances in which the paragraph in the draft declaration would not apply at all. Therefore, the suggestion to place it in brackets, for consideration at the time in the specific circumstances, seemed sensible.

The Executive Directors agreed to place the second paragraph of the draft declaration on noncooperation in square brackets.

The Director of the Exchange and Trade Relations Department noted that in the light of the discussion at the previous meeting, the staff had revised the paragraph relating to the procedure for communicating with selected Governors, which would read as follows:

> The Managing Director would in each case recommend to the Executive Board whether a communication should be sent to a select set of Fund Governors or to all Fund Governors. If it

were considered that it should be sent to a select set of Fund Governors, an informal meeting of Executive Directors would be held, some six weeks after the emergence of overdues, to consider the thrust of the communication. Alternatively, if it were considered that the communication should be sent to all Fund Governors, a formal Board meeting would be held to consider the/a draft text and the preferred timing. A sample text for a communication to all Fund Governors is set out in Attachment I. It would also be understood that, in some circumstances, the Managing Director might wish to recommend advancing the Executive Board's consideration of the complaint regarding the member's overdues.

Mr. Adachi asked whether, when a letter was sent to a selected set of Governors, the Executive Director for the country to receive the letter would have an opportunity to review the communication beforehand.

The Director of the Exchange and Trade Relations Department said that he felt sure that management would wish to have the input of the Executive Director concerned.

The Executive Directors then resumed their consideration of the draft second letter to all Governors and certain international financial institutions, based on a further revision of the wording in the light of the discussion at the previous meeting. 1/

The Treasurer explained that the first paragraph of the draft second letter had been amended to note that the Managing Director was writing to all Governors, in response to the request during the previous meeting that it should be clear to whom the letter was addressed. In the second paragraph, the reference to the member not having responded to earlier requests to settle its arrears had been deleted, because the same thought was already covered in the fourth paragraph. The latter paragraph had been shortened considerably and merged with the final paragraph in the second revision of the draft second letter, which had been considered at the previous meeting. Reference had been made to the Fund having developed a set of procedures for dealing, as appropriate, with members that had protracted overdue financial obligations, in place of the pointed reference to the intensified collaborative approach in helping a member to clear its arrears and restore its position in the international financial community. The sentence referring to the matter of compulsory withdrawal had been placed in square brackets because the staff had not gained a clear impression from the previous meeting as to whether or not it should be retained. The final sentence of the fourth paragraph no longer referred to the Fund appreciating assistance in supporting its continuing

---

1/ Reproduced in Annex II.

efforts to resolve an arrears problem but to appreciation for whatever action the addressee considered appropriate to help bring about an early resolution of the arrears problem.

Mr. Kafka observed that it could only be helpful to retain some mention of the collaborative approach, even if qualified with the words "as appropriate."

The Acting Chairman noted that the desire of several Directors to mention the intensified collaborative approach could perhaps be met if the revised text referred to a set of procedures, including the intensified collaborative approach. Less emphasis would then be given to that approach than in the preceding version.

Mr. Warner remarked that although the line between the intensified collaborative approach and a collaborative approach was a fine one, the latter seemed to be an integral part of the Fund's system and to be worthy of mention, whereas the former inferred that a support group was about to be established. It would be premature to indicate in such a communication that the establishment of such a group was imminent. Concerns about moral hazard would also arise. There would be no harm in saying that the collaborative approach was an available alternative under the appropriate conditions.

The Executive Directors accepted the Acting Chairman's proposal to refer to a set of procedures, including the intensified collaborative approach.

The Treasurer said that the second sentence of the fourth paragraph might be clearer and apply more generally to both the procedures for members not the subject of the intensified collaborative approach, as well as those that were, if it stated that the application of the procedures for members in arrears had not resulted in the member taking steps that could be expected to resolve promptly the arrears problem.

Mr. Hogeweg suggested that as the communication to all Governors was itself part of the procedures, it should perhaps be stated that the application of the procedures for members in arrears up to now had not resulted in steps to resolve the problem.

The Director of the Exchange and Trade Relations Department remarked that it must be borne in mind that the set of procedures mentioned in the first sentence was not necessarily identical to the procedures mentioned in the second sentence, as having been applied up to now.

Mr. Appetiti said that he agreed that the fact that the set of procedures, including the intensified collaborative approach, had been developed did not imply that it had begun to be implemented. Presumably, the fact that the letter was being sent to Governors also indicated that that approach had not been launched. Therefore, he could accept Mr. Hogeweg's proposed amendment.

