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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 90/59

10:00 a.m., April 16, 1990

M. Camdessus, Chairman
R. D. Erb, Deputy Managing Director

Executive Directors	Alternate Executive Directors
G. K. Arora	
F. Cassell	
C. S. Clark	G. C. Noonan
Dai Q.	Zhang Z.
	Shao Z., Temporary
T. C. Dawson	C. S. Warner
	J. Prader
E. T. El Kogali	L. B. Monyake
E. A. Evans	S.-W. Kwon
E. V. Feldman	R. J. Lombardo
L. Filardo	A. Napky, Temporary
R. Filosa	N. Kyriazidis
M. Finaish	A. M. Othman
M. Fogelholm	I. H. Thorláksson
	O. Kabbaj
G. Grosche	
J. E. Ismael	
	L. M. Piantini
	F. A. Quirós, Temporary
	J.-F. Cirelli
	J.-L. Menda, Temporary
	J.-C. Obame, Temporary
	B. A. Sarr, Temporary
Y. A. Nimatallah	M. Al-Jasser
G. A. Posthumus	G. P. J. Hogeweg
K. Yamazaki	S. Yoshikuni

J. W. Lang, Jr., Acting Secretary
L. Collier, Assistant

Also Present
Staff Association Committee: H. Flinch. Administration Department: G. Rea, Director; H. J. O. Struckmeyer, Deputy Director; D. S. Cutler, A. D. Goltz, F. X. Hogan, J. P. Kennedy, K. M. La Fleur, V. Swenson. European Department: U. Dell'Anno. Exchange and Trade Relations Department: L. A. Whittome, Counsellor and Director; J. T. Boorman, Deputy Director; E. Brau; M. R. Kelly, G. R. Kincaid, J. M. Landell-Mills, A. K. McQuirk, B. C. Stuart. External Relations Department: I. S. McDonald, E. Ray. Legal Department: F. Gianviti, General Counsel; W. E. Holder, Deputy General Counsel; R. Munzberg, Deputy General Counsel; T. M. C. Asser, R. C. Effros, A. O. Liuksila. Secretary's Department: L. Van Houtven, Secretary and Counsellor; A. Tahari. Treasurer's Department: G. Laske, Treasurer; J. E. Blalock, D. R. Hutton, D. Gupta, G. Wittich. Western Hemisphere Department: S. B. Brown. Bureau of Language Services: A. Wright, Director. Bureau of Statistics: R. T. Stillson. Office of the Managing Director: R. Noë, Director, Internal Audit; A. K. Sengupta, Special Advisor to the Managing Director; E. A. Milne. Personal Assistants to the Managing Director: P. Andrews, H. G. O. Simpson. Advisors to Executive Directors: N. Adachi, M. B. Chatah, Z. Iqbal, J. M. Jones, K.-H. Kleine, B. S. Newman, D. Powell, A. Raza, N. Toé. Assistants to Executive Directors: G. Bindley-Taylor, B. A. Christiansen, B. R. Fuleihan, S. Gurumurthi, A. Hashim, M. Hepp, Hon C.-W., K. Ichikawa, C. J. Jarvis, M. E. F. Jones, C. Y. Legg, R. Marino, S. Rouai, D. Saha, H.-J. Scheid, J.-P. Schoder, M. J. Shaffrey, Wang J., J. C. Westerweel, Yang J.

1. STAFF RETIREMENT PLAN - PROPOSED MODIFICATIONS

The Executive Directors considered a staff paper (EBAP/90/95, 4/11/90) outlining the arrangements envisaged for implementing the proposed changes in the Staff Retirement Plan (EBAP/89/296, 12/13/89).

The Chairman of the Staff Association Committee made the following statement:

> We welcome the opportunity to address the Board on management's proposal for amendments to the Staff Retirement Plan. While we have not expressed our views directly to the Board on this proposal before, we have worked closely with the staff representatives on the Pension Committee, and we have followed the informal Board discussions on management's proposal. As you know, the Plan has been under review, more or less intensely, for the past decade. This prolonged review has created considerable uncertainty among staff members concerning their retirement expectations and the adequacy of their pensions. Under the circumstances, we urge the Board to bring this review to a conclusion.
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> In considering management's proposal, you should bear in mind that for most staff members, the Fund retirement represents by far the major element of financial security for themselves and their families. Equally important, staff members contribute a significant portion of their income to the Plan: 7 percent of gross pensionable remuneration and substantially more in terms of net salaries. By comparison, for FY 1991, the contribution rate of the Fund to the current Plan is less than half that of the staff, and it is projected to be nil in the following year.
>
> By way of background, you may be aware that management's proposal represents a compromise with World Bank management on a package developed last August that was supported by the staff and the Staff Association as broadly balanced, in terms of both overall value and equity in the distribution of benefits among different groups of staff. Two important changes were made to the August package that reduced its value to the staff: the weight of the United States in the grossing-up formula was increased to one half from a level the staff already viewed as too large, and a pension supplement for lower-income staff was eliminated. On the positive side, the proposed modifications to the structure of benefits were retained. The staff supports these changes, which provide greater flexibility in the choice of retirement options with little change in cost.
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> In judging management's proposal overall, the bottom line for the staff is the value of the pension package in relation to the total and employer-provided retirement benefits of market

comparators. It has been the position of the Staff Association that the value of the current Plan is not out of line with the market. The results of the Quadrennial Benefits Survey, which became available to the Staff Association only recently, solidly confirm this view. We regret that a thorough comparison of the kind we had been urging from the outset was not carried out much earlier.

The Survey shows that the total value of pension benefits under the current Plan is slightly below the mean of retirement benefit values for the three comparator countries, with the largest shortfalls at the lower income levels. The revisions to the Plan proposed by management would not alter these results, except at the lowest income levels where the value of the revised Plan is somewhat less than the current Plan. While the value of the pension benefits does not differ markedly from the average of comparators, this is only because the staff's own contributions are relatively high. The value of employer-provided retirement benefits ranges from 34 percent to 46 percent below those of comparators. These gaps would be narrowed somewhat under management's proposal, but they would remain large.

Clearly, the proposal before the Board is not a generous one. Indeed, the results of the Survey indicate that there is scope to improve benefits or reduce the relative contributions of the staff. We do not feel that it would be productive at this late stage to change the amendments to the Plan that management has proposed; compromises have had to be made on all sides to reach this point. However, we would like to share with you our views on the principal areas where the package falls short of what is justified on the basis of comparability and equity.

First, the Plan should provide greater assurances on maintaining the inflation-adjusted value of pension benefits to participants. The valuation of the Plan for purposes of market comparisons is based on the assumption of full indexation of Fund pensions; anything less would reduce its value relative to the market even further. More generally, we believe that participants must be assured of the continuing adequacy of their postretirement incomes.

Second, the cost sharing between the staff and the Fund should be brought in line with the market. If the total pension value is kept at a competitive level, it stands to reason that contribution rates would need to maintain market relativities and ensure that the financial strength of the Plan is not eroded.

Third, the results of the Survey justify a pension adjustment for lower-income staff. The adjustments to the tax line at lower income levels do not fully compensate for the well-documented inadequacy of pension benefits for this group of staff. Moreover, the cost to the Fund of providing this supplement would be relatively small.

Fourth, the periodic reviews of the Plan proposed by management should be infrequent and limited to updating the grossing-up formula for developments in tax laws and exchange rates. This would ensure the more stable framework that many Directors and the staff believe is an essential feature of a pension plan. Issues of comparability should be dealt with by establishing market-related contribution rates for the staff and the Fund.

