0404

CONFIDENTIAL

INTERNATIONAL MONETARY FUND

Committee of the Whole on Review of Quotas
Meeting 90/14

3:00 p.m., March 19, 1990

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

Executive Directors	Alternate Executive Directors
	L. E. N. Fernando
F. Cassell	J. Heywood, Temporary
C. S. Clark	
Dai Q.	
T. C. Dawson	
	J. Prader
	L. B. Monyake
	S.-W. Kwon
E. V. Feldman	
L. Filardo	M. A. Fernández Ordóñez
R. Filosa	
	A. M. Othman
M. Fogelholm	I. H. Thorláksson
M. R. Ghasimi	O. Kabbaj
G. Grosche	
J. E. Ismael	
A. Kafka	L. M. Piantini
J.-P. Landau	J.-F. Cirelli
	C. V. Santos
	M. Al-Jasser
G. A. Posthumus	G. P. J. Hogeweg
K. Yamazaki	S. Yoshikuni

J. W. Lang, Jr., Acting Secretary
S. W. Tenney, Assistant

Also Present

African Department: R. C. Williams. Asian Department: P. Gotur. European Department: J. R. Wein. Exchange and Trade Relations Department: L. A. Whittome, Counsellor and Director; T. Leddy, Deputy Director; M. Shadman-Valavi. External Relations Department: E. Ray. Legal Department: F. P. Gianviti, General Counsel; R. H. Munzberg, Deputy General Counsel. Research Department: S. Takagi. Secretary's Department: C. Brachet, Deputy Secretary; A. Tahari. Treasurer's Department: D. Williams, Deputy Treasurer; A. J. Tweedie, G. Wittich. Office of the Deputy Managing Director: A. K. Sengupta, Special Advisor to the Deputy Managing Director; E. A. Milne. Personal Assistant to the Managing Director: H. G. O. Simpson. Advisors to Executive Directors: N. Adachi, M. B. Chatah, Z. Iqbal, J. M. Jones, K.-H. Kleine, P. O. Montorfano, B. S. Newman, D. Powell, F. A. Quirós. Assistants to Executive Directors: T. S. Allouba, J. R. N. Almeida, G. Bindley-Taylor, C. Björklund, B. A. Christiansen, S. K. Fayyad, B. R. Fuleihan, M. A. Ghavam, S. Gurumurthi, A. Hashim, M. E. F. Jones, R. Marino, G. Montiel, J. A. K. Munthali, S. Rouai, D. Saha, H.-J. Scheid, J.-P. Schoder, Shao Z., J. C. Westerweel, Yang J.

1. NINTH GENERAL REVIEW OF QUOTAS - STATEMENT BY MANAGING DIRECTOR

The Executive Board, meeting as a Committee of the Whole, continued from Committee of the Whole on Review of Quotas Meeting 90/13 (3/19/90) their consideration of a statement made at that meeting by the Managing Director on the Ninth General Review of Quotas.

The Managing Director recalled that during Committee of the Whole on Review of Quotas Meeting 90/13 and with one exception, Directors had--in a spirit of compromise--indicated that they could agree to a 50 percent increase in the size of the Fund if the next review of quotas was held in 1993. In that connection, an agreement to postpone the next quota review until 1995 would give rise to two important issues: the appropriate legal means for accomplishing such a postponement and the extent to which the size of the quota increase would have to be enlarged to cover the additional period. In that connection, while a few Directors had indicated that no additional increase would be needed to extend the interval between reviews to 1995, some others had considered that an increase of at least 67 percent would be needed to cover the period to 1995, and still others had indicated that their positions were flexible on that issue. In addition, many Directors had indicated some support for Mr. Ismael's proposal, which was to conclude the Ninth and Tenth Review simultaneously, with a 50 percent increase in quotas becoming effective in 1991 and an additional 12 percent increase becoming effective in 1993; the same methodology and data period would be used to calculated quotas for both increases, with the second increase distributed entirely on an equiproportional basis; in that way the Eleventh Review could be held in 1995. It would be helpful if Directors could comment on those issues for the current discussion.

The Deputy General Counsel stated that Mr. Ismael's proposal was legally feasible, because it did not deviate from the proposal to complete the Ninth and Tenth Reviews at the same time; consequently, the five-year period for the Eleventh General Review of Quotas would begin upon completion of the Tenth Review.

The Deputy Treasurer noted that Mr. Ismael's proposal would obviously stagger the coming into effect of an increase under the Ninth and Tenth Reviews, which could present a problem in light of the staff's expectation that the future demand for Fund resources would be front-loaded.

Mr. Al-Jasser commented that, as the Managing Director's statement had pointed out, the appropriate size of the Fund in the early 1990s was a matter of judgment rather than calculation. Over the past three years, Directors had considered a number of calculations provided by the staff and during that time, his chair had expressed a number of reservations about the forecast demand for Fund resources, the role of the Fund, and the need to maintain its size relative to that of the world economy. His authorities considered that a quota increase of 50 percent would be sufficient to enable

the Fund to fulfill its responsibilities in the international monetary system. In the light of those considerations, the most appropriate course of action would be to agree to an increase of 50 percent at the present stage, and review the financial position of the Fund and the adequacy of Fund quotas in the light of the circumstances prevailing in the world economy in 1992--when the Committee of the Whole for the Tenth Review would be established. He would not consider any additional increase in quotas under the Ninth Review beyond that already agreed.

