January 14, 2000
Approval: 1/24/00

INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 98/101

10:00 a.m., September 21, 1998

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Executive Board Attendance

S. Sugisaki, Acting Chairman

Executive Directors

R.F. Cippà
B. Esdar
E.R. Grilli

W. Kiekens
K. Lissakers
J.-C. Milleron

S. Pickford
A.S. Shaalan
M.R. Sivaraman
G.F. Taylor
J.J. Toribio
J. de Beaufort Wijnholds

Alternate Executive Directors

S.M. Al-Turki
C.X. O'Loghlin
M. Askari-Rankouhi, Temporary

W.-D. Donecker
J. Spraos
J.P. de Morais
O.-P. Lehmussaari
O.L. Bernal, Temporary
J. Prader
B.S. Newman
R. Fernandez
M. Daïri
A. Lushin
M.A. Brooke, Temporary
M.H. Elhage
A.G. Karunasena
O. Kwon

A. Barro Chambrier
A.R. Ismael, Temporary
H. Ono
C. Harinowo
Zhang F.
N. Eyzaguirre
O.A. Hendrick, Temporary

R.H. Munzberg, Secretary
P. Cirillo, Assistant

European Economic and Monetary Union and the Fund—Surveillance; Use of Fund Resources and Use of Euros in Operational Budget—Preliminary Considerations; and Main Legal Issues Relating to Rights and Obligations of EMU Members in the Fund

Staff representatives: Gianviti, LEG; Lipschitz, PDR; Kuhn, TRE; Artus, EU1

European Economic and Monetary Union and the Fund—SDR Valuation and SDR Interest Rate

Staff representative: D. Williams, TRE

Also Present
African Department: E. Hernández-Catá, Deputy Director. European I Department: M.C. Deppler, Director; J. Artus, Deputy Director; M.D. Knight, Deputy Director; J. Canales, K.H.W. Knot, A. Leipold, D.C. McDonald, K.A. Swiderski, H.J. Temprano. External Realtions Department: P.E. Gleason. Fiscal Affairs Department: E.A. Mottu. Legal Department: F.P. Gianviti, General Counsel, W.E. Holder, Deputy General Counsel; R.C. Baban, H. Elizalde. Policy Development and Review Department: J.T. Boorman, Director; T. Leddy, Deputy Director; G.A. Barnard, K.J. Langdon, L.J. Lipschitz, R.H. Nord, R. Weber. Research Department: M. Mussa, Economic Counsellor and Director; P.B. Clark, G.J. Schinasi. Secretary's Department: J.M. Boughton, P. Gotur, A. Mountford, J. Prust, B.A. Sarr. Statistics Department: E. Ayales, S.P. Quin. Treasurer's Department: D. Williams, Treasurer; S.P. Bernhardt, K. Boese, C.P. Clarke, J.C. Corr, L.U. Ecevit, C.A. Hatch, D.K. Kar, M.G. Kuhn, C.J. McAuliffe, A.F. Moustapha, O. Roncesvalles, M.A. Wattleworth, I. Zaidi. Western Hemisphere Department: S.P. Tokarick. Office of the Managing Director: M. Russo, Special Advisor; B.V. Christensen, J.A.P. Clément, P.J. McPhillips. Advisors to Executive Directors: P.M. Fremann, A. Giustiniani, C.M. Gonzalez, E.J.P. Houtman, B. Konan, H. Ogushi, O. Sein, M.R. Shojaeddini, M. Sobel, F. Zurbrügg. Assistants to Executive Directors: A.S. Alosaimi, T. Belay, J.G. Borpujari, S.A. Bakhache, R. Burgess, M. Carlens, H.W. Cocker, D.A.A. Daco, K. Gobe, N. Goffinet, M.R. Hajian, S. Hinata, C. Josz, A. Kapteijn, K. Kpetigo, Lu A., A. Lucenti, W. Merz, K. Ongley, J.L. Pascual, J.N. Santos, J. Schaad, C-P. Schollmeier, G. Vigliotti, M. Walsh, Wang X., I. Zakharchenkov.

1. **EUROPEAN ECONOMIC AND MONETARY UNION AND THE FUND—SURVEILLANCE; USE OF FUND RESOURCES AND USE OF EUROS IN OPERATIONAL BUDGET—PRELIMINARY CONSIDERATIONS; MAIN LEGAL ISSUES RELATING TO RIGHTS AND OBLIGATIONS OF EMU MEMBERS IN THE FUND**

The Executive Directors considered staff papers on the European Economic and Monetary Union (EMU) and the Fund with respect to surveillance (SM/98/215, 8/26/98), on preliminary considerations regarding the use of Fund resources and the use of euros in the Fund's operational budget (EBS/98/132, 8/4/98), and on main legal issues relating to the rights and obligations of EMU members in the Fund (SM/98/131, 7/8/98).