Since agreement had been reached on the declaration of noncooperation, including a reference to Section 22 of the By-Laws, which would lead to compulsory withdrawal, he understood that the square brackets could be removed from the sentence in paragraph 4 on that matter, Mr. Appetiti concluded.

Mr. Fogelholm stated that he could not go along with deleting the square brackets and thus retain the reference to compulsory withdrawal. The declaration of noncooperation on which agreement had been reached was worded in a fairly neutral way, whereas the sentence in square brackets would again clearly link the declaration to compulsory withdrawal. He was not even sure that it was necessary to draw the attention of Governors to the Fund's By-Laws, especially as the threat of compulsory withdrawal was an empty one in any event. If reference had to be made to compulsory withdrawal in the letter, it should be made in a more neutral way.

Mr. Nimatallah said that he failed to understand why compulsory withdrawal was viewed by some as an empty threat. Even if there was only one case of a member actually facing the threat of compulsory withdrawal, because it continued not to cooperate with the Fund, the possible application of Section 22 of the By-Laws should at least be mentioned.

Mr. Appetiti said that he agreed with Mr. Fogelholm that what was needed was to describe in the sentence under discussion the declaration of noncooperation on which Directors had just reached agreement.

Mr. Prader remarked that he too would be in favor of neutral wording. Discussions about giving serious consideration to compulsory withdrawal should be started only when it was felt that the intensified collaborative approach was not working.

Mr. Hogeweg said that of course the declaration of noncooperation itself was a most serious step that did not derive its seriousness from the fact that the next step might be different. Perhaps the two stages should be separated in the wording of the letter.

Mr. Ghasimi considered that referring to a member being subject to a declaration of noncooperation would by itself embody the idea conveyed in the sentence in brackets, as the text of the declaration itself made clear. Once a member was the subject of a declaration of noncooperation it was subject to procedures leading to compulsory withdrawal.

Mr. Warner remarked that it was only in the event of a declaration of noncooperation that exposure to the provisions of Section 22 of the By-Laws would occur, but the two steps were separate. Perhaps it should be said that in the event of such a declaration, the member might at some subsequent state be subject to the provisions of Section 22 of the By-Laws.

Mr. Hogeweg said that it had to be clear that the declaration of noncooperation did not necessarily lead to the application of those provisions.

The General Counsel suggested that the fact that there were two separate steps--declaration of noncooperation and compulsory withdrawal--that were not necessarily linked directly could perhaps be made clear if it was mentioned that in the event of a declaration of noncooperation, the member could subsequently be subject to the procedures under Section 22 of the By-Laws leading to compulsory withdrawal.

Mrs. Hepp said that she fully agreed with Mr. Ghasimi that the sentence in square brackets should be deleted altogether.

Mr. García said that he too also supported the deletion of the sentence in square brackets. It was inappropriate to mention even the possibility of the subsequent step in the letter to Governors.

Mr. Nimatallah considered that including the reference to compulsory withdrawal as a possible consequence of a declaration of noncooperation would alert Governors to the seriousness of the situation of the member in arrears, even though the letter was to be sent before such a declaration was issued. The need for the help of all Governors in avoiding such an outcome would be conveyed more effectively.

Mr. Kafka asked whether the member could not be subject to compulsory withdrawal without having been the subject of a declaration of noncooperation.

The General Counsel responded that Mr. Kafka's assumption was correct. But the idea expressed in the letter to Governors was that the Fund's intention was not to initiate the procedures on compulsory withdrawal without first issuing the declaration of noncooperation. The whole purpose of the approach under consideration was to introduce an intermediate step between the declaration of ineligibility and compulsory withdrawal.

Mr. Kafka commented that the procedures that had been proposed were not very practical. The only workable solution would be to make a determined effort to implement the intensified collaborative approach.

Mr. Warner asked what recourse the Fund would have in the case of noncollaboration.

Mr. Kafka responded that he would have no problem with compulsory withdrawal in a case in which a member willfully refused to collaborate and to meet its obligations.

Mr. Warner considered that that was the point that was being reached.