Fifth, as a matter of equity, the provisions for grandfathering should cover all staff. Cutoff rules by their nature treat staff in similar circumstances differently. Full grandfathering would not involve a significant increase in costs to the Fund since the provisions of the two packages are of broadly equal value, and staff members who choose to stay on the old Plan would bear the cost of continuing to contribute at the current higher tax line.

We welcome the Director of Administration's remarks at the meeting of April 2, suggesting that once the baseline pension is established, consideration could be given to optional savings plans or other vehicles that might benefit the staff. However, we would stress that in an international organization such as the Fund, the pension plan must provide an adequate and competitive retirement income in order to attract and retain highly qualified staff.

To summarize our position, the results of the Quadrennial Benefits Survey clearly show that the value of employer-provided benefits in the proposed Plan remains well below that of market comparators. In our view, any weakening of the package would be unjustified and, procedurally, would require the endorsement of the Pension Committee. Finally, while we believe that there is justification for the recommendations we have outlined and that they deserve your consideration, we agree with management that the prolonged uncertainty over pensions must be brought to a conclusion.

The Director of Administration reported that the proposed decision, giving effect to changes in the Plan as recommended by management, had been circulated following consideration by the Committee of the Whole on April 2, 1990. The decision was complex and technical, because it would serve as the legal basis for administering pensions during the period between the time the decision giving effect to the modifications was adopted and the time that formal amendments to the text of the Plan could be drafted, reviewed by the Administration and Pension Committees, and placed before the Board for consideration.

World Bank Executive Directors would meet on April 18 to consider the Bank management's proposals, which in all material respects were similar to those of the Fund, the Director continued. The normal practice in matters of joint interest involving parallelism--such as changes in the Staff Retirement Plan--was that although one institution's Board could decide to adopt the proposals in principle, the decision would not become effective until the other institution had had an opportunity to consider the matter. Therefore, even if the Fund Board were disposed to agree to management's changes, it was not proposed that a formal decision be adopted that day. Instead, as soon as a clear picture was available of developments in the Bank, and assuming no changes had been proposed by the Bank that would suggest the need to reconsider some of the Fund's provisions, a decision, including the effective date, would be circulated for approval on a lapse of time basis. The staff hoped that the effective date could be May 1--the beginning of the Plan's fiscal year--which would be useful for technical reasons.

The Chairman commented that all aspects of the Staff Retirement Plan had been studied by Directors, and their suggestions had been incorporated in the package of proposals. Therefore, he hoped that the decision could be approved in principle that day, according to the procedures described by the Director of Administration.

Mr. El Kogali and Mr. Posthumus said that they supported the draft decision.

Mr. Warner made the following statement:

> We have consistently and strongly advocated the global approach to the review of benefits as the most secure method for the fair and equitable determination of individual benefits. It also facilitates the appropriate balancing of the Fund's total package. The Quadrennial Benefits Survey by Hewitt Associates has now further substantiated that position. The section of the Quadrennial Benefits Survey by Hewitt Associates devoted to retirement benefits is described in EBAP/90/78 (3/29/90) as a "more comprehensive and sophisticated analysis" than the Hay-Huggins study. The strength of management's embrace of this Survey is impressive. Indeed, Hewitt's study has shed much needed light on the evaluation of the Staff Retirement Plan and strongly verifies the validity of our steadfast insistence on a second opinion prior to taking a decision. Hewitt's study also demonstrates clearly the essentiality of several independent findings to support a judicious evaluation process. The beneficial perspective gained through the "total picture approach" is

unmistakable. Notwithstanding the scale of effort by the Joint Compensation Committee (JCC) and the many hours devoted by the Board to the definition of the market and the Fund's relationship to that market, we remain concerned that this basis is not sound and will continue to transmit defective inputs into the oversight process of this Board.

The Hewitt correspondence of March 23, 1990, contained in EBAP/90/78, Supplement 1 (4/10/90), raised a profound point relevant to this and future reviews. Hewitt states: "Unless an integrated study of direct compensation and benefits is performed, it is not possible to determine accurately the percentile at which benefits must be provided in order to achieve a particular percentile relationship for total compensation." We strongly endorse this independent observation and urge management to initiate this study. We see great potential in an integrated study that would bring clarity to an otherwise flawed procedure for overseeing our benefits program. The Administration Department has developed recognized competence in compensation and retirement benefits. A more appropriately framed base of data is needed to compliment those assets. A properly drawn integrated study would make a measurable contribution to that goal.

My reference to reaching a goal indicates our view that a sound basis for oversight has not yet been reached. This chair has consistently expressed concerns over the comparator market survey methodology as it has been applied to the compensation system and now employed in support of recommended changes in the Staff Retirement Plan. Other Directors have joined in these concerns and have expressed other independent concerns as well. The record is replete with these positions. We maintain the view that comparator market data were founded on an unsound basis last year; therefore, all subsequent decisions predicated on these data remain open to question. Our discussion later this week on compensation will afford us an appropriate time to develop this fundamental reservation in greater detail.

For our purposes today, I shall comment on two basic elements that management has recommended for change. First, the weighing of the comparator markets in the grossing-up formula needs moderate rebalancing to reflect properly the actual pattern of retiree activity. A 60-20-20 alignment is advocated now, rather than deferring an obvious present need for reproportioning to the regular review interval program noted in the staff paper. Second, upon further reflection, we see merit in the retention of the present accrual system of the nominal uniform rate of 2 percent per year of service up to a maximum of 70 percent at 35 years. Therefore, management's proposal for revision of the accrual system, as presented in the staff paper as well as in EBAP/89/296 (Section X), is not supported.

I have one final recommendation: the inclusion of a capital accumulation plan in the Fund's pension system. One of the principal findings of Hewitt's study was the significance of the capital accumulation plans in the U.S. and French comparator markets. In the course of the Board's long examination of proposed changes to the Staff Retirement Plan, a number of constructive proposals have been tabled, and innovative suggestions were presented by several Directors. The Board, while observing their relative merits, chose to move ahead to fulfill what it deemed a higher priority--the time frame for reaching a conclusion. I will not speculate on what may have been lost through this course of action; however, the Board has a clear opportunity to be innovative and to establish a capital accumulation plan and fund it by ending the process of separation grants. As an employer contribution, it would strengthen the Staff Retirement Plan, bringing it in line with the comparator market. As an employer contribution, it should be recognized by the staff as a major enhancement. In the vein of budget neutrality, the Fund would be ending a mushrooming contingent liability, latent with management complexities, replacing it with a straightforward element in the qualified retirement system that would, through compounding effects, work productively for the staff. As we have reviewed this concept earlier with the Administration Department, we look forward to the staff's amplification.

At several points in the course of this lengthy review, certain innovative and realistic proposals were under consideration, and this chair considered that endorsable standards were within reach. Those moments have passed, and those standards were not reached. Accordingly, we cannot support this decision.

Mr. Grosche wondered whether Mr. Warner was advocating an annual integrated study of direct compensation and benefits. Such a procedure would deviate from the recommendation of the JCC that the character of both parts of the total compensation package--direct compensation and benefits--was such that it would be extremely difficult to have an integrated study undertaken on a recurrent basis.

Mr. Warner agreed that the review need not be an annual one. His chair had consistently concurred with Mr. Grosche and other Directors that reviews of the Staff Retirement Plan, except for a very few components such as the grossing-up formula and certain tax determinations, should be infrequent. However, Hewitt Associates, at the end of their work on the Quadrennial Benefits Survey, had recommended to management that a study be made of total compensation, and he supported that recommendation.