Ms. Lissakers and Mr. Newman submitted the following statement:

> The advent of EMU and adoption of the euro will pose some unique issues for the IMF. In particular, there is a need to reconcile the rights and obligations of EMU members under the Fund's country-oriented Articles of Agreement with the economic realities and logic of a monetary union with an international currency issued by a supra national body. The staff papers might have considered the option of an amendment of the Articles of Agreement to deal with the potential dilemmas created by this situation although we recognize that EMU is still in a transitional phase and an amendment would raise sensitive political issues that might best be addressed at a later time. Therefore, we would agree that our efforts should focus on integrating EMU and the euro into the Fund's activities on the basis of the present Articles, provided it can be accomplished in a way that does not impair the IMF's ability to fulfill its responsibilities in an effective and equitable manner.
>
> As regards the operational budget, the staff legal paper makes the basic point that the transfer of monetary powers by members of the euro-area to institutions of the EMU will not affect their IMF rights and obligations, including those related to the Fund's financial operations, representation in the IMF's governing bodies and voting powers. Moreover, the concept of the balance of payments applies whether a country is a member of a monetary union or has its own currency. However, the balance of payments strength and weakness as well as financing capacity of the individual member states cannot be determined separately from the overall position of the union. Thus, while an individual member state or region may experience economic and financial difficulties, this need not imply a union-wide balance of payments problem, inadequate reserves or a weak euro.
>
> Therefore, we would agree with the staff that decisions on inclusion of the euro in the operational budget should be based on an assessment of the financial position of the overall union. What is less clear, however, is how to determine the amount of euros to be included in the operational budget and how the obligations to provide resources should be allocated among the IMF members participating in the euro-area.
>
> One method for determining the amount of euros in the budget would be an ad hoc approach such as currently used for the dollar. Under this

approach, the amount of euros in the budget would be based on the share of the euro in the Fund's holdings of usable currency as is now done with the dollar. However, this would still leave open the issue of how to allocate euro use and the corresponding reserve claim on the Fund among EMU member states. The current approach of allocating currency transfers based on the members' gold and foreign exchange reserves is problematic with regard to EMU members, given the difficulty of distinguishing between the gold and foreign exchange reserves of the member states and the ECB. Moreover, since the euro presumably will be a freely usable currency for IMF purposes, EMU members will be able to meet their IMF obligations without experiencing foreign exchange reserve losses. The amount of external assets held by the member states and the ECB is therefore less relevant in assessing the capacity of EMU members to provide resources to the Fund in the operational budget.

In these circumstances, we would agree with the staff that a more transparent and equitable approach would be to allocate proposed transfers in the operational budget among all members, both EMU and non-EMU, on the basis of quotas. However, we do not see the need for an extended transition period as the magnitude of the changes in currency use that would occur is small relative to the reserves and financing capacity of countries in the operational budget. Moreover, an early change to a quota-based allocation could help to strengthen the Fund's financial position by facilitating full use of a wider range of currencies.

The staff legal paper argues that an EMU member would retain all its rights and obligations under the IMF Articles, including those regarding the provision of financing and the use of Fund resources. However, the ability of an EMU member to meet its IMF obligations to provide euros will depend primarily on its taxing and borrowing capacity, particularly as it will not be able to acquire euros from the ECB due to the no bail-out clause. While remote, the possibility exists that an EMU member could be unable to provide euros and would be excluded from the operational budget due to fiscal, rather than balance of payments problems, even though the euro would continue to be used in IMF transactions and operations. In some circumstances, an EMU member might even be able to obtain Fund resources, including euros, to deal with a fiscal rather than a balance of payments problem.

Such an outcome may be legally feasible but one wonders whether it is economically desirable or equitable to other Fund members. For example, excluding an EMU member from the operational budget due to fiscal problems unrelated to a balance of payments difficulty would increase the financing burden on other members, including countries which are not EMU participants. Similarly, use of Fund resources by the fiscally challenged EMU country could have implications for the no bail-out clause as other EMU participants could be required to provide euros. In some circumstances, IMF conditionality associated with the use of Fund resources could involve measures that would conflict with the EMU objectives.

The potential for such policy dilemmas may appear limited, particularly given the magnitude of transfers in the operational budget relative to the financing capacity of individual EMU states. However, the risk is not zero and prudence suggests that it might be useful to consider ways to eliminate it altogether. The staff legal paper indicates that issues relating to the assessment of balance of payments need for a member of a monetary union will be considered at a future Board meeting. In view of the important role which the euro will play in the IMF, we believe that this issue should be given a high priority, preferably before the euro is launched on January 1, 1999. In this context, the staff may want to consider whether it would be desirable to have an understanding with EMU participants whereby the ECB and/or other EMU members agree to provide euros to a member to enable it to fulfill its financial obligations to the Fund and that all euro members agree to refrain from using IMF resources as long as the euro is included in the operational budget.