Mr. Nimatallah remarked that the alternative solution preferred by Mr. Kafka, of giving the intensified collaborative approach a chance to work, had the drawback of delaying a solution. The objective was to speed up the process and give member countries that were making no effort to settle their arrears an incentive to come forward and collaborate with the Fund. Everyone was in favor of the collaborative approach, but in waiting for it to take effect, the membership carried a heavy burden. Therefore, the reality of eventual compulsory withdrawal should be mentioned in the communication to Governors, if the objective was to inform them and to encourage them to assist a country in settling its arrears promptly.

The Director of the Exchange and Trade Relations Department remarked that compulsory withdrawal should be mentioned partly because, as had been pointed out, all Governors should know that that was a possibility, but also because the letter would presumably be followed within a few weeks by a declaration of noncooperation that would be published and that would or could refer to compulsory withdrawal.

Mr. Engert said that as he had mentioned previously, his authorities were skeptical about the compulsory withdrawal approach. However, since it might be necessary, in order to reach an agreement, to mention compulsory withdrawal in the letter, the various concerns that had been expressed about such a reference might be met by wording which would explain that the declaration of noncooperation would be a most serious step that would refer, inter alia, to Section 22 of the By-Laws concerning compulsory withdrawal. The issue would then be stated clearly, more or less along the lines of the declaration itself, but in a relatively nonthreatening way.

Mr. Enoch said that he could go along with Mr. Engert's suggestions. It might be helpful to mention also that the declaration of noncooperation would involve publication in order to draw the attention of Governors to the issue.

Mr. Nimatallan said that he wondered whether the final sentence of the letter, stating that the Board would review again the member's arrears, should not refer to the problem or case of the member's arrears.

The Director of the Exchange and Trade Relations Department said that Mr. Nimatallah's point could be met by stating that the Executive Board will review again the position of the member with regard to its arrears.

The Acting Chairman observed that the staff would incorporate the amendments that had been discussed into the draft statement and attachments and circulate a revised version. Many Directors had expressed skepticism about the overall approach but at the same time a willingness to go along with it. The opposition to specific parts of the procedures on the part of many Directors had been stated for the record. It could not therefore be said that a consensus had emerged. The revised text would be circulated for review by Executive Directors on a lapse of time

basis, leaving it to Directors to decide whether or not it was necessary to bring the matter to the agenda.

The revised statement reflecting the sense of the meeting, as circulated for approval by Executive Directors prior to the close of business on August 17, 1989, read as follows:

> The Fund, as a cooperative institution, relies on the mutually supportive actions of its membership in all areas of its endeavors. Overdue financial obligations are a breach of obligations to the Fund and are demonstrably a noncooperative action, which imposes financial costs on the Fund's membership, impairs its capacity to assist members, and more generally weakens the Fund's ability to perform its broader responsibilities in the international financial system.
>
> As the experience with arrears demonstrates, countries which accumulate arrears to the Fund also damage themselves, in part through the deterioration which inevitably follows in their financial relations with other creditors. When arrears exist the Fund is not able to provide its own assistance and its effectiveness is diminished as a catalyst for helping the country restore regular financial relations with other creditors.
>
> This statement outlines procedures aimed at preventing the emergence of overdue financial obligations to the Fund and the elimination of existing overdues, including protracted arrears. The need for flexibility in the implementation of the Fund's policies dealing with overdues has been stressed in the past; flexibility must continue to be exercised in order to take account of the specific circumstances of the member. Nonetheless, a balance must be struck between the need for appropriate flexibility and the need for clear and credible procedures that act as a deterrent to members against incurring arrears and to encourage members with overdues to become current.
>
> Arrears prevention
>
> The importance of preventing new cases of arrears has been stressed by the Executive Board. As noted in the past, our best safeguard is the quality of Fund arrangements and we will continue to direct our efforts to ensure that arrangements of the highest quality are placed before the Board. These efforts would include assisting members to design strong and comprehensive economic programs, careful attention to access levels and phasing, explicit assessment of a member's capacity and willingness to repay the Fund, and adequate assurances regarding external financing during the period of the Fund arrangement. Special understandings with creditors and donors may also need to be sought in certain cases to help assure progress toward

external viability. In some cases, specific financial or administrative arrangements--designed to ensure that forthcoming obligations to the Fund are settled on time--will be used to increase the assurance that the Fund's resources will be repaid on time. Moreover, the importance of members remaining current on obligations falling due and observing the Fund's preferred creditor status will continue to be stressed.