The staff representative from the Administration Department recalled that, in reply to a question that had arisen in the course of the Executive Board discussion concerning the interaction of salaries and benefits in terms of the market pitch, Hewitt Associates had stated that they were not in a position to provide a definitive answer and that further study of market data would be necessary. He did not consider their response a recommendation that the Fund should move toward a total compensation system for determining salary and benefits in an integrated fashion. For many reasons, the Board had felt that to do so would be inappropriate. Nevertheless, further analysis of market behavior in establishing compensation could provide useful background information.

The Director of Administration observed that the range of surveys available was already quite wide and expensive. The Board had mandated a survey of benefits every four years and a survey of salaries every year. The issues raised by a comprehensive compensation survey could more usefully be discussed in the broader context of the Board's consideration of the Quadrennial Benefits Survey. It could prove informative to have a Hewitt consultant meet with Board members in a seminar discussion of the methodology used by the consultants and of the points made in their report.

Mr. Grosche said that the suggestion put forward by Mr. Warner might entail a salary study by Hewitt Associates, in parallel with the survey already undertaken by Hay, raising concerns about a possible link to one particular consultant firm and about cost effectiveness.

Mr. Warner explained that he shared Mr. Grosche's concerns about the vulnerability of using one consultant exclusively and about the unjustifiable cost of parallel studies. However, he had found that an enormous amount of time was consumed by the Board on discussions on compensation and benefits, although, admittedly, it was difficult for all members of the Board to be equally expert on such matters. A reasonable investment of time and resources in a survey of the compensation-benefit package would be fundamentally important to achieve transparency while promoting efficient use of the Board's time. It would be opportune at the time of the review of the Quadrennial Benefits Survey to determine whether the demand for a second opinion was such that the Fund was willing to invest in a more global study.

Mr. Ismael said that he supported management's proposals for the Staff Retirement Plan.

Mr. Menda made the following statement:

Prolonged discussions in the Pension Committee, as well as in the Committee of the Whole, were held on the review of the Staff Retirement Plan. These were warranted, as the reform package being considered is both comprehensive and complex. The Quadrennial Benefits Survey has provided additional information on the comparability of the proposed Plan that reinforces previous conclusions. We hope that, in view of those previous discussions, it is now possible to reach a consensus on this question, and therefore to end a period of uncertainty for staff members.

This chair has supported management's proposals from the beginning, basically for three main reasons. First, we believe, as the Chairman said in his statement to the Committee of the Whole, that these proposals constitute "a careful and thoughtful balancing of different interests." On the one hand, the proposals provide more accuracy to the definition and calculations of pensions, with the introduction of a new grossing-up formula more in line with the present tax structures of member countries. Lengthy discussions were held on the comparators used to establish the grossing-up formula, and I believe that the present sample, which balances high-level personal taxation countries--namely, the Federal Republic of Germany and France--with a low-level taxation country--the United States--is appropriate. A different sample would not have produced significantly different results, although compensatory modifications should have been adopted to keep the Plan broadly competitive vis-à-vis comparator markets. We also note that this new formula results in a large decrease in the grossing-up figure, and consequently, in savings for the Plan.

On the other hand, the proposed Plan incorporates some features that are not only necessary to ensure its competitiveness, but are also sound from a personnel management's point of view. Indeed, 4 of the 11 proposed modifications aim at reducing the present Plan's heavy bias against early retirement. The adoption of a split accrual rate is certainly the most innovative feature of the package. I can understand those who believe that a pension plan should not be a tool for personnel management; however, in the present case, it seems well adapted to the Fund's present employment structure and is certainly less costly than specific early retirement packages.

Second, it is of the utmost importance to keep the Staff Retirement Plan in line with comparator markets. We have had lengthy discussions on this matter, including very technical ones about the adequate pitch to the market. Additional information provided by the recent report of Hewitt Associates on the Quadrennial Benefits Survey allows us to draw two main conclusions. The first, which is shared with the earlier study, is that the retirement benefits are broadly in line with the mean of the comparator markets and will remain so after the proposed changes. It also shows clearly that, given the correlation between the value of benefits and salary levels, a benefit structure pitched at the market mean would result in a total compensation that would not reach the 75th percentile of the market. The second conclusion drawn from the Hewitt study is that the share of the employer's contribution--the employer-provided value--is significantly below the mean of the comparator markets, and therefore that the appropriate level of retirement benefits is due to the higher level of the staff's contributions. I agree that the burden-sharing formula may have to be reviewed if, in the future, the Fund seems to be moving out of line with market trends.

Our third consideration in supporting the Plan was the financial cost to the Fund. The initial study showed that the new package would bring some savings to the Fund. We recognize, however, the sensitivity of such valuations to actuarial assumptions, but it is reasonable to say that, because of the margin for error of such estimates, the proposed package is broadly cost neutral to the Fund. This is an important conclusion that should make the package acceptable to those members of this Board who are less supportive of the package.

All in all, the rights and benefits of the staff are preserved or improved, an aspect that is essential to make the package acceptable to this institution. Present staff members will be able to preserve their situation, while future staff members will face a different environment. This is a good balance: the package is both acceptable in the short term and far-reaching in its consequences in the longer term.

Mr. Thorláksson said that his chair had, on several occasions, expressed its support for the suggested changes in the Staff Retirement Plan. The recent findings of the Quadrennial Benefits Survey reinforced his opinion that the effects on total compensation of the proposed retirement benefits would not lead to undue deviation from the comparator markets. Therefore, he welcomed the conclusion of the review and supported the proposed decision, including the proposal that May 1, 1990 be the effective date.

Mr. Cassell noted, on one point raised by Mr. Menda, that while the proposals for the Staff Retirement Plan were revenue neutral on the Fund side, they were not so on the World Bank side; that situation did not cause a problem for the Fund Board, but it should be explored in the Bank to understand why costs in the two institutions were different.

Originally, he had not supported Fund management's proposals, and one of his main reservations had been the suggestion that the pension should be set at a 10 percent premium over the comparator market, Mr. Cassell remarked. It had been argued that the premium was justified as a proxy for the 75th percentile used in the calculation of Fund salaries. That argument seemed spurious since pensions were a function of salaries, which were already set at the 75th percentile of those comparator organizations; to set pensions at a further 10 percent premium would result in double counting.

However, his worries had been resolved in a rather unexpected way, Mr. Cassell continued. The Quadrennial Benefits Survey by Hewitt Associates indicated that the Fund's contribution to the Staff Retirement Plan was substantially below that of comparator organizations. If that conclusion was correct, and he considered the methodology underlying it superior to that of the Hay-Huggins study, there was a good case for management's proposals to bring the Fund's contributions up to the mean of the comparator market. Especially welcome was the fact that the Hewitt survey accepted the principle that Fund benefits should be set at the mean of the market--a principle established not only for the present exercise but for others as well.

For those reasons, he could accept the proposals before the Board, Mr. Cassell stated. But the process by which the proposals had been defined left a lot to be desired. For months, the Hay-Huggins study had been discussed without any hint that the data would soon be superseded by better information. Indeed, Directors had been discouraged from waiting for the results of the Quadrennial Benefits Survey. Not only had Directors' time been wasted, but the quality of the work of the Hay organization in general was called into question. The Fund should deal only with the highest quality supplier of information. Two rival studies would, rather than assist the Board in reaching future decisions, render the process more complicated and more protracted.

In addition, no attempt had been made to consider the merit of flexible contributions, although that idea had been submitted earlier, Mr. Cassell said. Nor had any attention been given to the extent to which pensions were transferable to or from the Fund--a curious omission in an organization that set great store in attracting people in midcareer. He hoped that those aspects could be considered in the future. Meanwhile, he could support management's proposals.

Mr. Kyriazidis said that he endorsed the proposed decision.