Turning to Fund surveillance, the adoption of a single monetary policy under the responsibility of an independent ECB will require a regional approach to IMF surveillance of EMU countries. We have a preference for the more formal approach suggested by the staff as that would be most consistent with the surveillance mandate provided in the Articles of Agreement. We also believe that it can be undertaken in a manner that does not damage political sensitivities during the continuing transition phase of EMU. We would also agree with the staff that regional surveillance of the euro should extend beyond the conduct of monetary and exchange rate policy to include other issues, particularly the fiscal position of the euro-area as well as union-wide structural issues, especially financial and labor market issues. For this purpose, the staff should consult with a wide range of individuals and institutions both at the regional and national levels. We are open-minded on the frequency and timing of such consultations, although it is not clear why regional consultations need to be more frequent than bilateral Article IVs. We would also support an annual report to and discussion by the Executive Board, including issuance of a PIN. We would leave to EMU members the decision on which EU institution should make the decision on release but would note that the problem could be eliminated by adopting mandatory PINs for all Article IV consultations.

We would also agree to continue bilateral surveillance discussions with the member states on national fiscal, financial and structural policies as well as the impact of ECB monetary policies. Over time, it may be useful to reduce the frequency of bilateral Article IVs although continued annual consultations would be useful during the initial phase of EMU.

With regard to EU participation in Executive Board discussions, we would agree to extending observer status to the ECB for bilateral Article IV consultations with member states, regional surveillance of the euro-area and discussions of the WEO and international capital markets. However, participation should be on the same basis as other observers in Board meetings and thus limited to responding to specific questions. The reaction of other relevant EU institutions to staff papers should be communicated to the Board through an EU Executive Director.

We would agree that EU members have an obligation to provide the Fund with the data necessary for the IMF to fulfill its responsibilities, including information on regional developments. Similarly, we would have no objection to providing the ECB the country documents currently provided to the EC as well as other relevant papers related to the international monetary system, especially the WEO and International Capital Markets reports.

As to SDR valuation and interest rate, the current rules on SDR valuation and interest rate are also country centered rather than currency based, reflecting the basic orientation of the Articles of Agreement. We would support the staff's proposal to substitute the euro for the DM and French franc in the valuation basket with the current weights as a transitional measure. However, the introduction of the euro may raise more fundamental issues regarding the valuation of the SDR, including the composition of the basket and the appropriate weighting scheme. For example, the continued inclusion of the euro in the basket on the basis of German and French exports could require a substantial reduction in the euro's weight in a post-EMU world as intra EU trade is excluded. Therefore, we would prefer a somewhat shorter interval for considering the next revision of the valuation basket, possibly 2001 or 2002 rather than the 2003 proposed by the staff.

Finally, we can accept the staff's proposals regarding the SDR interest rate basket.

Mr. Kiekens and Mr. Prader submitted the following statement:

A discussion on how country members of the Economic and Monetary Union (EMU) should participate in the Fund's Operational Budget is timely because of the imminence of both the review of the operational budget's guidelines, and the start, on January 1, 1999, of EMU's stage III.

In determining our position on this issue, we have been guided by the following principles: Any solution must accommodate the overriding imperative of securing the financing of the Fund. The solution must be fair and equitable. The solution should be as transparent as possible. The solution should be workable, i.e. it must provide a sufficiently long transition period to ensure the smooth, uninterrupted functioning of the operational budget.

We agree with the staff that for purposes of deciding on the participation of euro-area members in the operational budget, the level of their external reserves "can be meaningfully identified only at the level of the Union as a whole."

We believe identification of the currencies that are strong enough to participate in the operational budget should still be based on reserves. Here, not only the reserves held by the european Central Bank (ECB) but also those remaining with the national central banks (NCBs) should be counted. The reserves remaining with the NCBs are available to augment the reserves of the ECB. Moreover, the NCBs will manage their external reserves in accordance with the ECB's instruction for the purposes of their tasks as members of the European System of Central Banks (ESCB). Consequently, the NCBs' reserves should be considered as belonging to the general pool of reserves.

It follows from these considerations that options 1 and 2 are neither practical nor useful. Option 1—basing the allocation solely on the reserves of the ECB—would dramatically reduce the EMU countries' total contribution to the operational budget. Option 2—basing the allocation on the reserves of the national central banks—would be much more realistic, but leaves out the ECB's reserves, which after all represent the core of the ESCB system.