The Fund's response to overdue obligations

The Fund has developed a set of procedures for dealing with members with overdue financial obligations which are designed to bring about a reduction and the eventual elimination of these overdue obligations. In addition to the procedures set out below, the Fund makes an effort to assist members willing to cooperate to eliminate their arrears through the design and implementation of appropriate policies as well as to help members adopting these policies to secure the necessary financial support.

The procedures initiated immediately after a member falls into arrears provide for a sequence of actions by management, the staff, and the Executive Board.

- Whenever a member fails to settle an obligation on time, the staff immediately sends a cable urging the member to make the payment promptly; this communication is followed up through the office of the Executive Director concerned.

- When an obligation has been outstanding for two weeks, management sends a communication to the Governor for that member stressing the seriousness of the failure to meet obligations to the Fund and urging full and prompt settlement. The Executive Board understands that the Governor will bring this communication and the circumstances that gave rise to it to the attention of his authorities at the highest level. The communication to the Governor would also note that unless payment is received in due course, the Managing Director would intend to raise with the Executive Board the possibility of communicating with Governors of the Fund concerning the situation. The Managing Director has on occasion raised the matter of overdue financial obligations to the Fund directly with the head of government of the member concerned, and he would intend to continue to do so in those cases where he believes it would be a useful procedure.

- The Managing Director notifies the Executive Board normally one month after an obligation has become overdue.

- When the longest overdue obligation has been outstanding for six weeks, the Managing Director informs the member

concerned that unless the overdue obligations are settled a complaint will be issued to the Executive Board in two weeks' time.

The Managing Director would in each case recommend to the Executive Board whether a communication should be sent to a selected set of Fund Governors, or to all Fund Governors. If it were considered that it should be sent to a selected set of Fund Governors, an informal meeting of Executive Directors would be held, some six weeks after the emergence of overdues, to consider the thrust of the communication. Alternatively, if it were considered that the communication should be sent to all Fund Governors, a formal Board meeting would be held to consider a draft text and the preferred timing. A sample text for a communication to all Fund Governors is set out in Attachment I.

- A complaint by the Managing Director is issued two months after an obligation has become overdue, and is given substantive consideration by the Executive Board one month later. At that stage, the Executive Board has usually decided to limit the member's use of the general resources, and if the member has overdue obligations in the SDR Department, to suspend its right to use SDRs, and has provided for a subsequent review of the decision. This and subsequent review periods would normally not exceed three months. It would be understood that the Managing Director may recommend advancing the Executive Board's consideration of the complaint regarding the member's overdues.

- The Annual Report and the financial statements identify those members with overdue obligations outstanding for more than six months.

Beyond these procedures, the Executive Board has expressed its intention to provide that a member must first discharge its overdue financial obligations to the General Resources Account before it would be permitted to pay for an increase in its quota under the Ninth General Review, and that, in the event the quota payment were not made within a prescribed period, the proposal for an increase in the member's quota would lapse.

Another measure being considered by the staff relates to the possibility of withholding SDR allocations for members with arrears in the General Department. This measure would require an amendment of the Articles and will be examined further in the next Six-Monthly Report on Overdue Financial Obligations.

Declaration of ineligibility

- If a member persists in its failure to settle its overdue obligations to the Fund, the Executive Board declares the member ineligible to use the general resources of the Fund.

The timing of the declaration of ineligibility would vary according to the Board's assessment of the specific circumstances and of the efforts being made by the member to fulfill its financial obligations to the Fund. The procedures for dealing with members with protracted arrears that have been declared ineligible include further reviews at intervals of not more than six months.

- For members with protracted arrears willing to cooperate with the Fund in settling those overdues, the Fund has adopted an intensified collaborative approach, which incorporates exceptional efforts by the international financial community.

- For members that are judged not to be cooperating actively with the Fund, remedial measures would be applied.

- Members not showing a clear willingness to cooperate with the Fund have been informed that in these circumstances the provision of technical assistance would be inappropriate, but the Fund would reconsider providing technical assistance once the member has resumed active cooperation. The Managing Director may also limit technical assistance provided to a member, if in his judgment that assistance was not contributing adequately to the resolution of the problems associated with overdues to the Fund.