Mr. Evans commented that he had expressed his disappointment at the outcome of the review of the Staff Retirement Plan on previous occasions. However, bearing in mind the need to bring the matter to a conclusion, he was prepared to join a consensus in support of the proposals.

The staff paper (EBAP/90/95) stated that Article 12 of the Plan gave the Board the authority to act as employer with regard to modifying or amending provisions of the Plan, Mr. Evans noted. He considered that the current procedure would have been helped had the Board played that role at an earlier stage in the review. For the future, it would be essential that the Board act as employer throughout the review as necessary.

Mr. Obame said that his chair could go along with the proposed changes in the Staff Retirement Plan and, therefore, he supported the proposed decision.

Mr. Feldman reiterated his support for the proposed decision; he expressed the hope that, following the discussion in the World Bank, the effective date could be May 1.

Mr. Arora, Mr. Kabbaj, Mr. Othman, Mr. Prader, and Miss Napky said that they supported the proposed decision.

Mr. Al-Jasser commented that, following protracted Board discussions, it was time to conclude the matter. He endorsed the proposed decision, and he hoped that following the World Bank's timely consideration of the issue, a mutually convenient date for implementation could be determined.

Mr. Shao remarked that he could agree to management's proposed changes in the Staff Retirement Plan. Given the considerable length of time spent discussing those changes, both in the Pension Committee and in the Board, it was appropriate to conclude the debate if no major differences remained. To that end, the proposed decision should be approved in principle, with the effective date to be determined, and final adoption on a lapse of time basis should coincide with the World Bank's decision on the same subject. He therefore supported the proposed decision.

Mr. Noonan said that he favored the proposed decision; it would, in fact, be unfair to the staff to defer the decision further. Nevertheless, he regretted that despite the time spent considering the proposals, no solution had been put forward in response to Mr. Evans's criticism of the grossing-up formula, particularly the breakdown in progressivity for remuneration between $50,000 and $80,000. He also regretted that the staff's preference for the grandfathering option, which would have been inexpensive, had not been incorporated in the proposals.

Mr. Quirós recalled that his chair had stated that it did not favor a grandfathering clause applicable to those with 20 years of service with the Fund; rather, it considered that the option should protect the rights only of those who had accrued 25 years of service with age and service totaling 70 years. Nevertheless, he could go along with the consensus.

Mr. Grosche observed that during the thorough discussions of the proposed changes, the staff had gone a long way toward addressing the many questions and concerns raised, including those pertaining to the revised grossing-up formula. Although his reservations remained with regard to the provisions facilitating early retirement, he could join the consensus in support of the proposed decision.

Mr. Yoshikuni commented that he had no difficulties with the results of the Quadrennial Benefits Survey, and he could go along with the proposed changes to the Staff Retirement Plan. His authorities hoped that the Board could reach a clear consensus on the matter.

The Chairman observed that while one chair could not support the proposal and while some reservations had been expressed by a few speakers, the broad sense of the meeting was that there was a strong endorsement of the proposed changes to the Staff Retirement Plan.

The Director of Administration noted that although it was not essential that the World Bank adopt exactly the same decision, care would be taken that the Bank did not endorse any material differences in provisions that were common to the two institutions. If that difficulty should arise, Board members would be given the opportunity to discuss the issue. Otherwise, a decision would be circulated shortly for approval on a lapse of time basis.

Mr. Grosche stated that he endorsed the staff's position. He found it awkward to attempt to define parallelism too strictly; the primary objective was to determine benefit packages that filled the needs of each organization.

Mr. Cassell and Mr. Yoshikuni said that they concurred with Mr. Grosche's views.

Subsequently, the Executive Board took the following decision: 1/

The Executive Board approves the modifications in the Staff Retirement Plan proposed by management as set forth in EBAP/90/95, Supplement 1 (4/19/90).

Decision No. 9416-(90/64), adopted
April 20, 1990

2. SUSPENSION OF VOTING AND RELATED RIGHTS

The Executive Directors considered a staff paper on a possible amendment of the Articles of Agreement to provide for the suspension of voting and related rights (SM/90/55, 3/30/90).

Mrs. Filardo recalled that some months previously the staff had circulated a note on the suspension of voting and related rights of membership (2/1/90), which contained several points that had to be evaluated before any decision on an amendment of the Articles could be taken. As that evaluation had not yet been provided, she considered it inappropriate to indicate a preference for a preliminary version of a possible amendment at that time.

Mr. El Kogali said that he was opposed to amending the Articles of Agreement simply to include additional punitive measures that the Fund could take against a member with overdue financial obligations. Therefore, he saw

1/ The text of the decision was approved on April 20, 1990 on a lapse of time basis (EBM/90/64, 4/23/90).

no useful purpose in discussing the proposed alternative amendments. On the one hand, it was unacceptable that the Fund would amend its Articles to harden its stance vis-à-vis the very few cases of protracted arrears that appeared difficult. There was no stronger action than compulsory withdrawal, and the Articles already included a transparent provision to that effect. On the other hand, using the amendment to deter future cases of arrears seemed a moot point, because the Board had recently spent an enormous amount of time working out procedures to prevent the re-emergence of that problem.

One of the arguments heard in the Board was that a provision for suspension was necessary because it would likely be difficult to have the Board of Governors approve a resolution for compulsory withdrawal, Mr. El Kogali remarked. He did not accept that argument; it prejudged the actions of Governors by attempting to implement Executive Directors' preferred course of action when the Governors might want to act otherwise. Such methods were not expected of the Board. Also, the suspension provision would not necessarily strengthen the resolve of the Board of Governors to vote for expulsion.

The present provision in the Articles of Agreement, which required an 85 percent majority to effect the compulsory withdrawal of a member, provided a sufficient safeguard against precipitous actions injurious to the interest of members and the reputation of the Fund, Mr. El Kogali concluded. When an 85 percent majority supported a decision on compulsory withdrawal, the member concerned would have little doubt that the international community disapproved of its behavior.

The Chairman noted that the purpose of the proposal was to avoid the heavy sanction of compulsory withdrawal by instituting a penultimate step.

Mr. Dawson made the following statement:

> As Directors are aware, my authorities have considered a suspension provision an integral part of a strengthened arrears strategy. This view reflects three fundamental considerations. First, we consider such a provision a matter of equity. A country that does not fulfill the obligations of membership should not enjoy the associated rights and privileges, particularly its right to exercise its voice and vote to influence the affairs of the institution. Second, such a provision would provide the Fund with a more flexible instrument than that now provided in the Articles of Agreement. We consider suspension a measure that would be applied somewhere between a declaration of ineligibility and the ultimate sanction of compulsory withdrawal. Suspension, which can be reversed when the member is again fulfilling its obligations, represents a less draconian sanction than compulsory withdrawal while still leaving open compulsory withdrawal for the most egregious cases. Third, a suspension provision is essential to ensure

that the package of measures to strengthen the arrears strategy is credible and balanced. A consensus is emerging on steps to prevent new arrears cases and to handle the ones that now exist. The third leg of the strategy needs to deal with the situation when a member does not cooperate with the Fund in meeting its obligations.

I would also note that the World Bank has had a suspension provision since its inception which has been used only once. It is our hope that the Fund will never need to suspend a member but we should also prepare for the worst.

With regard to the alternatives in the staff paper, I do not find Alternative C appealing. It could delay decisions undesirably in each case by causing a debate over which voting and representation rights are being affected. In this connection, we see no particular logic in suspending representation at one level, such as the Board of Governors, but not at another, such as the Executive Board. Furthermore, we are concerned that choosing among a menu of options could lead to sharp differences in treatment among members.