Option 3—treating only the EMU members' contribution and the U.S. contribution to the operational budget on the basis of quotas—is a clear improvement over options 1 and 2, both in terms of greater simplicity and transparency and in terms of securing the financing of the Fund. At least this would amount to a recognition by the Fund that "for those countries that are fully integrated into the international monetary system, such as the euro-area countries," the distribution of the allocation on the basis of foreign exchange and gold reserves is an outdated concept. Even though option 3 would probably cover some 80 percent of the Fund's operational budget, it would violate the principle of uniform treatment.

We prefer Option 4—basing all countries' allocations on their quota shares—because it offers a clear, transparent, simple and equitable solution to the operational budget problem. Not only would it end years of controversy about the equity of the current distribution of the operational budget, it would also achieve symmetry of rights and obligations in the Fund based on the Fund's own standard of equity. In addition, it would immediately make all contributors' shares comparable and transparent, thereby opening the way to a consensus on publishing the list of contributors.

Both Option 3 and Option 4 would increase the total share of euro-area countries in the financing of the Fund above its level under the present system.

We accept a transition period long enough for members' positions in the operational budget to be harmonized smoothly on a quota basis.

In regards to the EMU and Fund surveillance, the advent of the EMU on January 1, 1999 represents a major change in the international monetary system. The adoption by member states of the European Community (EC) of common policies in the framework of EMU, particularly a common monetary policy conducted by an independent central bank, will require the Fund to adjust its surveillance to the shift of significant responsibility from national authorities to the institutions and bodies of the EC.

When the responsibility for monetary, exchange rate, and other economic policies, subject to the Fund's surveillance has been transferred to institutions and bodies of the EC, Fund surveillance discussions have to be enlarged to include these competent institutions and bodies as specified by the staff.

The Fund's discussions with European Union (EU) institutions will typically include monetary and exchange rate policies, the fiscal position of the euro-area as a whole, structural policies critical for the smooth functioning of the EMU, and the soundness of the euro-wide financial system. This applies also to trade and competition policies, the responsibility for which has been transferred to EU institutions.

As to the frequency of the consultation on common policies in the framework of EMU, the staff prefers two consultations resulting in two staff papers and two Board discussions a year. However, Article IV consultations with Fund members of systemic importance take place only once a year unless there is a threat of crisis. In addition, reviewing issues too often can result in empty Board discussions. We see merit in an annual consultation mission, complemented by a follow-up staff visit about six months later. The annual consultation would produce a staff report and be completed by a Board discussion. The follow-up visit would produce an information paper for the Board, which could be discussed together with the World Economic Outlook. This paper would also provide background information for bilateral Article IV consultations that could not be clustered around the annual consultation.

The summing up of the Board discussion concluding the consultation on EMU policies can be published as Public Information Notice (PIN), subject to the consent of all concerned members.

EMU is a long step forward for European integration. But since many important policy areas will remain at the national level, bilateral Article IV consultations with individual members of the euro-area must remain the main element of Fund surveillance. The focus of these bilateral consultations will be fiscal, financial, and structural policies, with consideration of monetary policy limited to the consistency of other policies with the monetary policy stance of the ECB. This arrangement is not much different from that prevailing for countries like Belgium, Luxembourg, and Austria that for many years have pegged their currencies to the deutsche mark.

It is useful to grant observer status to the ECB in the Fund, the modalities of which will have to be determined. It is also important for other EU institutions to be able to communicate their opinion on selected issues discussed in the Fund.

The Fund should make the necessary arrangements, particularly with the ECB and EUROSTAT, to ensure the availability of all data and information necessary for effective surveillance of EMU policies.

It is evident that EC member states can transmit all Fund documents to the competent EC institutions and bodies, in accordance with arrangements made by and among them.

The staff provides an analysis of the legal effects of EMU on the rights and obligations of euro-area members under the Fund's Articles of Agreement. The paper does not examine the relations of the member states of the European Community with the IMF under European law. A comprehensive clarification of the legal effects of EMU for the IMF will require the issue to be examined from both standpoints. If this exercise reveals that the two legal orders are not congruent, the European members and the IMF must cooperate in interpreting or adjusting the Fund's Articles.

Since our authorities have not yet had time to examine the details of the legal issues paper, our observations must be preliminary.

In contradiction to the view of the IMF staff, the Fund's Articles should be interpreted as not permitting countries that issue euros to obtain euros from the Fund, since the euro is their domestic currency and cannot therefore be regarded as a foreign currency.

Contrary to the apparent position of the IMF staff, it would be appropriate in some cases to consider the balance-of-payments position of the euro-area as a whole, rather than the balance-of-payments positions of individual euro-area countries. This might be the case when deciding on the Fund's operational budget. For the same budget, it would likewise be appropriate to consider the reserve position of the ESCB as a whole, including the reserves held by the ECB, rather than the reserve positions of individual countries. More generally, it seems appropriate to treat the foreign reserves held and managed by the ECB as part of the reserves held by euro-area countries when applying the Fund's Articles.