Mr. Cassell stated that an increase of 50 percent of present quotas would be adequate. Moreover, he was opposed to the proposal to build an automatic additional increase into the future. Indeed, his authorities had originally favored an increase of 25 percent, but they had increased that amount to up to 50 percent of present quotas, partly owing to the longer duration of the increase under consideration.

Mr. Landau said that the tentative position of his chair was in favor of further considering the proposal put forward by Mr. Ismael, which was a useful addition to the option of combining the Ninth and Tenth Reviews, in particular because it would not leave the Tenth Review completely meaningless. However, at the present stage, Mr. Ismael's proposal was overly rigid, owing to the suggestion to use the same methodology and data period in calculating quotas under the Tenth Review as in the Ninth. Moreover, an entirely equiproportional distribution of the second increase would be contrary to the methodology agreed for the first increase.

Mr. Grosche commented that he agreed with Mr. Al-Jasser that the most appropriate course of action would be to agree to a 50 percent quota increase at the present stage and review the adequacy of quotas again in 1992 when the Committee of the Whole for the Tenth Review was established. However, if it was not possible to reach a consensus on the suggestion put forward by Mr. Al-Jasser, he would prefer to conclude the Ninth and Tenth Reviews simultaneously and further consider Mr. Ismael's proposal.

Mrs. Filardo noted that if the interval between reviews was extended until 1995, it would be necessary to increase quotas by at least 67 percent. In order to accommodate the position taken by the U.S. chair that the next quota review should be in 1995, her authorities would be willing to consider Mr. Ismael's proposal for an additional automatic increase of 12 percent. However, if that proposal did not receive widespread support, she agreed with Mr. Al-Jasser that the Fund should preserve its option to review the adequacy of quotas again in 1992.

Mr. Dawson remarked that the most appropriate course was to approve a 50 percent increase in present quotas to last until 1995. While, from a legal perspective, it might be desirable to combine the Ninth and Tenth Reviews, he saw no justification for attributing part of a quota increase to one review and part to the other. The most appropriate method for the Fund

to follow--both legally and politically--was to recommend increases in Fund quotas to its members as infrequently as possible.

In that connection, Directors would recall that at the time of the Eighth Review, a number of Directors had indicated that the quota increase agreed might prove to be inadequate to support the Fund's operations over the envisaged review period, Mr. Dawson noted. However, in the event, the interval between the conclusion of the Eighth Review and the current Review had been seven years, instead of five, and the increase approved under the Eighth Review had proved clearly adequate in terms of maintaining a prudent and sustainable liquidity level over that longer than envisaged period.

Mr. Fernando stated that he supported the proposal put forward by Mr. Ismael, and he agreed that the second increase to become automatically effective in 1993 should be distributed entirely on an equiproportional basis.

Mr. Posthumus commented that it would be useful to further consider Mr. Ismael's proposal. He was surprised by Mr. Cassell's intervention, because on previous occasions the U.K. chair had indicated that it was willing to agree to a quota increase of more than 25 percent in order to narrow the differences among Directors. If the United Kingdom had made that compromise with a view to extending the interval between reviews, it was clearly less concessional than Mr. Cassell had originally indicated.

Mr. Monyake suggested that, if Directors could not reach a consensus on Mr. Ismael's proposal, it would clearly be appropriate to follow the provisions of the Articles with respect to the timing of the next quota review.

The Committee members then took up the question of the data period to be used in calculating quotas under the Ninth Review.

The Chairman recalled that during Committee of the Whole on Review of Quotas Meeting 89/11 (11/3/89), a number of Directors had indicated that their positions were somewhat flexible with respect to the period of the data that should be used in calculating quotas. However, since that time, several Directors had indicated that if the interval between quota reviews was extended until 1995, the data period ended in 1986 should be used. In that connection, the most recent breakdown of Directors' positions indicated that there was a slight majority in favor of the data period ended in 1986, as opposed to that ended in 1985, but two Directors had not yet indicated final positions. Therefore, it would be helpful if Directors could clarify their positions during the current discussion.

Mr. Grosche said that the position of his chair had not changed; he could agree to the use of either data period.

Mr. Landau stated that he preferred the data period ended in 1986 for two reasons. First, as a matter of principle, the most recent available data should be used in calculating members' quota shares. Second, in the light of the delay in completing the Ninth Review, it would clearly be more appropriate to use the data period ended in 1986 in order to more accurately reflect members' current positions in the world economy.

In addition, any extension of the interval between reviews would further support the need to use the most recent available data, Mr. Landau considered. As Mr. Ghasimi had indicated, any postponement of the next review of quotas would delay the progress toward realigning members' actual quota shares to reflect their positions in the world economy. In the light of those considerations, it would be extremely difficult to accept the use of data that would be outdated by ten years at the time of the next quota review.

Mr. Filosa said that he strongly supported the position expressed by Mr. Landau.

Mr. Al-Jasser commented that the position of his authorities was flexible with respect to the data period used in calculating quotas under the Ninth Review. However, if 1986 data were used in connection with the Ninth Review, they should not be used again in connection with the next quota review.