As between Alternatives A and B, I have a preference for B. This reflects my view that members of a constituency that elect an Executive Director should be able to decide how they wish to be represented in the event that a member is suspended. The most democratic means of expressing that wish is through a new election to fill the unexpired term of the Executive Director. If the members of the constituency wish to keep the same Executive Director, we would have no objection. We would, however, appreciate clarification from the staff as to whether a suspended member, under either Alternative A or B, would be permitted to attend Interim Committee meetings, vote on resolutions submitted to the Board of Governors on issues other than amendments, and speak or circulate papers at the Annual Meetings, Interim Committee meetings, or Executive Board sessions.

Given our view that suspension should be regarded as a step prior to, and more flexible than, compulsory withdrawal, we believe that the suspension process should differ from that for compulsory withdrawal. Thus, a decision should be taken by the Executive Board based on a 70 percent majority vote. Similarly, repeal of a suspension decision should also be by a 70 percent majority of the Executive Board.

Although we have been considering suspension primarily in the context of the arrears strategy, it would apply to any failure of a member to meet its obligations to the Fund. Therefore, some flexibility in the timing of suspension should be permitted, rather than setting a fixed timetable in the amendment. However, in developing the schedule for remedial measures in arrears cases, we continue to believe that suspension should come at the midway point and be related to a declaration of noncooperation.

Finally, I believe that there has been some confusion regarding U.S. views on the relationship between a suspension amendment and the quota increase. Given that we are in the final stages of our discussions on these matters, I want to make the position of my authorities perfectly clear. The United States is convinced that a strengthened arrears strategy is essential to obtain public and congressional support for an increase in Fund quotas and the use of Fund gold to backstop resources of the enhanced structural adjustment facility to finance purchases under the rights program. In this context, a suspension amendment is vital to ensure that the arrears package is credible and balanced. Therefore, my authorities believe that the quota resolution should provide that any quota increase will become effective only when the amendment of the Articles of Agreement providing for suspension has been ratified and adopted by the necessary 85 percent majority vote.

The General Counsel explained that in Alternative B, as in Article XII, Section 3(f), the reference to the election of "another" Executive Director did not mean that a new Executive Director would have to assume that position--the same Director could be maintained, irrespective of nationality. As to attendance at Interim Committee and Board of Governors' meetings, a provision to the effect that the Governor could not attend--already present in Alternative C--could be added to the language of Alternative A. In Alternative B, there was no need for such a provision as a suspended member could not have a Governor. Of course, when a matter particularly affecting the member was being considered, a representative could be in attendance, as stated in paragraph 5 of Alternative B and paragraph B.4 of Alternative C.

In reply to a question, the General Counsel noted that, according to Article XXVI, a declaration of ineligibility or compulsory withdrawal could be applied in the case of any breach of obligation under the Articles of Agreement. There were few precedents, but one example was Czechoslovakia, which had not provided information required by the Fund. Obligations under the Articles included the undertaking to avoid manipulating exchange rates, imposing restrictions on the making of payments and transfers for current international transactions, or engaging in any discriminatory currency arrangements or multiple currency practices.

The Chairman commented that Mr. Dawson had stated clearly the views of his authorities: the adoption of the proposed amendment of the Articles would create the condition necessary for the effectiveness of the quota increase. He invited other Directors to make their positions known.

Mr. Grosche stated that he preferred Alternative B. The Executive Board, rather than the Board of Governors, should have the responsibility to suspend the voting rights of the member and, if appropriate, terminate the suspension. He could go along with the proposed majority requirement of 70 percent. To have any tangible impact on the arrears country, the new step between the declaration of ineligibility and compulsory withdrawal had to make a difference--an effect not produced by Alternative A. Alternative C presented too broad a menu of options and, because it would undoubtedly lead to lengthy discussions in the Board, was not workable.

He basically agreed with Mr. Dawson's position on the effectiveness of the quota increase, Mr. Grosche continued. Nevertheless, he was concerned that if there was no assurance that the quota increase--linked to an amendment of the Articles--would take effect by the end of 1991, the Fund's liquidity position could be jeopardized, and the Fund's access policy in the interim period would have to be reviewed carefully. As borrowing was not an option he could support, access might have to be reduced in the period until the quota increase became effective.

Mr. Prader observed that three basic issues were being discussed. First, Directors were being asked to consider the question of suspension and whether an amendment of the Articles of Agreement required by such an instrument was acceptable. He believed that essentially the matter lay within the purview of the Interim Committee because of its implications for the Articles; nevertheless, he had some preliminary views.

Before introducing such a measure, it was necessary to be clear about its purpose, Mr. Prader continued. Would it constitute the penultimate step before expulsion, or would it be an instrument to avoid expulsion? He tended to favor the second view, and therefore he could support the adoption of suspension by a 70 percent majority. Thus he could not endorse any version that led, as in the case of the related World Bank rules, to automatic expulsion after one year because that would be tantamount to an understanding that suspension was a preparation for expulsion, which he believed should be undertaken only on the basis of an 85 percent majority. That approach was confirmed by the views of Sir Joseph Gold who, in an interview reported in the Staff News, argued, on the basis of his experience, against expelling members. Sir Joseph considered it essential to keep the dialogue with members open, even if at some point the membership's patience might be close to exhaustion. The question of a further reasonable period before compulsory withdrawal was critical, and he himself believed that it should be addressed in a flexible manner.

On the second issue--the three alternatives for amending the Articles--he could accept Alternative B, for the reasons described by Mr. Grosche, Mr. Prader said. Alternative C, although attractive from the point of view of the Fund's case-by-case approach, did not seem advisable because it would give rise to disputes when deciding on a menu of options, as a result of political lobbying, maneuvering, and judgmental differences.

As to the third issue--the relationship between the quota increase and the suspension amendment cited by Mr. Dawson--during the discussion on the draft report to the Interim Committee, he had stated that reference to the link should not be included in the report, Mr. Prader remarked. A quota review should be conducted on its own merits and not be used as an instrument for other purposes. The link might exist as an implicit political understanding but should not be explicit in a quota decision or in a discussion leading to that decision. With respect to the effect on the Fund's liquidity position resulting from the timing of the effectiveness of the quota increase, he shared Mr. Grosche's views.

Mr. Posthumus recalled that at earlier meetings he had indicated that he could accept in principle a proposal to make it possible to suspend voting and related rights, and to amend the Articles of Agreement for that purpose, if a member failed to fulfill any of its obligations under the Articles. The possibility of suspension could act as a real deterrent, yet suspension could be terminated, while forced withdrawal was a more definitive step. The aim was to bring a member back to cooperative behavior--a legitimate desire on the part of the other members of a multilateral, cooperative institution. Therefore Alternative B seemed the best option from the point of view of a deterrent that made it possible to suspend a member. Alternative C, which modified suspension, seemed to involve too much finetuning.

However, Alternative B raised a number of questions, Mr. Posthumus continued. One concerned the conditions under which suspension could be terminated; they should be clear--perhaps stated in the text of the new Article--and it should be apparent that suspension could be terminated only if the circumstances leading to suspension ceased to exist. To indicate only that suspension could be terminated at any time opened the way to arbitrary behavior. Suspension and its repeal should take place by a 70 percent majority of the total voting power and should be enacted by the Executive Board. He would appreciate comment from the staff as to whether it had looked into the relationship of the Fund's actions with the applicable rules of the World Bank.