Still contrary to the staff's position, assets of national banks denominated in the former currencies of other euro-area countries before their conversion into euro denominated assets should be classified as domestic assets and not international reserves when applying the Fund's Articles.

We agree that the ECB is eligible under the Fund's Articles to hold SDRs as a prescribed holder.

Under the Fund's Articles, the legal title to reserve positions in the Fund remains with the member states. However, the EC Treaty requires that the ESCB hold and manage the member states' reserve positions in the Fund. In consequence, all the rights normally attached to ownership of the reserve position in the Fund will be vested in the national banks as members of the ESCB. The same holds, mutatis mutandis, for SDR holdings and allocations.

Extending his remarks, Mr. Prader said that, in response to the preliminary statement by Ms. Lissakers and Mr. Newman, he would basically be amenable to considering the need for an extended transition period until a quota-based operational budget was achieved; however, it was important to recognize that, for some countries, there would be more than a small change. A transition period might help develop an as broad as possible consensus on the matter. On the potential for policy dilemmas, which, according to the U.S. statement, was small but not zero, it was unnecessary, in practical terms, to require an understanding with EMU participants, whereby the ECB and/or EMU participants would agree to provide euros to a member to enable it to fulfill its obligations to the Fund and all euro-area members would agree to refrain from using Fund resources as long as the euro was included in the operational budget

Mr. Cippà made the following statement:

The four staff papers set out the multitude of issues that the creation of the European Monetary Union (EMU) will have on our institution. Integrating a group of currently eleven countries that not only have decided to adopt a common currency, but also to create a single market for goods, services, labor, and capital poses a formidable challenge for a country-based institution. While we have already successfully accommodated various monetary unions, the latter characteristic of the EMU makes this case exceptional. However, after reading the detailed presentation of the various issues, I have the impression that many of them are perhaps legally complex, but should not pose major problems at the practical level. For example, we are dissecting the problem of how we can identify possible future balance of payments needs of individual EMU members, because each of them will of course continue to have the right to request Fund resources under such circumstances. Another example is the question on whether the use of Fund resources would be consistent with the "no bailout" clause of the Maastricht Treaty. The practical relevance of such questions for the operations of the Fund is probably quite small.

Concerning legal issues relating to the rights and obligations of EMU members, the paper gives one clear message: despite the introduction of a common currency, the one-country-one-member principle will still be valid for member countries of EMU. The shift of economic and monetary responsibilities to EMU institutions does not exempt each euro-area member of its obligations vis-à-vis the Fund. EMU institutions will have to act consistently with the obligations of members of the Fund under the Articles. This is an important message in terms of equal treatment of all members. However, the fact that many of the rights and obligations of a Fund member hinge on its balance of payments position and reserve position poses some serious obstacles. While measuring the EMU's balance of payments and reserves position is straightforward, making these two concepts operational for each member is problematic.

Regarding the issue of reserves, I share the staff's view that it is very difficult to determine whether NCBs still hold reserves according to the Fund's definition or not. It is thus important that the ECB soon clarifies this issue by providing adequate guidelines. However, given the need in the EMU to conduct a single and coherent monetary policy for the whole euro-area, it is difficult to imagine that NCBs can be allowed too much discretion over the use of their foreign reserves. It would thus seem logical that reserves held by NCBs will not be covered by the Fund's definition. I am confident that the ECB together with the Fund and eurostat will find a mutually acceptable way to define the individual members' reserve positions

However, regarding the identification of individual members' balance of payments positions, the obstacles are formidable. I don't want to repeat the points made in the staff paper on this issue. It is clear that a lot of effort has to be put into compiling meaningful balance of payments statistics for EMU countries However, the difficulties arising in the compilation of intra-EMU flows are evident and the Fund will probably have to live with the fact that the data for these members will be less reliable. Compiling national balance of payments positions primarily to satisfy the data obligations towards the Fund might not necessarily receive top priority.

As regards use of euros in the operational budget, a members' balance of payments position and its holdings of international reserves are the primary criteria for the assessment of external financial strength and, therefore, crucial for the allocation of currencies in the operational budget. If external strength should be assessed at the level of individual EMU members, then meaningful balance of payments for each member will have to be established. Given the recognized difficulties of this endeavor, I share the staff's view that is reasonable to include in or exclude all EMU members from the operational budget, depending on whether the euro itself is deemed sufficiently strong.

In terms of allocation mechanisms, we should concentrate on the staff's third and fourth approaches. The adoption of the framework used for the US dollar, could be a valid alternative. The EMU will resemble the US in many respects, given its single currency, centralized monetary policy, highly integrated markets in combination with its crucial position in the world economy. The crucial advantage of this approach is the easy calculation of transfers, since reserve positions must not be known for individual EMU members. Furthermore, the important drawback of the first approach, namely a substantial change from the current distribution of transfers among the different currencies, would be avoided.