Mr. Dawson noted that a change in the data period that ended in 1985 would result in changes in members' calculated quotas, which in turn could necessitate further consideration of the emerging consensus on the distribution of the quota increase and requests for ad hoc quota increases. Since a change in the data period would not help to resolve the outstanding issues concerning the ranking of certain members within the Fund, he saw no advantage to deviating from the consensus that was emerging in favor of the data period ended in 1985, in particular since such a decision could decrease the prospect for reaching a timely agreement on the Ninth Review. In that connection, it should be noted that Directors would have the opportunity to include seven years in the data period used in calculating quotas under the next review, in order to avoid any omission or overlapping of data for specific years.

Mr. Othman stated that he favored the data period ended in 1985.

The Committee members then took up the method to be used in distributing quotas under the Ninth Review.

Mr. Yamazaki said that he could support the proposal to distribute 60 percent of the quota increase equiproportionally. His position was flexible with respect to the distribution of selective increases.

Mr. Fernando commented that the position of his authorities was based on the assumption that the next review of quotas would take place in 1993. On that basis, they were willing to support a distribution that would be 60 percent equiproportional, with selective increases distributed according to Method A. He was opposed to any use of Method B in the absence of an agreement to distribute 75 percent of the quota increase on an equiproportional basis.

He supported the request from Japan for an ad hoc quota increase within the context of the Ninth Review, Mr. Fernando said. In that connection, he supported the proposed modalities of distribution that would preserve the quota share of the developing countries to that reflected in the 60/40 apportionment of the overall increase. He also supported the Korean and Iranian requests for ad hoc quota increases.

Mr. Grosche stated that he could agree to a distribution method that would be 60 percent equiproportional and 40 percent selective, with selective increases allocated mostly according to Method A. In addition, he could agree to some use of Method B in distributing a small amount of the selective element of the quota increase.

He could maintain a flexible position with respect to the requests from Korea and the Islamic Republic of Iran for ad hoc quota increases, provided those increases would be financed by the membership as a whole, except the G-7 countries, which were to finance the ad hoc increase for Japan, Mr. Grosche concluded. He could also agree to special increases for the four members with very small quotas, whose shares in actual quotas were smaller than their shares in calculated quotas.

Mr. Filosa said that he favored a combination of Method A and Method B in the distribution of selective increases, as that was the most appropriate way to avoid the continuation of discrepancies in the future. He agreed with the proposal to round up all quotas. In addition, he could support the requests from Korea and the Islamic Republic of Iran for ad hoc quota increases, provided those increases were financed by the membership as a whole, axcept for the G-7 countries, who were to share the financing burden for Japan's ad hoc increase.

Mr. Cirelli stated that he fully agreed with the position expressed by Mr. Filosa.

Mr. Kwon commented that a number of interrelated issues needed to be addressed in connection with the distribution of the overall increase in quotas. On previous occasions, his chair had indicated its support for a 60/40 apportionment of the overall increase, with selective increases allocated according to Method A. In that connection, his authorities appreciated the United Kingdom's offer to fully absorb the non-G-7 countries'

share of the financial burden arising from the ad hoc increase for Japan that would place it in second position in the Fund.

On previous occasions, his chair had expressed its support for an ad hoc quota increase for the Islamic Republic of Iran, Mr. Kwon continued. Since his chair had put forward the Korean request for an ad hoc quota increase on several previous occasions, he would not repeat the arguments in support of that request. However, Directors should bear in mind three main points. First, the disparity between Korea's actual quota share and its share in calculated quotas was among the largest in relative terms, and no combination of uniform distribution methods was likely to have a significant effect on that disparity. Second, the disparity in Korea's quota shares was a long-standing problem, dating back to the Sixth Review; thus, it should be resolved at the current stage, while an ad hoc increase could still be accommodated relatively easily by the membership as a whole. Third, Korea had demonstrated its willingness to assume its full responsibility as one of the leading newly industrialized economies in the international community, as evidenced by its contributions to the enhanced structural adjustment facility, the International Development Association, the World Bank, and numerous regional banks.

Aside from those points, it should be noted that Korea's position in the Fund had not benefited from the history of arbitrary and inconsistent policies that had been adopted with respect to new members, Mr. Kwon went on. For example, in 1982, Hungary's actual quota share had been set at 70 percent of its share in calculated quotas, well above the average for new members at that time.

In the light of those considerations, the Fund should give sympathetic consideration to Korea's request for an ad hoc quota increase, Mr. Kwon concluded.

Mr. Ghasimi said that the envisaged distribution method, which would entail an equiproportional element of 60 percent of the overall increase and a selective element of 40 percent, would result in a decline in the quota share of his constituency. Nevertheless, he was prepared to go along with the emerging consensus on that method in the hope that the Board would give sympathetic consideration to the Islamic Republic of Iran's request for an ad hoc quota increase. He also supported the Korean request for such an increase.

As he had presented the case for an hoc increase in the quota of the Islamic Republic of Iran on numerous previous occasions, he would not repeat that case in detail for the current discussion, Mr. Ghasimi continued. Nevertheless, several facts pointed to the need for an ad hoc increase in the Islamic Republic of Iran's quota. First, the ratio between the actual quota share and the calculated quota of the Islamic Republic of Iran was twice that of the membership as a whole. Second, the special circumstances

of the Islamic Republic of Iran prevailing at the time of the Seventh and Eighth Reviews and the difficulties encountered by the authorities had prevented the Islamic Republic of Iran from participating in those reviews. Third, the Islamic Republic of Iran had traditionally contributed to the financial resources of the Fund whenever its balance of payments position had allowed it to do so. Finally, the Islamic Republic of Iran had collaborated closely with the Fund. Indeed, a staff mission had recently returned from the Islamic Republic of Iran, after successfully completing the first Article IV consultation discussions with the authorities in 11 years.