At an earlier stage, he had expressed considerable hesitation about a reference, in the report to the Board of Governors, to a link between the quota increase and an amendment to the Articles, Mr. Posthumus remarked. Amendment of the Articles required not only 85 percent of total voting power but also acceptance by three fifths of the members, while the quota increase was conditional only on an 85 percent majority. He wondered whether linking the two proposals might not be legally unacceptable, as the possibility could arise where two fifths of the members' refusal to endorse an amendment of the Articles would be ineffective. He recognized that the same procedure had been used for the Second Amendment of the Articles, but as that package had concerned only the Articles, he did not regard that precedent as binding. He hoped that two distinct votes by each Governor would be possible on the two proposals; if that distinction was possible, he had no problem with the linkage. Otherwise, Directors should return to that aspect when the nature of the link and the consequences for the individual voting behavior of Governors were clearer.

The General Counsel said that the present Articles did not state the particular condition that had to be fulfilled for a termination of ineligibility because it could be extremely difficult in practice to ascertain whether the circumstances leading to ineligibility had changed; thus, the Executive Board had the freedom to determine whether termination was appropriate. As to suspension, it would seem that, in the light of past Fund experience, flexibility in the application of provisions was necessary, but the staff could look into the question of formulating specific conditions for termination.

The World Bank's Articles of Agreement referred to the termination of membership in the Fund, which normally terminated membership in the Bank unless decided otherwise by a 75 percent majority vote, the General Counsel noted. But because suspension had not existed in the Fund's Articles when the World Bank had been established, it was not cited. Thus, suspension of voting rights in the Fund would have no effect in the World Bank unless the Bank amended its Articles of Agreement.

The difference between adoption of a quota increase resolution and a proposed amendment of the Articles had been described correctly by Mr. Posthumus, the General Counsel remarked. At the time of the Second Amendment, two separate legal instruments had been proposed: a quota in crease resolution and an amendment of the Articles; it had been specified that the quota increase would not become effective before the amendment. He believed that the intention of Executive Directors who advocated a linkage between the quota increase and a Third Amendment of the Articles was not to have a single resolution but rather to have two separate legal instruments. It would therefore be possible for a Governor to vote for the quota increase but to oppose the amendment. As long as the required majority supported the amendment and a required majority supported the quota increase, both proposals would become effective, but not necessarily owing to endorsement by the same constituencies.

There was no reason in the present case to find the linkage between a quota increase resolution and an amendment of the Articles contrary to the Articles, the General Counsel stated. The main function of a quota increase was to provide liquidity to the Fund, and obviously members might want to consider whether that liquidity was used effectively. A paragraph in the quota increase resolution submitted to the Board of Governors for approval could specify, for example, that the effectiveness of the increase would be suspended until the amendment of the Articles became effective--a technique used at the time of the Second Amendment.

Mr. Grosche suggested that the staff draft a formulation to the effect that Governors could vote with, say, an 85 percent majority on a declaration stating that they were committed to obtain the necessary authorization from legislatures to vote in favor of the resolution on the amendment of the Articles, without linking it formally to the effectiveness of the quota increase.

Mr. Evans said that both the industrial and developing country members of his constituency believed at present that there was a role for a suspension provision in the Articles. In particular, the developing countries had become increasingly frustrated about the issue of prolonged arrears; indeed, one country had communicated those views frankly in a communication to the Managing Director. He therefore supported the suspension proposal.

Alternative A did not provide an adequate deterrent; Alternative C was too unwieldy; therefore he preferred Alternative B, Mr. Evans stated. The decision should be taken by the Executive Board, and 70 percent was an adequate majority. On the link of the amendment with the quota increase, he was opposed in principle, but he would be willing to keep an open mind on the issue pending further consideration.

Mr. Quirós reiterated the position of his chair, which opposed the amendment of the Articles to provide for the suspension of voting rights. In the history of the Fund, previous amendments had been constructive: the creation of the SDR, and the adoption of a mechanism when the par value system had collapsed. A recognized authority had recently stated that the Fund's influence was mainly over the conduct of its developing country members; and it would seem that the Fund was adopting punitive measures that would affect only those members. Such action was neither equitable nor constructive. The present Articles had adequate mechanisms to penalize those countries that did not comply with the overall obligations of members. He believed that the two resolutions--one on the quota increase and the other on the amendment of the Articles--should be voted on separately.

The Chairman commented that the proposed amendment would protect the institution from the serious danger of arrears. The Fund was not establishing a code of conduct applicable only to developing countries. Suspension would be activated not only in the case of arrears but in respect of breaches of other obligations, for example, the provision of information or compliance with exchange rate obligations--which applied to both developed and developing countries as well as to surplus and deficit countries.

Mr. Clark said that over the past few months, the Board had discussed extensively the ways to develop a strengthened arrears strategy, including preventive and deterrent measures and the rights approach. Those discussions had yielded constructive proposals on how to proceed, and in that respect he could support a proposed amendment to the Articles on the suspension of voting and related rights. That action should not be regarded as punitive but should be considered part of the process of having those countries not fulfilling their obligations practice cooperation and return to a more normal financial relationship with the Fund. He favored Alternative B, with a 70 percent majority enacted by the Executive Board.

As to the link between the quota increase and the proposed amendment, Mr. Clark considered that the question of prolonged arrears to the Fund could not be separated from the proposed increase. If legislatures were to be asked to ratify a quota increase, they should first be shown that the Fund was prepared to deal with countries that were not fulfilling their obligations to the Fund, as evidenced by the proposed legislation on suspension. Therefore, he could support the proposal by Mr. Dawson with respect to the linkage.

Mr. Filosa made the following statement:

> I wish to reiterate our support for introducing into the Articles of Agreement a form of suspension of voting rights for those members who fail to fulfill their obligations under the Articles. This amendment will constitute an additional deterrent measure in our arrears strategy. We see the interdependence between this amendment and the quota increase, and we can sympathize with the desire expressed by some members to link the two issues. The rationale of the interdependence between the quota increase and the strengthened arrears strategy, aimed at providing a more effective solution to the problem of overdue obligations, lies in the fact that a further accumulation of arrears would seriously limit the smooth functioning of this institution while the quota increase is expected to facilitate the functioning of the Fund. Therefore, the increase in quotas and the implementation of the arrears strategy, including its deterrent components, need to be agreed simultaneously.
>
> We are, however, seriously concerned that the benefits expected from the completion of the Ninth Quota Review could be delayed owing to the sometimes long administrative process needed to complete the amendment on suspension. To give more certainty to the Fund and its membership on the timing of the availability of these additional resources, I wonder whether a satisfactory interdependence between these two issues could not be substantially assured by the approval of this amendment by the Board of Governors and by the commitment to ratify the amendment by the end of 1991.
>
> On the staff's proposals for the amendment of the Articles, I would tend to rule out Alternative C, because its flexibility vis-à-vis the member could well be its major shortcoming, perhaps giving rise to a two-step decision and a multitude of unnecessary differentiations.

> Alternative A is a less drastic solution than Alternative B. However, all things considered, Alternative B is closer to the formulation we could accept than the other two proposals. In any event, the decision to suspend a member should be taken by the Executive Board, leaving to the Board of Governors only the further step of compulsory withdrawal. Since this proposal was included in the staff paper, I assume that it should not create a legal problem. I believe that the principle of symmetry should hold and that a 70 percent majority should be required both to suspend a member and to terminate such a suspension. As to the wording of the proposed amendments, I wonder whether the insertion of "further" in paragraph (c) of all three alternatives indicates that suspension is a required step before compulsory withdrawal. If so, I would prefer to avoid introducing a new constraint on the exercise of the Fund's power to decide on compulsory withdrawal.

The General Counsel confirmed that Mr. Filosa's interpretation was accurate: suspension would constitute an intermediate step between ineligibility and compulsory withdrawal, reflecting the Board's desire to have a more compelling measure at that point. Incidentally, the time period between ineligibility and compulsory withdrawal had not been defined but had been left to the discretion of the Executive Board.