- A further remedial measure in cases of protracted arrears would be communications with all Governors of the Fund and with heads of certain international financial institutions. Use of such communications would normally be raised for the Executive Board's consideration at the time of the first post-ineligibility review of the member's arrears. At that time the staff would prepare a draft text of a communication along the lines set out in Attachment II to this statement. It should be noted that the Fund's communication to certain other international financial institutions, such as the three main regional development banks (Asian Development Bank, African Development Bank, Inter-American Development Bank), like its communication to the Governors, would not request the addressee to take specific actions and would leave any action to the institution's discretion. This does not preclude informal contacts with other international financial institutions. The staff would intend to propose to send this latter type of communication on the occasion of the next post-ineligibility review for members that at present have arrears that have been outstanding for a protracted period, in the event the Executive Board judges that the member concerned is not cooperating actively with the Fund in efforts to resolve the problem of its overdue financial obligations to the Fund.

Censure or declaration of noncooperation

- A declaration of censure or noncooperation would come as an intermediate step between a declaration of ineligibility and a resolution on compulsory withdrawal. The decision as to whether to issue such a declaration would be based on an assessment of the member's performance in the settlement of its arrears to the Fund and of its efforts, in consultation with the Fund, to follow appropriate policies for the settlement of its arrears. Three related tests would be germane to this decision regarding (i) the member's performance in meeting its financial obligations to the Fund taking account of exogenous factors that may have affected the member's performance; (ii) whether the member had made payments to other creditors while continuing to be in arrears to the Fund; and (iii) the preparedness of the member to adopt comprehensive adjustment policies. The declaration would follow any communication to Governors after ineligibility and would be considered at a subsequent post-ineligibility review. The period between such communications and the declaration could be about six months, but this time period would be determined on a case-by-case basis.

A draft of the declaration is set out in Attachment III. The actual declaration would be based on this draft text taking account of the circumstances of the individual case. The declaration would be adopted by the Executive Board and published.

Other remedial measures

- On suspension of membership, Directors noted the necessity of amending the Fund's Articles of Agreement to provide for suspension of membership. Some Directors showed an interest in introducing a provision into the Articles of Agreement under which the voting rights of a member that has been declared ineligible to use the Fund's general resources could be suspended. However, most Directors felt that it would not be advisable to propose an amendment of the Fund's Articles of Agreement at this time, but that this matter could be reconsidered in the future.

- Finally, Directors noted the availability to the Fund of procedures under Section 22 of the By-Laws on compulsory withdrawal. These procedures would only be pursued once the Fund has exhausted all other possible avenues to redress the problem of overdue financial obligations and, despite a declaration of noncooperation, the member has not exhibited a willingness to cooperate with the Fund. The Articles of Agreement and the By-Laws provide for procedures for settling claims by the Fund on a member in the event that it withdraws from the Fund. If

the procedures were initiated, the staff would prepare an analysis of the effect of the member's withdrawal on the Fund's financial position.

APPROVED: March 26, 1990

JOSEPH W. LANG, JR.
Acting Secretary

ATTACHMENT I

Draft First Letter to All Governors

Dear :

The Executive Board has considered the complaint which was recently issued regarding [member]'s overdue financial obligations to the Fund. In considering this complaint the Executive Board has agreed that I write to all Governors of the Fund to draw their attention to this development. Prompt and effective actions now by [member] and the international community would avoid a further deterioration of this situation including the possibility of declaring [member] ineligible to use the general resources of the Fund, would permit these overdues to be cleared before their magnitude makes the problem more intractable, and before they place a financial burden on other members.

[Paragraph on background circumstances of member leading to the emergence of arrears, the views of the member regarding its overdue obligations, and the member's intended approach for addressing the problem of its overdue obligations. This paragraph would be tailored to the specific circumstances of the member concerned.]

The Executive Board is very concerned about these developments which have serious potential implications both for the [member] and for the Fund as a whole, if the problem is not resolved early. The existence of these overdue financial obligations to the Fund precludes the Fund from extending financial assistance to the member. In addition, experience to date indicates that when a country incurs arrears to the Fund its financial relations with other creditors are also likely to deteriorate. These arrears also have an adverse impact on the Fund as an international financial cooperative, which is the central monetary institution in the international monetary system. As you are aware, overdue obligations, if they are not settled, place a financial burden on other members: on the Fund's debtor members in the form of higher charges and the Fund's creditors in the form of reduced remuneration.

The Fund would greatly appreciate any assistance in urging the member to effect the full and prompt settlement of its overdue obligations to the Fund.