Those considerations made a strong case justifying sympathetic consideration of the Islamic Republic of Iran's request for an ad hoc quota increase, Mr. Ghasimi considered.

Some Directors had indicated that they could agree to the Korean and Iranian requests for ad hoc quota increases only if the financial burden of those increases were shared among the membership as a whole, excluding the G-7 countries, Mr. Ghasimi noted. As he had indicated on previous occasions, the quota shares of all members, including those in the Group of Seven, had been augmented in connection with the Seventh and Eighth Reviews as a result of the Islamic Republic of Iran's inability to participate in those quota reviews. Therefore, it would not be appropriate to exclude the G-7 countries from the burden sharing for the Islamic Republic of Iran's ad hoc quota increase in connection with the Ninth Review.

Mr. Al-Jasser recalled that on previous occasions, his chair had indicated its preference for a larger equiproportional element, of 70 percent, in the overall distribution of the quota increase, with the remainder distributed according to Method A. Nevertheless, in order to facilitate a consensus, he could go along with the proposal contained in the Managing Director's statement for a 60/40 apportionment of the overall increase between equiproportional and selective increases. As he had indicated on several previous occasions, his chair welcomed the rise of Japan to the second ranking position.

Mr. Dawson remarked that the United States would be prepared to support a uniform method of distribution, based on a 60/40 apportionment of the overall increase, with selective increases distributed according to Method A. However, his chair's willingness to accept an ad hoc reduction of its quota share to protect the positions of other members was contingent on a satisfactory resolution of other outstanding issues related to the Ninth Review that were of particular concern to his authorities. In any event, he would not agree to any adjustment that would reduce the U.S. voting share below the existing level of 19.10 percent.

He continued to consider that the case for an ad hoc quota increase for Japan that would take it to second position in the Fund was unique and

compelling, Mr. Dawson stated. He could go along with the proposal put forward by the staff to round up the very small quotas.

Mr. Feldman said that he favored a 60/40 apportionment of the overall quota increase, with selective increases distributed according to Method A. He supported the requests from Korea and the Islamic Republic of Iran for ad hoc quota increases.

Mr. Othman stated that his authorities continued to consider that it was crucial to effect a significant adjustment of quotas in the context of the Ninth Review that would reflect members' relative positions in the world economy. Therefore, they strongly supported some use of Method B in the distribution of selective quota increases, in particular given that a relatively large portion--60 percent--of the overall increase was to be distributed equiproportionally. Nevertheless, if a consensus emerged in favor of a 60/40 apportionment, he could go along with it.

In addition, he could go along with any consensus on the requests from Korea and the Islamic Republic of Iran for ad hoc quota increases, Mr. Othman said. However, in that connection, it should be noted that several members of his constituency supported the Islamic Republic of Iran's request for an ad hoc quota increase.

Mr. Kafka stated that he supported the Japanese request for an ad hoc quota increase, and he could go along with a consensus among Directors on requests from Korea and the Islamic Republic of Iran for ad hoc quota increases. He strongly supported the proposal to distribute the quota increase 60 percent equiproportionally and 40 percent selectively, based on Method A. He was opposed to any use of Method B in the distribution of the quota increase.

Mr. Heywood said that his chair supported a 60/40 apportionment of the overall quota increase between equiproportional and selective increases. If that method of distribution was agreed, the United Kingdom was willing to take up the share of financing an ad hoc quota increase for Japan that would otherwise be borne by the non-G-7 countries--assuming the other G-7 countries would participate in the financial burden sharing for the Japanese increase in proportion to their quotas. The proposal put forward by Mr. Cassell on the burden sharing for Japan's ad hoc increase had been designed to deviate as little as possible from the principle of uniform treatment, which had been strongly supported by the Interim Committee and endorsed by the Board on several previous occasions.

Mr. Dai commented that he could go along with Mr. Cassell's proposal on the financial burden sharing for Japan's ad hoc quota increase. He could also support the requests from Korea and the Islamic Republic of Iran for ad hoc quota increases.

Mr. Ismael stated that he could go along with the consensus for a 60/40 apportionment of the overall increase, although he considered that an apportionment of 60/35/5 between the equiproportional and selective increase, using Method A and Method B, would have been more helpful to the members with quota shares that were out of line. He could also agree to Mr. Cassell's proposal on the burden sharing for Japan's ad hoc quota increase and with the proposal put forward in the Managing Director's opening statement on adjustments for members with very small quotas. He could agree to the consensus among Directors on the requests for ad hoc increases from Korea and the Islamic Republic of Iran.

Mr. Clark said that he agreed with the Managing Director's assessment that there appeared to be a broad consensus that 60 percent of the increase should be distributed on an equiproportional basis and that there had been widespread support for the use of Method A in distributing the remaining 40 percent. In addition, there had been broad support for an ad hoc increase for Japan, with the financing burden limited to the G-7 countries. He could agree to the consensus on those issues.

The Managing Director's statement had also noted that there did not appear to be sufficient support for the requests for ad hoc quota increases for Korea and the Islamic Republic of Iran, and he agreed with that assessment, Mr. Clark concluded. He could support the proposal to raise the quota shares of the members with very small quotas that had calculated shares in excess of their actual quota shares and to make further adjustments for the members with very small quotas in the context of the rounding techniques proposed by the staff.