Mr. Cirelli said that, on the proposed amendment, as his chair had stated several times during past discussions on the new arrears strategy, he supported measures that strengthened pressure on member countries to stay current with the Fund. While countries currently in arrears could be helped with the rights approach, it was also necessary to ensure that no further arrears cases of such magnitude appeared in the future. Therefore, he supported additional deterrent measures. His chair had indicated that it could endorse an amendment of the Articles aimed at introducing the possibility of suspending voting and related rights of a noncooperating member as a supplementary deterrent weapon in the Fund's arsenal; but it had also indicated that the amendment should be balanced by a strengthened strategy to assist those countries cooperating with the Fund.

With respect to the link between the quota increase and the amendment, he understood that two conditions were necessary for the coming into effect of the quota increase, Mr. Cirelli continued. The first, but not sufficient, condition was adoption of the quota increase resolution by an 85 percent majority of the Board of Governors. The second was the adoption of an amendment of the Articles. It would thus be necessary to rewrite the paragraph on the period of consent in the resolution. Like some Directors, he had a strong reluctance to establish such a tight link between the adoption of a suspension amendment and the quota increase, which could delay the quota increase unduly, given the long parliamentary process required in most member countries. Indeed, after lengthy discussions, he had accepted the extension of the period of consent for the quota increase to end-1991, and his authorities were concerned that a further extension of the period could be entailed by Mr. Dawson's proposal. A clearer description of the link was necessary.

On the modalities of the amendment, he had a slight preference for Alternative C, but he was flexible, Mr. Cirelli concluded. The 70 percent majority was appropriate, with the Executive Board in charge of the procedure.

Mr. Sarr remarked that his chair had stated on previous occasions that the actual sanctions provided under the Articles of Agreement for countries failing to fulfill their obligations to the Fund were sufficient to address the problems of members with protracted arrears to the Fund. The Board had recently thoroughly reviewed and strengthened the strategy on arrears to the Fund. In particular, the sequence and timetable of deterrent measures had been addressed, and he believed that suspension would not greatly add to the arsenal of measures dealing with arrears and could even reduce incentives for countries facing arrears problems to take the necessary steps. In addition, the relationship that had been established between the Ninth Quota Review and the amendment to the Articles of Agreement would entail further delays in the period until the quota review would become effective. In view of the problems raised with respect to the linkage, a decision on suspension should await further clarification of that issue.

He also had a number of problems in determining the consequences of suspension on multiple country constituencies, as well as the conditions under which suspension would be terminated, Mr. Sarr concluded. Under those circumstances, his chair could not support any of the alternatives proposed by the staff on the suspension of voting rights. In any event, should the Board decide to submit that proposal to the Board of Governors, he could not agree to the majority requirement of only 70 percent.

Mr. Yamazaki said that, as he had already indicated on previous occasions, his authorities supported the introduction of suspension of voting rights as an intermediate step between a declaration of ineligibility and compulsory withdrawal. The suspension would constitute a credible deterrent measure without resorting to an irreversible measure, thereby encouraging arrears countries to normalize their relationship with the Fund. It would be important for the Fund to take timely action on a case-by-case basis, in terms of both suspension and termination of suspension. Therefore, the Executive Board would be an appropriate organ to decide those issues.

He supported the proposal that suspension should be imposed by a 70 percent majority, Mr. Yamazaki noted. As to the requirement for termination, he would also prefer a 70 percent majority of total voting power in order to make the provision credible. Nonetheless, if the majority of the Board had a different view, he was willing to be flexible. Similarly, he preferred Alternative B, which contained reasonable implications for suspended members. However, given the importance of the Board reaching a consensus on the issue in order to secure smooth implementation of the strengthened arrears strategy, he was ready to be flexible if the Board was moving toward a compromise.

The issue of the timing of the amendment of the Articles had been raised by Mr. Dawson, Mr. Yamazaki recalled. The strengthened arrears strategy should be well balanced, and suspension would constitute an essential element of the package. Thus, the amendment should be agreed by the Ministers at the Interim Committee as an element of the strengthened arrears strategy, and the Board should propose the amendment to Governors immediately after ministerial endorsement.

Mr. Cassell said that it was necessary to add suspension to the Fund's arsenal, and he supported an amendment to the Articles to incorporate that power. A 70 percent majority of the Executive Board was credible and workable, and as a matter of balance, the same majority should also be required to terminate suspension. The Governors should remain executors of the final sanction, namely, compulsory withdrawal, by an 85 percent majority.

The timing of suspension would fall between ineligibility and compulsory withdrawal, Mr. Cassell continued. While such a serious step should be preceded by a warning of ineligibility, a rigid timetable should not be incorporated in the Articles, and he preferred not to specify that compulsory withdrawal must be preceded by suspension. When the Board had discussed remedial measures, it had expressed a strong preference for flexibility. Suspension could be applicable in the case of a breach of the Articles, when timely action and flexibility would be required.

On the scope of suspension, the options under consideration extended only to voting and related rights, which was acceptable, Mr. Cassell stated. The Articles already contained provisions for partial suspension through ineligibility, and another restrictive measure was not inconsistent. Of the three options, like most speakers he would rule out Alternative C, and he preferred Alternative B to Alternative A because it was fairer and more definite.

There was bound to be a link between the quota increase and the amendment to the Articles, Mr. Cassell remarked. But formulations should be drafted to define the link, as it was difficult to discuss the issue in the abstract.

Mr. Dai said that his position on the proposed amendment remained unchanged, as he was not convinced that it was necessary and appropriate to amend the Articles of Agreement at present simply to insert the new measure of suspension of voting and related rights. Given that deterrent measures had been further modified and intensified following recent meetings, a reasonable time should be allowed for the newly strengthened approach to take effect and to be tested in practice before adopting additional drastic measures requiring changes in the Fund's Articles of Agreement. In any event, even if a decision could be made on a proposed amendment to the Articles, the process would be time consuming, and serious consideration would have to be given to the grave consequences.

An amendment to the Articles was a serious matter and should be undertaken only when absolutely necessary, Mr. Dai stated. He did not see the justification for an amendment at the present time, and his chair, therefore, continued to have strong reservations regarding the proposal.

Mr. Arora recalled that the Chairman had referred to the deadly danger that faced the Fund in the form of arrears. His chair shared that concern; arrears were a serious problem, with implications for the Fund's members. However, the Fund had found the right instrument to deal with the situation: the strengthened cooperative strategy in which the rights approach was a cardinal element. It was strange that while the Fund was not yet assured of adequate financial resources under the rights approach to help a country in arrears that wished to cooperate with the Fund, it was ready to institute an element which, while some justification for it had been given, would not prevent members from falling into arrears and would not correct the situation of countries that were already in arrears.

Arrears had arisen for a variety of causes--as exemplified by the specific cases discussed by the Board--that had not been adequately addressed by the Fund or other institutions, Mr. Arora commented. He agreed with Mr. Dai that it was a serious matter to alter the Articles of Agreement without due regard for the consequences for both members and the effectiveness of the Fund in the difficult period ahead. Therefore, he could not support a link as suggested by Mr. Dawson or as modified by Mr. Grosche. The quota increase had its own rationale, merit, and justification; it should not be impaired by the mechanics of a supplementary resolution that would have to take effect before the increase could be adopted. Like Mr. Prader, he believed that the objective of the link was to use the quota increase for purposes other than those required by the Fund. He was strongly opposed to the link, and he did not support the proposed amendment.

Mr. Feldman said that he fully shared Mr. Arora's position. His chair could not support the proposed amendment of the Articles.