The fourth approach suggesting to use the quota shares for all members included in the operational budget for the allocation of currencies for transfers would have the important advantage of uniformity in application. All sufficiently strong members would be treated according to the same criterion and consequently the transparency of the allocation mechanism would increase. However, this approach would signify a important shift in burdens from "Other Strong" members to "Other European" members. In my view, breaking with the past distributions would be justified in view of the advantage of uniformity of treatment under this approach. This aspect will also be important in the context of our endeavor to enhance transparency regarding the Fund's liquidity position.

As to EMU and Fund surveillance, the shift in authority on monetary and exchange rate policy as well as the strong interdependencies between policies taken at the national and the European level will without any doubt require intensified consultations with EU institutions, to fulfil the Fund's surveillance mandate. I have the following comments on the staff's framework.

As regards the status, frequency and timing of these discussions, I think it would be useful to continue annual consultations at the national level within the established framework of Article IV consultations. To take due account of the shift in policy responsibilities under EMU, I believe that systematic biannual consultations would be needed, especially during the first years of EMU. As it would not be efficient to have visits to the ECB and other EU institutions in the context of individual Article IV consultations, nor would it be feasible to have a single cluster of bilateral consultations with regional surveillance missions to EU institutions, I believe that there would be a clear benefit to cluster bilateral consultations with the staff's visits to EU institutions Preferably these biannual consultations should coincide with the preparations for the World Economic Outlook

With respect to the issues of coverage and reporting, respective responsibilities between the national and European level should be used as a guiding line for consultations. Consultations on the national level should focus more on fiscal and structural policy issues. Discussions on monetary policy should mainly be concerned with the impact of the stance of monetary policy on the national economy as well as the implementation of monetary policy operations through the national central banks, as suggested by the staff. Consultations on the European level would therefore focus on monetary and exchange rate policy issues. Nevertheless, it will be important to assess the fiscal position as well as the labor market developments from the European level, as they are crucial for the smooth functioning of EMU. To enhance transparency I encourage the use of PIN's with respect to regional surveillance.

Regarding the representation of EU institutions at the Board, I could support the emerging consensus among EU members to establish an observer status for the ECB for selected meetings. However, the higher relevance of the ECB compared to the other organizations that already have an observer status must be taken in to account by appropriate arrangements in terms of participation in the Board discussions Regarding the views of the Council, in my opinion one of the EU chairs could be mandated to communicate them in the relevant discussions. This could be done on a rotating basis similar to the presidency of the Council

On SDR valuation, the introduction of the euro poses only minor problems for SDR valuation and the determination of the SDR interest rate. I welcome the pragmatic approach proposed, which ensures continuity and results in an appropriate initial weight of the euro in the SDR basket. I agree with decisions 2, 3 and 4.

Regarding decision 1, I agree with the staff's proposal to reset the five-year cycle for revision of the SDR to start in January 1999, thus coinciding with the start of EMU. However, I would like to emphasize that the provision for a possible revision of the valuation method in 2003 or before means that the calculations will be based on euro transactions data of at most four years. Nevertheless, we think that such a data base will be large enough to generate a sensible weighting. We therefore agree on decision number 1.

Mr. Bernal made the following statement:

In regards to the main legal issues relating to rights and obligations of EMU members in the Fund, we thank the staff for the comprehensive set of documents providing an ample view of the main operational issues. From these documents and previous discussions at the Board, it is clear that euro-area Fund members will continue to be members of the Fund in their own individual capacity as countries; all rights of membership will continue to be available to each individual member, and all obligations vis-à-vis the Fund will continue on each euro-area member country Also under the Fund's Articles, the creation of a monetary union does not create collective rights and obligations in the members' relations with the Fund However, the implementation of individual rights and obligations by each member may be affected by the adoption of the monetary union, particularly in relation to reserve assets, balance of payments data, transactions with SDRs, and access to Fund resources

Given the importance of the concept of reserves and balance of payments in most of the operational relations of the Fund with member countries, and in addition to the commitment of the members of the euro area to provide information to the Fund in accordance with Article VIII, Section 5(a) that will allow the Fund to ascertain each individual member's balance of payments situation, a prompt consensus is required among ECB, eurostat, and the Fund in how reserves should be defined for individual members of the euro area, the ECB, and EMU In this connection, specific characteristics need to be defined for the financial instruments to be used in the transfer of reserves by national central banks to the ECB.