Mr. Kwon commented that there were clear advantages to addressing the special needs of the members with very small quotas with respect to their access to Fund resources in a way that would also redress the existing anomalies within the quota structure and restore a sensible ranking within that group of members. However, the proposal put forward by his authorities had not received the necessary broad support. Therefore, he could support the proposal to use rounding techniques, as described in the Managing Director's opening statement. However, it should be noted that the use of rounding techniques was a second-best solution that would inevitably cause further distortions, which would need to be resolved in the context of future quota reviews. He could support the proposal to round all quotas up to the next higher multiple of SDR 1 million.

Mr. Othman stated that he continued to strongly support the proposal put forward by Mr. Evans to raise the shares of the members with very small quotas to the average ratio of actual to calculated quotas for that group of members. If that proposal did not receive sufficient support, he could go along with the approach outlined in the Managing Director's opening statement.

Mr. Fernando said that he could agree to adjust the quota shares of the four members with very small quotas that had calculated quota shares above actual quota shares up to the calculated quota. In addition, he agreed that adjustment for the 16 other members with very small quotas should be made within the framework of the proprosed rounding of quotas to the next higher multiple of SDR 1 million.

Mr. Fogelholm commented that from Committee of the Whole on Review of Quotas Meeting 90/9 (1/24/90), he had received the impression that a consensus had been reached to apply the compromise proposal put forward by the staff in column 6 of Table 1A of EB/CQuota/90/1 (1/7/90) to the very small quotas. In that connection, it should be noted that any rounding of quota shares would cause the actual quotas of some members to overshoot their shares in calculated quotas. To the extent that the actual quotas of those members were rounded up, they would move further from--rather than toward--their calculated quotas, an adjustment Directors had agreed should be avoided.

The Deputy Treasurer recalled that during Committee of the Whole on Review of Quotas Meeting 90/9 (1/24/90), progress was made toward a consensus that for the four members with very small quotas that had calculated quota shares in excess of their actual quota shares, the actual quota share should be raised to the calculated quota share. In addition, Directors had agreed that the rounding technique used in connection with the Eighth Review should be considered as a special adjustment for members with very small quotas.

For the current discussion, another issue had been raised with respect to rounding up quotas for all members, the Deputy Treasurer said. In the past, all quota shares had been rounded up to the next higher multiple of SDR 0.1 million. However, given the current size of the Fund and the quota increase under consideration, it would be sensible to give consideration to raising quotas to the next higher multiple of SDR 1 million.

As Mr. Fogelholm had correctly noted, any rounding of quotas would result in some members--i.e., those with present quota shares in excess of, or very near, their calculated quota shares--overshooting their calculated quota shares, the Deputy Treasurer concluded. Thus, a decision to round up quota shares to the next higher multiple of SDR 1 million would allow the actual quota shares of 120 members to move slightly further away from their calculated quota shares. Alternatively, if Directors could not agree to a rounding system, the quota shares of some members would need to be truncated, but that had never been done in the past.

Mr. Grosche said that he agreed with Mr. Fogelholm's comments. He supported the use of the same rounding techniques that had been applied in connection with the Eighth Review.

Mr. Dawson stated that he could associate himself with the observations made by Mr. Fogelholm. He wondered whether the staff could prepare illustrative calculations of the quota share that would result for each member as a result of the staff's proposal in order to clarify the nature and the magnitude of likely perverse adjustments.

Mr. Al-Jasser commented that he agreed with the comments made by Mr. Fogelholm, Mr. Grosche, and Mr. Dawson. While he would prefer to use the same rounding technique applied in connection with the Eighth Review, he could agree to the new method proposed by the staff if there was broad support for it.

Mr. Kafka said that he agreed with the positions expressed by Mr. Fogelholm and Mr. Dawson.

Mr. Santos stated that he could support the new rounding method proposed by the staff.

The Chairman noted that the broad preference of Directors was to repeat the same rounding technique that had been used in connection with the Eighth Review.

The Committee members then took up the issues related to the period for consent for the Ninth General Review of Quotas.

The Deputy Treasurer recalled that during previous discussions on the Ninth Review, two proposals had been put forward with respect to the period for consent and participation requirement. Under the first proposal, the period for consent would be for 12 months following the conclusion of the review, with a participation requirement of 70 percent of members. Under the second proposal, there was a split participation requirement in that the quota increase would come into effect up to end-1991 if 85 percent of the members had agreed to participate and thereafter when 70 percent of members had agreed to participate.

Mr. Fernando said that he could support the proposal that members should be required to consent to the full amount of the proposed quota subscription under the Ninth Review. His position on the period of consent and corresponding participation requirement was flexible; he could go along with either of the proposals under consideration.

Mr. Grosche commented that he would have no objection to allowing members to decide whether or not to consent to the full amount of the increase allocated to them. Members generally were interested in consenting to the full amount of quota allocated to them, and the effect of a few members not consenting to the full amount probably would not be significant in terms of the Fund's future liquidity position.

As he had indicated on previous occasions, he could go along with the proposal put forward by Mr. Dawson to extend the period of consent to end-1991, Mr. Grosche concluded. Finally he agreed with the participation requirement suggested in the Managing Director's statement.