Mrs. Filardo remarked that, taking into consideration the experience of Guyana and Honduras, and recognizing the difficulty of defining noncooperation, she could not go along with the amendment of the Articles or with the link. Without a clear definition of noncooperation, suspension could be applied unjustifiably. Like Mr. Arora, she believed that the quota increase had its own merit, based on the requirements of Fund liquidity and access policy.

The General Counsel explained that the Articles of Agreement set out that ineligibility and compulsory withdrawal were based not on noncooperation but on the failure of a member to fulfill any of its obligations under the Articles of Agreement. The Board had adopted a declaration of noncooperation in other circumstances, but that declaration had no legal effect.

Mr. Ismael said that he wished to associate himself with Mr. Arora's statement.

Mr. Kabbaj commented that the issue of suspension of voting and related rights went beyond the legal aspects presented by the staff. Although some Directors had asked for specific legal language that would clarify their position on the issue, the case had not yet been made for an amendment of the Articles for several reasons. First, it was not wise to amend the Articles on the basis of a very narrow issue. The two precedents were wide-ranging amendments that had taken a long time to implement. Second, such an amendment could set a dangerous precedent that would set the stage for requests for multiple amendments whenever the Executive Board was deadlocked on any given issue. Third, the present Articles already provided the possibility of implementing a wide range of deterrent measures, including compulsory withdrawal. Fourth, such an amendment and its linkage to the Ninth Quota Review would pose complicated problems in member countries--including some in his constituency--where parliamentary approval was required for quota increases. Therefore, he could not go along with the staff's proposals.

Mr. Fogelholm noted that even though his chair acknowledged the fact that the concept of suspension of voting and related rights was not novel because it existed in other organizations, it still had a great deal of hesitation about the issue. Other newly established measures of deterrence, such as the declaration of noncooperation, should have been allowed more time to establish their effectiveness before the Board embarked on the preparation of additional measures. However, to facilitate a final agreement on the Ninth Quota Review, he would not oppose the commencement of work on an amendment to the Articles of Agreement to that end.

His authorities were in favor of Alternative C, but they could go along with Alternative B as well, which seemed to be generally favored by the Board, Mr. Fogelholm continued. He endorsed the proposal of 70 percent for the majority requirement needed to implement suspension. Finally, his Governors would prefer to vote for a resolution on the quota increase that did not contain a direct linkage to suspension. In that connection, Mr. Grosche's points on access were highly relevant and should be discussed.

Mr. Finaish recalled that in the past, he had expressed some reservations about embarking on the highly exceptional step of amending the Articles unless the need for doing so were obvious and pressing. He was still not convinced that there was a need in the case of the suspension amendment. Furthermore, although that amendment was being proposed in the context of the arrears problem, it could have a much broader significance since it could apply to other types of situation that did not involve a breach of financial obligations. Therefore, it was necessary to be sure that, in the broader scheme of things, the proposed amendment was useful and necessary. For those reasons, and because some of his authorities had not yet expressed a view on the specific proposals before the Board, he was not in a position to endorse any of the alternatives.

On the link between the quota resolution and the suspension amendment, he continued to believe that the two issues were separate and should be dealt with accordingly, Mr. Finaish remarked. It would be inappropriate to present Governors with a quota resolution under which an affirmative vote would mean that the member accepted the link between the effectiveness of the quota increase and the suspension amendment.

Mr. Al-Jasser said that during the discussion on the strengthened cooperative strategy (EBM/90/38, 3/16/90), his chair had expressed the belief that compulsory withdrawal was not a feasible deterrent option because it was an extreme measure that would be used only in hopeless cases and as a last resort. However, the lack of credible and convincing deterrent measures might discourage creditor countries from joining support groups. Therefore, it seemed appropriate to devise an intermediate measure between the declaration of ineligibility and compulsory withdrawal. Such a measure should keep the member in the fold, while increasing peer pressure and moral suasion to convince that member to cooperate with the Fund in adjusting its economy and clearing its arrears.

The proposed measure of suspending the voting and related rights of the noncooperating member seemed sensible, especially if the decision and its reversal were taken by a majority of 70 percent of the total voting power of the Executive Board, Mr. Al-Jasser remarked. Keeping the decision in the Executive Board should permit the flexibility and timeliness needed, especially when a reversal was called for after the member had cooperated with the Fund for a reasonable period of time.

As to the three alternatives, although he had an open mind on Alternative B, Alternative A was the most appropriate because it not only was the least punitive, but it also was the least disruptive to the functioning of the Fund at large, Mr. Al-Jasser noted. For example, the constituency to which the suspended member belonged should not suffer as a result of that member's suspension, nor should the functioning of the Executive Board and other organs of the Fund be unduly affected. Suspension was meant to be a temporary measure that was reversible in an expeditious manner.

He hoped that the Fund would not need to resort to that measure, Mr. Al-Jasser continued. However, it was important that such action would convince the international community that once the present arrears problem was resolved, it would not be allowed to reappear. In addition, the institutional evolution of the Fund required that it have at its disposal all the measures necessary to induce its members to observe their obligations to the organization.

On linking the amendment to the Ninth Quota Review, the absence of such a link would make the adoption of the amendment impossible, and hence would undermine the satisfactory conclusion of the present discussions on the quota review and the strengthened arrears strategy, Mr. Al-Jasser observed. Such a failure to conclude those discussions would not send the right signals about the Fund's safeguarding of its resources, and especially their revolving nature.

Mr. El Kogali stated that he was opposed to both the proposed amendment of the Articles and the link.

The General Counsel observed that a few aspects mentioned by Directors could be studied further. For example, one suggestion had been to change the sequence of ineligibility, suspension, and compulsory withdrawal to a two-pronged approach whereby, after ineligibility, either the Executive Board could implement suspension or the Board of Governors could implement compulsory withdrawal.

The Chairman commented that Governors should continue to have the power to implement compulsory withdrawal directly following a major breach of the obligations of membership. He also saw merit in the alternative course of action provided by the intermediate step of suspension of voting rights, an issue that warranted further consideration by the Executive Board. While he had noted the strong reservations of many Directors to suspension, those Directors who endorsed suspension preferred the language of Alternative B and supported its implementation by a 70 percent majority vote of the Executive Board. The staff would provide formulations on the linkage of the amendment of the Articles to the quota increase that would allow Directors to express more precise views on that issue.

Mr. Al-Jasser explained that, while he had an open mind, he had preferred Alternative A because of his concern about the disruptive effect that the other alternatives might have on the functioning of the Fund, especially if an Executive Director's chair were declared vacant immediately. That action could have marked consequences in the case of a multicountry constituency. He would take into consideration the explanation of the staff that the same Executive Director could be re-elected.

Mr. Evans noted that it was important not to lose sight of the more obvious link between the question of suspension and the rest of the revised arrears strategy. His chair considered that if agreement were not reached on suspension, other aspects of the arrears strategy, such as the rights approach, might not be endorsed.

The Executive Directors concluded for the time being their discussion on the suspension of voting and related rights.

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/90/58 (4/13/90) and EBM/90/59 (4/16/90).

3. GULF COOPERATION COUNCIL (GCC) - TECHNICAL ASSISTANCE

In response to a request from the Associate Secretary General for Economic Affairs of the Gulf Cooperation Council for technical assistance in the fiscal field, the Executive Board approves the proposal set forth in EBD/90/112 (4/10/90).

Adopted April 13, 1990

4. APPROVAL OF MINUTES

The minutes of Executive Board Meetings 89/116 through 89/118 are approved.

5. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors as set forth in EBAP/90/50, Supplement 1 (4/12/90) and EBAP/90/96 (4/12/90) and by an Assistant to Executive Director as set forth in EBAP/90/97 (4/12/90) is approved.

APPROVED: February 13, 1991

LEO VAN HOUTVEN
Secretary