On the use of the Fund resources and use of euros in the Fund's operational budget, a request for the use of the Fund's general resources by an EMU member should be honored in the same way as a requests by any other Fund members. Although under the actual strong economic conditions of euro-area members it may be unlikely that a balance of payments need would arise, it is likely that the Fund would be able to recognize the need if there was one. Given the difficulties which arise in the accurate measurement of reserves and balance of payments situations, we recognize that a balance of payments need for an individual member of a union has to derive from evidence of other accommodating transactions, including financing or liquidity support by the ECB and evidence of interest rate pressures and market segmentation.

We also share the staff proposal that inclusion in or exclusion from the operational budget should be common to all members of the currency union, depending on the euro-market condition. However, such a practice does not precluded that in the event a euro-area member develops balance of payments problems, the Fund would not use its holdings of that member's currency for transfers in the operational budget.

In relation to the allocation of transfers under the operational budget, we found a reduction in the contribution of the euro-area countries to the financing of the Fund inconvenient, especially under the present circumstances of world financial markets. Further analysis of this matter is required from the staff. We are of the opinion that the current system must be revised to avoid problems of uniformity of treatment. As a preliminary departure, we could be in favor of an approach based on Fund quotas as the distributive criterion.

As to EMU and Fund surveillance, the advance of EMU into the Stage 3 implies changes not only in euro-area countries but also in the international monetary system. Thus, under its surveillance mandate, the Fund must consider intensifying discussions with EU institutions in a more formal approach as part of the Article IV process. Although we prefer annual reports, the introduction of Stage 3 of EMU and its possible implications, at least in the early developments, demands permanent vigilance, such that the Board would be informed in an appropriate and timely manner. Also we are of the opinion that the policy on PINs which applies to regional surveillance should apply to regional surveillance of EMU. In this context, we consider that annual consultations for most EU members are appropriate at least until the currency union is consolidated.

We found that effective representation of EU institutions' views in Executive Board discussions is quite important for enhancing Fund surveillance in euro-area countries. In consequence, we support the idea of granting observer status to the ECB for selected Board meetings, as well as the possibility for relevant EU institutions to circulate a statement prior to the discussion. Finally, given the need and importance of adequate data, we agree that the staff should make arrangements with the ECB and EUROSTAT on the transfer of a set of data on a regular and timely basis.

Mr. Donecker made the following statement:

At the advent of EMU I welcome this opportunity for a necessarily somewhat preliminary exchange of views on several important operational and legal issues with regard to EMU and the Fund's operations and Articles of Agreement.

I am very grateful to the staff for providing us with a set of laudably short and concise papers on the subject matter, and to some of our colleagues for their helpful preliminary statements. Let me state at the outset that I fully agree with Ms. Lissakers and Mr. Newman that the European Monetary Union and the adoption of the euro will pose some unique issues for the IMF. There is indeed a need to reconcile the rights and obligations of EMU members under the Fund's country-oriented Articles of Agreement with the economic realities and logic of a monetary union with an international currency issued by a supra-national body. This challenging task will require from all of us a certain amount of flexibility, political pragmatism and above all the will to cooperate in the search for sensible solutions to any controversial issues that may arise in this context. For our discussion today and beyond, it is certainly useful to keep in mind that the European Monetary Union and in particular the ECB and the ESCB is still in status nascendi, i.e. in an early transitional phase, and that the respective motives of their founding fathers have been and are very much in line with the objectives of the Fund.

Our efforts should focus on integrating EMU and the euro as best as possible into the Fund's activities, on the basis of the present Articles.

As to the issue of "EMU and Fund surveillance," I think it is safe to say that EMU and the establishment of the European System of Central Banks as well as the introduction of the euro will certainly change the surveillance process of the Fund with some of its European member countries. However, I should like to stress that, while EMU will represent a profound step in European integration, the Article IV consultations with individual members of the euro area must remain the central, core part of Fund surveillance—not only because the responsibility for important policy areas such as fiscal policy will remain at the national level, but also because membership and a member's rights and obligations in the Fund are based—and will continue to be based—on national states. We would put more emphasis on this important aspect of Fund surveillance than the staff has done in its paper. But I note that the Legal Department has taken due account of this issue in its separate paper.

As to the content of bilateral surveillance discussions with EMU members, we can go along with the thrust of staff's proposals contained in paragraph 15. Here, as well as with regard to the periodicity of such future bilateral Article IV consultations—and in particular with regard to the details of the envisaged regional surveillance over EMU—we should, at this early stage, avoid becoming too definite on every detail of process and timing. After all, EMU and the creation of the euro are an evolutionary process: some of the related questions and issues can be best dealt with after we have gained some concrete experience in this field.

As to the framework for strengthening the Fund's regional surveillance in the context of EMU, it is important to recognize that EMU participants remain sovereign member countries of the IMF. Any regional surveillance over EMU members that includes the participation of, first and foremost naturally the ECB, but also, albeit surely to a much lesser degree, additional supranational EC institutions, has to respect this fact and the existing legal and contractual interlinkages and responsibilities.