Mr. Ismael said that he continued to consider that members could be provided with more flexibility if the new quotas proposed under the Ninth Review were treated as maximum limits, thereby allowing members to decide the amount of the increase they wanted to take up. If a member was not prepared to take up the full amount of its quota increase, it would be more in keeping with the cooperative spirit of the Fund to allow that member to consent to some increase, thereby partially increasing its role in, and contribution to, the Fund, rather than not allowing it any increase in quota. Such flexibility would also enable the Fund to accommodate cases in which members were unable, owing to budgetary restrictions, to take up the entire amount of the proposed new quota. In that connection, he wondered what practice other international financial institutions, such as the World Bank, followed.

Mr. Kwon stated that he supported the staff proposal for a period of consent of 12 months and a 70 percent participation requirement. Like Mr. Ismael, he considered that there was merit to allowing members to consent to less than the full amount of their new quotas. In that connection, he was not convinced by the legal argument that had been presented on previous occasions that it would be extremely difficult to reallocate unused quotas among members. He wondered whether the staff had received indications from any members that they intended to forgo part or all of the quota increases allocated to them under the Ninth Review.

Mr. Al-Jasser said that he wondered whether the staff could comment on any ill effects that could result from members' participating in less than the full amount of the quota increases allocated to them.

The Deputy Treasurer commented that, for the current discussion, the staff could not give precise details on the practice of other international financial institutions with respect to general resource increases. However, it was the staff's understanding that some of those institutions issued shares as maximum subscriptions and members were allowed to decide the amount they would take up.

With respect to the question raised by Mr. Kwon, the agreed distribution of the increase in members' quotas would be attached to the Resolution that would be sent to the Board of Governors for voting, the Deputy Treasurer noted. Once the Resolution concluding the Ninth Review was approved by the Board of Governors, the Board would not be able to change the quota shares of individual members. During previous discussions on the Ninth Review, the Managing Director had asked members to inform the Fund if they did not intend to take up the full amount of the quota increase that

would probably be allocated to them, so that any forgone quota shares could be redistributed among members before the Resolution on the Ninth Review was finalized. It should be noted that in connection with some previous reviews, in particular the Sixth Review, when members had informed the Fund well in advance of the review's conclusion that they were not interested in taking up the full amount of the quota increase that had been allocated to them, the forgone quota shares were redistributed among the membership before the Resolution concluding the review of quotas was finalized. However, in the case of other reviews, when up to eight or nine members had not subscribed to the full amount of the quotas allocated to them after the Resolution had been finalized, the excess quotas had in effect been wasted.

Although the staff had not been informed of any members that did not intend to take up the full amount of their new quotas in connection with the Ninth Review, the precise amounts of new quotas for individual members had not yet been agreed, the Deputy Treasurer concluded.

The Deputy General Counsel commented that if the Fund was informed of a member's intention not to take up the full amount of its increase in quota before the Resolution concluding the review was sent to the Board of Governors for voting, it would be possible to take the excess quota shares into account in distributing quota shares to individual members.

Mr. Fogelholm asked whether it would be possible to include a provision in the Resolution concluding the Ninth Review that would allow the Fund to distribute forgone quota shares to other members, such as those with actual quota shares below their shares in calculated quotas.

The Deputy General Counsel replied that there were two ways in which forgone quota shares could be reallocated after the Resolution concluding the Ninth Review was approved by the Board of Governors. First, the proposed Resolution could include a provision for redistributing forgone quota shares automatically, according to precise distribution criteria that would be established within the text of the Resolution. Second, the Board of Governors could agree to reassess the results of the quota increase after it came into effect and reallocate forgone quota shares at that time. However, such a reassessment would require a second Resolution to redistribute additional quota shares and probably, in some cases, parliamentary approval from members taking up additional quotas shares.

Mr. Posthumus said that he agreed with the comments made by Mr. Grosche and Mr. Ismael. It should be noted that the U.S. proposal on the period of consent and participation requirement would prolong the coming into effect of the quota increase by an additional year.

Mr. Kafka stated that he supported the U.S. proposal to set the period of consent at end-1991 with a participation requirement of 85 percent, and at 70 percent thereafter. However, that period of consent should be subject

to extension by the Executive Board. While the requirement that members should participate to the full amount of the quota increase was not appealing, it would be overly complicated to deviate from it.

Mr. Al-Jasser commented that, although he would prefer members to consent to the full amount of the quota increase, his position was flexible on that issue, and he could go along with the consensus among Directors. In that connection, he agreed with management and staff that any member that did not intend to consent to the full amount of its quota increase should notify the Fund as soon as possible.

He could go along with the proposal to extend the period of consent to December 30, 1991, with a participation requirement of 85 percent, Mr. Al-Jasser said. After that date, 70 percent of members participating would be sufficient to bring the quota increase into effect.

Mr. Clark said that he supported the proposal to extend the period of consent to December 30, 1991, with a participation requirement of 85 percent and 70 percent thereafter. While his position was flexible with respect to the consent requirement of individual members, he would prefer members to consent to the full amount of the quota increase, as in the Eighth Review.

Mr. Dai stated that he was in favor of following the practice used in connection with the Eighth Review, when members were required to consent to the full amount of the proposed quota increase. He could agree to set the deadline for the period of consent 12 months from the conclusion of the review, to be extended if necessary. He would prefer to preserve the participation requirement of 70 percent established in connection with the Eighth Review, but his position was flexible and he could go along with the consensus among Directors.