Sincerely yours,

Michel Camdessus
Managing Director and
Chairman of the Executive Board

ATTACHMENT II

Draft Second Letter to All Governors and
Certain International Financial Institutions

Dear :

The Executive Board has reviewed the overdue financial obligations of [member] and its circumstances. In this context it agreed that I write to all Governors of the Fund to seek their assistance in resolving the problem of [member]'s overdue financial obligations to the Fund [and that I inform at the same time the heads of [names of certain international financial institutions]].

As you know, [member] was declared ineligible to use the general resources of the Fund on [date], as it had failed to meet its financial obligations to the Fund. As of [date], [member]'s overdue financial obligations to the Fund amounted to SDR[ ] million and the longest overdue obligation had been outstanding for [ ] months. As you are aware, these overdue obligations reduce Fund resources available to help other members and place a financial burden on debtor members in the form of higher charges and on creditor members in the form of reduced remuneration.

[Paragraph on background circumstances of member leading to the emergence of arrears, the views of the member regarding its overdue obligations, and the member's intended approach for addressing the problem of its overdue obligations. This paragraph would be tailored to the specific circumstances of the member concerned.]

The Fund has developed a set of procedures, including the intensified collaborative approach, for dealing, as appropriate, with members that have overdue financial obligations outstanding for a protracted period. The application of the procedures for members in arrears up to now has not resulted in [member] taking steps that could be expected to resolve promptly the problem of its arrears to the Fund. If, in the period prior to the next review of [member]'s arrears, [member] does not take action to demonstrate its willingness to resume active cooperation with the Fund toward the resolution of the problem of its arrears, [member] may be subject to a declaration of noncooperation. This would be a most serious step that would involve the publication of this declaration, which would refer, inter alia, to the availability to the Fund of procedures under Section 22 of the By-Laws on compulsory withdrawal of [member] from the Fund. The Fund's Executive Board has emphasized the critical stage that has been reached with respect to [member]'s arrears and has stressed its sincere hope that the consideration of further steps will be unnecessary. The Fund would appreciate your [Government/institution] taking whatever actions it considers appropriate to help bring about an early resolution of this situation.

The Executive Board will review again the position of [member] with regard to its arrears to the Fund not later than [date].

Sincerely yours,

Michel Camdessus
Managing Director and
Chairman of the Executive Board

ATTACHMENT III

Draft Declaration on Censure or Noncooperation

The Fund notes that, since the declaration of ineligibility on [date], the member has remained in arrears in its financial obligations to the Fund, thus persisting in its failure to fulfill its obligations under the Articles, and that the level of its arrears has not decreased (or has increased);

[notes that the member has made payments to other creditors while not discharging its financial obligation to the Fund (or not to the same extent), thus ignoring the preferred creditor status that members are expected to give to the Fund;]

finds that the member is not cooperating with the Fund toward the discharge of its financial obligations to the Fund;

urges the member to discharge its financial obligations to the Fund promptly and to cooperate with the Fund;

reminds the member that arrears to the Fund, which is a cooperative institution, are detrimental to the whole membership of the Fund in that they hamper the proper performance by the Fund of its function of assisting members facing balance of payments difficulties;

reminds the member that members in breach of their obligations to the Fund may be subject to the procedures under Section 22 of the By-Laws leading to compulsory withdrawal.

Mr. El Kogali informed the Secretary on September 14 that his intention had been to request that the matter of the Fund's procedures for dealing with members with overdue financial obligations to the Fund should be placed on the agenda of the Executive Board for further consideration before being approved, even on a lapse of time basis. It had been his view that the second test of cooperation relating to whether the member had made payments to other creditors while continuing to be in arrears to the Fund did not reflect--in the section on censure or declaration of noncooperation--the flexibility that several Directors, including himself, had advocated, based on practical considerations. He had thought that the statement should leave no doubt that the Fund was expected to make its decision on the question of censure or declaration of noncooperation in light of the particular circumstances of each case. As he recalled, it had been the understanding that the Board considered the case-by-case approach to be essential to the effective application of all the procedures outlined in the staff statement, including the criteria mentioned as being germane to reaching a decision on the declaration of censure or noncooperation. He had also understood that the case-by-case approach meant, as suggested in the second sentence of the paragraph on the matter of censure, that the Board would exercise judgment on the member's performance in settlement of its arrears to the Fund and on its efforts to implement appropriate adjustment policies. While it had not appeared necessary for him to place the matter on the Board's agenda, based on those understandings, he wished his concerns to form part of the record on the subject.