Mrs. Filardo remarked that she could go along with the consensus among Directors on the period of consent and participation requirement.

Mr. Yamazaki said that his position was flexible with respect to the amount of the quota increase members should be required to subscribe to. He supported the proposal to extend the period of consent to December 30, 1991, with a participation requirement of 85 percent and of 70 percent thereafter.

Mr. Kwon commented that the management and staff should examine the methods used by the World Bank to reallocate forgone quota shares and the legal implications of pursuing such a reallocation.

The Chairman noted that the issue of payments for the increase in quotas had been considered on several previous occasions, and Directors had agreed that 25 percent of the increased subscription should be paid in SDRs or in currencies of other members specified, with their concurrence, by the Fund. In addition, a consensus had been reached that subscription payments

must be made within 30 days from the latter of the date on which the member consented to the increase in its quota or the date on which the Fund determined that the participation requirement had been met.

The Committee members then took up the issue of members with overdue financial obligations to the Fund.

Mr. Monyake stated that the members with overdue financial obligations that were actively cooperating with the Fund and that were in the process of economic adjustment should not be denied an increase in quota. There should be some provision that would allow such members to consent to an increase in their quotas if they were in a position to do so before the next quota review.

Mr. Ismael commented that he agreed that members must discharge their overdue financial obligations to the Fund before being allowed to consent to an increase in their quota and that some flexibility should be provided for members cooperating with the Fund.

He wondered whether the indication contained in the Managing Director's statement that "the Board will give sympathetic consideration to any request from a member for an increase in quota up to the amount that had been proposed under the Ninth Review" was intended to imply that an increase in quota could be requested at any time or that a special quota increase could be requested under the Tenth Review, Mr. Ismael said. The former interpretation would mean that the period of consent would not really lapse for members in arrears. In addition, he wondered whether the phrase "up to the amount" was meant to imply that members currently in arrears to the Fund would be allowed to take up less than the full amount of the quota increase proposed, while other members would have to choose to subscribe to the full amount or nothing.

Mr. Grosche stated that, as a matter of principle, a member in arrears should not be allowed to consent to an increase in its quota. In very exceptional circumstances, in which the member was cooperating with the Fund, an assured extension of the period of consent could be envisaged, but it would be prudent to refrain from defining such cases and the procedures to be followed in precise terms. At the present stage, when the Fund was strengthening its cooperative approach to dealing with cases involving overdue financial obligations, such precise criteria and definitions could convey a misleading signal that arrears could be condoned beyond the period of consent. Therefore, the Board should act at an appropriate time on a case-by-case basis.

Mr. Filosa said that he strongly agreed with Mr. Grosche's comments. In addition, it should be made clear to members in arrears that any extension of the period of consent would not be open ended.

Mr. Kafka remarked that, while the Fund needed to be tough, it also had to be sensible. Owing to the difficulties involved in obtaining the necessary resources to enable a country to clear its arrears, it would be possible for a member to miss the period of consent through no fault of its own. In that connection, it should be noted that two different types of cases were likely to arise. First, a determination would have to be made as to whether the period of consent could be extended for members who were actively cooperating with the Fund, but for reasons beyond their control would be unable to clear their arrears before the period of consent would lapse. Second, there could be cases in which the member had cooperated with the Fund, but the period of consent had not been extended, and requested an increase after the arrears were cleared. In the latter case, some Directors had suggested that, if a member settled its overdue financial obligations to the Fund after the period of consent had lapsed, sympathetic consideration should be given to a subsequent request for a quota increase. In dealing with such cases, he would prefer to follow the procedure that was established for other reasons at the time of the Eighth Review. In any event, it was necessary to distinguish between the different types of cases.

Mr. Dawson stated that he strongly supported the emerging consensus that a member in arrears should not be permitted to take up an increase in its quota. While he was prepared to allow for some flexibility in temporarily extending the period of consent to enable members to clear their arrears and subscribe to quota increases, such an extension should be limited to not more than one year following the deadline for the period of consent. In addition, the consideration of subsequent requests for quota increases should be based on the member clearing its overdue financial obligations to the Fund--not on its agreement to undertake a Fund-monitored program under the strengthened arrears strategy.

Mr. Grosche noted that there was a need to distinguish between the existing cases involving overdue financial obligations to the Fund and similar cases that might arise in the future. While some sympathetic consideration should be given to the existing cases, the Fund should be very tough in order to deter potential arrears cases from arising in the future. With respect to the latter cases, there should be no extension of the period of consent.

Mrs. Filardo commented, with respect to the position taken by Mr. Dawson that the period of consent could be extended for only one year, that it should be noted that one year might not be sufficient in present circumstances, when it was very difficult to obtain the resources needed to clear arrears.

Mr. Dawson responded that, given the December 30, 1991 deadline for the existing period of consent, such an extension would comprise two and a half years. If, by the end of 1992, a great deal of progress had been made by the 11 members currently in arrears, but one or two of those members still

had some overdue financial obligations, the Board would certainly be sympathetic in considering a somewhat longer extension. However, at that time, the Board would be able to base its decision on a track record of cooperation over two and a half years. That period should be sufficient for at least 8 of the 11 members with overdue financial obligations to clear their arrears. In any event, the Fund had to establish some limit to the possible extension of the period of consent in order to lend credibility to the strengthened arrears strategy.