Revised Statement prepared by the Staff on the Fund's Procedures for Dealing with Members with Overdue Obligations to the Fund
Executive Board Meeting
July 27, 1989

The Fund, as a cooperative institution, relies on the mutually supportive actions of its membership in all areas of its endeavors. Overdue financial obligations are a breach of obligations to the Fund and are demonstrably a noncooperative action, which imposes financial costs on the Fund's membership, impairs its capacity to assist members, and more generally weakens the Fund's ability to perform its broader responsibilities in the international financial system.

As the experience with arrears demonstrates, countries which accumulate arrears to the Fund also damage themselves, in part through the deterioration which inevitably occurs in their financial relations with other creditors. When arrears exist the Fund is not able to provide its own assistance or serve as an effective catalyst in helping the country restore regular financial relations with other creditors.

This statement outlines the procedures aimed at preventing the emergence of overdue financial obligations to the Fund and the elimination of existing overdues, including protracted arrears. The need for flexibility in the implementation of the Fund's policies dealing with overdues has been stressed in the past, and must continue, in order to take account of the specific circumstances of the member. Nonetheless, a balance must be struck between the need for appropriate flexibility and the need for clear and credible procedures that act as a deterrent to members to incur arrears and to encourage members with overdues to become current.

Arrears prevention

The importance of preventing new cases of arrears has been stressed by the Executive Board. As noted in the past, our best safeguard is the quality of Fund arrangements and we will continue to direct our efforts to ensure that arrangements of the highest quality are placed before the Board. These efforts would include assisting members to design strong and comprehensive economic programs, careful attention to access levels and phasing, explicit assessment of a member's capacity and willingness to repay the Fund, and adequate assurances regarding external financing during the period of the Fund arrangement. Special understandings with creditors and donors may also need to be sought in certain cases to help assure progress toward external viability. In some cases, specific financial or administrative arrangements--designed to ensure that forthcoming obligations to the Fund are settled on time--will be used to increase the assurance that the Fund's resources will be repaid on time. Moreover, the importance of members remaining current on obligations falling due and observing the Fund's preferred creditor status would continue to be stressed.

The Fund's response to overdue obligations

The Fund has developed a set of procedures for dealing with members with overdue financial obligations which are designed to bring about a reduction and the eventual elimination of these overdue obligations. In addition to the procedures set out below, the Fund makes an effort to assist members eliminate arrears through the design and implementation of appropriate policies as well as help members adopting these policies to secure the necessary financial support.

The procedures initiated immediately after a member falls into arrears provide for a sequence of actions by management, the staff, and the Executive Board.

- Whenever a member fails to settle an obligation on time, the staff immediately sends a cable urging the member to make the payment promptly; this communication is followed up through the office of the Executive Director concerned.

- When an obligation has been outstanding for two weeks, management sends a communication to the Governor for that member stressing the seriousness of the failure to meet obligations to the Fund and urging full and prompt settlement. The Executive Board understands that the Governor will bring this communication and the circumstances that gave rise to it to the attention of his authorities at the highest level. The communication to the Governor would also note that unless payment is received shortly, the Managing Director would intend to raise with the Executive Board the possibility of communicating with certain Governors of the Fund concerning the situation. The Managing Director has on occasion raised the matter of overdue financial obligations to the Fund directly with the head of government of the member concerned, and he would intend to continue to do so in those cases where he believes it would be a useful procedure.

- The Managing Director notifies the Executive Board normally one month after an obligation has become overdue.

- When the longest overdue obligation has been outstanding for six weeks, the Managing Director informs the member concerned that unless the overdue obligations are settled shortly a complaint will be issued to the Executive Board.

- Under the procedure for communication with selected Governors, depending on the circumstances of the case, the Managing Director would also intend to convene a meeting of the Executive Board to discuss the situation. For this meeting, a proposed text of the communication to be sent to a list of Governors selected by the Managing Director would be prepared by the staff for the consideration of Executive Directors. The communication would be sent with the concurrence of Executive Directors. A sample text is set out in Attachment I.

- A complaint by the Managing Director is issued two months after an obligation has become overdue, and is given substantive consideration by the Executive Board one month later. At that stage, the Executive Board has usually decided to limit the member's use of the general resources, and if the member has overdue obligations in the SDR Department, to suspend its right to use SDRs, and has provided for a subsequent review of the decision. This and subsequent review periods would normally not exceed three months.

- The Annual Report and the financial statements identify those members with overdue obligations outstanding for more than six months.

Beyond these procedures, the Executive Board has expressed its intention to provide that a member must first discharge its overdue financial obligations to the General Resources Account before it would be permitted to pay for an increase in its quota under the Ninth General Review, and that, in the event the quota payment were not made within a prescribed period, the proposal for an increase in the member's quota would lapse.

Declaration of ineligibility

If a member persists in its failure to settle its overdue obligations to the Fund, the Executive Board declares the member ineligible to use the general resources of the Fund. The timing of the declaration of ineligibility would vary according to the Board's assessment of the specific circumstances and of the efforts being made by the member to fulfil its financial obligations to the Fund. The procedures for dealing with members with protracted arrears that have been declared ineligible include further reviews at intervals of not more than six months.

For members with protracted arrears willing to cooperate with the Fund in settling those overdues, the Fund has adopted an intensified collaborative approach, which incorporates exceptional efforts by the international financial community.

For members that are judged not to be cooperating actively with the Fund, remedial measures would be applied. These measures are designed to function as tangible inducements to members with protracted overdues to avail themselves of the intensified collaborative approach, while at the same time they would act as a deterrent for other members. For remedial measures to be an effective deterrent, they would need to be clearly defined in advance; the procedures for their implementation broadly endorsed; and their implementation needs to be credible.

- Members not showing a clear willingness to cooperate with the Fund have been informed that in these circumstances the provision of technical assistance would be inappropriate, but the Fund would reconsider providing technical assistance once the member has resumed active cooperation. The Managing Director may also limit technical

assistance provided to a member, if in his judgment that assistance was not contributing adequately to the resolution of the problems associated with overdues to the Fund.

- A further remedial measure in cases of protracted arrears would be communications with all Governors of the Fund and with heads of selected international financial institutions. As discussed in EBS/89/133, use of such communications would be raised for the Executive Board's consideration at the time of the first post-ineligibility review of the member's arrears. At that time the staff would prepare a draft text of a communication along the lines set out in Attachment II to this statement. It should be noted that the Fund's communication to other international financial institutions, like its communication to the Governors, would not request the addressee to take specific actions and would leave any action to the institution's discretion.

The staff would intend to propose to send this latter type of communication on the occasion of the next post-ineligibility review for members that at present have arrears that have been outstanding for a protracted period, in the event the Executive Board judges that the member concerned is not cooperating actively with the Fund in efforts to resolve the problem of its overdue financial obligations to the Fund.

- Another remedial measure would be a declaration of censure or noncooperation which would come as an intermediate step between a declaration of ineligibility and a resolution on compulsory withdrawal. The decision as to whether to issue such a declaration would be based on assessment of the member's performance in the settlement of its arrears to the Fund and of its efforts, in consultation with the Fund, to follow appropriate policies for the settlement of its arrears. Three related tests would be germane to this decision regarding (i) the member's performance in meeting its financial obligations to the Fund; (ii) an assessment of the member's capacity and willingness to service its obligations to the Fund, reflecting exogenous factors that may have affected that capacity and payments made to other creditors; and (iii) the preparedness of the member to adopt comprehensive adjustment policies that would provide the basis for embarking on the intensified collaborative approach. The declaration would follow any communication to Governors after ineligibility and would be considered at a subsequent post-ineligibility review. The period between such communications and the declaration could be about six months, but this time period would be determined on a case-by-case basis. The declaration would be adopted by the Executive Board. No final conclusion was reached on whether the declaration should be published.

- Regarding the content of the declaration, a redraft of the draft declaration outlined on pages 2 and 3 of EBS/89/128 is attached which takes account of Directors' comments. The Board would consider proposed language in each individual case.

- On suspension of membership, Directors noted the necessity of amending the Fund's Articles of Agreement to provide for suspension of membership. Some Directors showed an interest in introducing a provisio into the Articles of Agreement under which the voting rights of a member that has been declared ineligible to use the Fund's general resources could be suspended. However, most Directors felt that it would not be advisable to propose an amendment of the Fund's Articles of Agreement at this time, but that this matter could be reconsidered in the future.

Finally the option of compulsory withdrawal remains but would only be pursued once the Fund has exhausted all other possible avenues to redress the problem of overdue financial obligations and, despite a declaration of noncooperation, the member has not exhibited a willingness to cooperate with the Fund.