Mr. Grosche stated that he agreed with Mr. Dawson. The Fund would probably have to provide for some synchronization in the timing of Fund-monitored programs, the clearing of arrears, and the period of consent. In that connection, if the Fund-monitored program and the clearing of arrears were planned over a prolonged period, it might be necessary to extend the period of consent beyond end-1992. However, each case would need to be assessed separately in terms of the time frame that was envisaged for the clearing of arrears.

Mr. Kafka noted that Mr. Grosche's comments implied an absolute exclusion of any member that did not currently have overdue financial obligations to the Fund from receiving flexible treatment, which was not fair. Why should the Fund discriminate between a member that had had arrears for three months and another that would fall into arrears through no fault of its own in the coming months? To the extent that members' circumstances differed, it would not be prudent to establish firm rules on extensions for the period of consent. On the contrary, the Board should preserve its ability to use discretion in extending sympathetic consideration to members.

The Chairman responded that the suggestions put forward by Mr. Grosche and Mr. Dawson contained an element of deterrence. While the Fund was certainly prepared to assist the 11 members currently in arrears, it would not be possible to respond as flexibly to arrears cases in the future. Perhaps the staff could comment on whether the Fund had established a regime of sympathetic consideration for members in arrears in connection with previous quota reviews.

The Deputy Treasurer recalled that the Fund had extended sympathetic consideration to members requesting quota increases after the period for consent had lapsed in four of the five most recent quota reviews, but those cases had not involved overdue financial obligations.

During the Eighth Review, several members had had overdue financial obligations to the Fund, but there had been no provision in the Resolution prohibiting such members from participating in a quota increase, primarily because none of those cases involved protracted arrears and the amounts involved were relatively small.

Mr. Fogelholm commented that he supported the views expressed by Mr. Dawson.

Mr. Dawson remarked, with respect to the degree of flexibility that would be extended to members in arrears when the period of consent lapsed, that it was important to bear in mind that the plans to strengthen the Fund's cooperative approach in dealing with such cases required members currently in arrears to enter into the "rights" approach before the May 1991 Interim Committee meeting. Therefore, the members currently in arrears should have a Fund-monitored program in place in the near future.

Mr. Kafka stated that the Fund should not establish firm rules and deadlines that could prove to be highly unfair. On the contrary, similar cases should be treated similarly without respect to timing, and the Board should always preserve the option to address the circumstances of members on a case-by-case basis.

Mr. Al-Jasser commented that Mr. Kafka's remarks could be interpreted as indicating that the flexibility the Fund was extending to members in arrears was a privilege and that the Fund had to use similar flexibility in giving equal treatment to future cases involving arrears, which was not true. Indeed, it would not be prudent to send such a signal to the international community. Instead, the main principle should be that a member in arrears must discharge its overdue financial obligations to the Fund before it would be permitted to consent to an increase in its quota.

With respect to the period of extension, he wondered what could be done for members under Fund-monitored programs, in particular under the strengthened arrears strategy, given that many of those programs were expected to extend beyond the date for the establishment of the Committee of the Whole for the next review, especially if the Tenth Review was held in 1993 as provided for in the Articles.

Mr. Cassell said that he agreed that no member with overdue financial obligations to the Fund should be allowed to consent to an increase in quota until its arrears were cleared. He also agreed that for members that were actively cooperating with the Fund there should be a limited extension of the period of consent. However, such an extension should apply to only those members currently in arrears, because that rule would help to deter other such cases from arising in the future.

At the present stage, it was difficult to determine whether an extension of one year beyond the deadline for the period of consent would be sufficient, Mr. Cassell considered. Therefore, it would be prudent to avoid such establishing rules at the present stage, and determine the period of extensions in the light of prevailing circumstances near the end of 1991.

Mr. Al-Jasser stated that he agreed with Mr. Cassell that it would be best to wait until end-1991, when the members in arrears had established a track record of cooperation with the Fund in the implementation of Fund-monitored programs, to determine an appropriate extension of the period of consent. In that connection, he agreed with Mr. Grosche's comments on the need to provide some synchronization between the timing of Fund-monitored programs, the clearing of arrears, and the period of extensions.

Mrs. Filardo asked what would happen if new cases involving arrears emerged before end-1991.

The Chairman replied that such an eventuality should be taken into consideration in the context of the discussions on the strengthening of the Fund's cooperative approach to dealing with overdue financial obligations. Directors did not seem to be prepared to consider extending the period for consent for members with overdue financial obligations other than the 11 countries already in arrears.

Mr. Clark and Mr. Yamazaki said that they supported the views expressed by Mr. Cassell and Mr. Grosche.

After a further brief discussion, the Chairman noted that the broad consensus among Directors was that no member with overdue financial obligations to the Fund should be permitted to consent to an increase in quota until the arrears were cleared. The Board would be in a better position by December 1991 to determine a possible extension of the period for consent, and could take into account the situation of the 11 members currently in arrears, on the basis of their record of cooperation with the Fund. In addition, Directors agreed that sympathetic consideration could be given to requests for quota increases from members with overdue financial obligations after the period for consent had lapsed in the light of their track record under a Fund-monitored program.

The Committee members then concluded their consideration of a statement by the Managing Director on the Ninth General Review of Quotas.

APPROVED: April 26, 1991