Against this background and with regard to the status of the Fund's discussions with EU institutions, we have a strong preference for the first option mentioned by the staff, i.e. that the Fund's discussions with EU institutions should continue essentially along the lines of the current approach, with the discussions providing an important input to surveillance without being directly part of the formal Article IV process. We agree with the staff that these discussions would need to be strengthened and be made more systematic to take account of the shift in policy responsibilities under EMU. In this context of regional surveillance, consultations with the ECB should have the highest priority and should be the centerpiece. However, I should like to emphasize here that fiscal and structural policies are solely the responsibility of member countries. The Fund would remain free to talk to all other relevant EU institutions. In any case, such discussions with supranational EU institutions, including the ECB must always remain an integral part of an Article IV consultation with one or several member countries. Discussions with EU institutions should not be accorded an independent Article IV status, since this would undermine the principle that only national states can be IMF members with the related rights and responsibilities.

With regard to frequency and timing, we share the staff's view to have an annual regional consultation mission complemented by a follow-up staff visit about six months later. Otherwise there might be too much of a split between bilateral consultations and regional surveillance. The annual consultation would result in a staff report and be completed by a Board discussion. I agree with Messrs. Kiekens and Prader that the follow-up visit should lead to an information paper for the Board, which could be discussed together with the World Economic Outlook. This paper would also provide background information for those bilateral Article IV consultations that cannot be clustered around the annual consultation. The summing up of the Board discussion concluding the consultation on EMU policies could be published as Public Information Notice, subject to the consent of all concerned members. It is up to the EMU participants and the ECB to agree on a modus as to who should be entitled to authorize such a PIN.

Still on the issue of transparency: Any mission statements at the conclusion of such regional surveillance discussions are informal comments by the staff. They should be solely addressed to the participants in these discussions and should not be published. Allow me a two brief additional comments on bilateral Article IV consultations with EMU participants: Here we share the staff's view that discussions about monetary policy with the national monetary authorities should be restricted to operational issues and to the question of how the common monetary policy affects the respective country.

The staff's notion to possibly introduce a longer consultation cycle for certain EMU countries should be addressed in the context of a broader discussion about the appropriate length of consultation cycles and should not be limited to EMU countries.

As to the representation of the ECB's views in relevant Board discussion, we too see the necessity to grant this central monetary authority of the EMU an observer status in the IMF Board. The details of this will have to be worked out in the coming months.

On data and information provision we have the impression that there is already a fairly satisfactory data exchange going on and we expect that the envisaged further formal arrangements on data exchange with the ECB and EUROSTAT will not raise substantial problems. Also we have no objections to further extend the exchange of documents between the Fund and EC institutions. The Fund should provide the ECB with all relevant country documents as well as other relevant papers related to the international monetary system, especially the WEO and International Capital Markets report.

Now to the staff paper on the Fund's operational budget—here we agree with the staff that any change with respect to the governing principles for the selection of currencies should be effected without undue haste, allowing for an appropriate transition period.

Following the decision as to which IMF members are included on the transfer-side of the operational budget, the relevant shares for each country, also for EMU-countries, should be calculated on the basis of their respective quota-share. Therefore, like Messrs Kiekens and Prader we prefer and support Option 4. This option has the important advantage that it underlines and thus strengthens the role of quotas as the central determinant for members' rights and obligations in the Fund while increasing the transparency and comparability in the operational budget.

As to the Main Legal Issues paper I have little to add to what has already been said by Messrs. Kiekens and Prader. I believe that this paper is a very useful starting point for our further deliberations on these legal issues and that it has provided a lot of food for thought for our national legal experts as well as for the legal department of the ECB. It appears advisable to set some priorities in this field according to the importance respectively urgency of some of these issues.

We have the impression though that a bit less legalistic and more pragmatic approach to the issues discussed—as exercised by the Fund on other occasions—would have helped our search for common ground. But I understand and respect the motives of our Legal Department in this venture. After all, Mr. Gianviti and his colleagues are particularly called to defend the principles of the Fund's Articles of Agreement , to make us aware of any inconsistencies between the Fund's Articles and the rights and obligations of members that are EMU participants and to help us find appropriate solutions for the various complex issues raised by the creation of the EMU and the introduction of the euro as the common currency of the EMU participants.

Ms. Lissakers noted that Mr. Donecker had agreed that the advent of EMU presented the need to reconcile the rights and obligations of EMU members under the Fund's country-oriented Articles of Agreement with the economic realities and logic of a monetary union. With regard to surveillance, however, his response to the need seemed to be a preference for the status quo. The core of the Fund's surveillance activity concerned monetary and exchange rate policies, which would be, as of January 1999, in the hands of the ECB and would be conducted on an EMU-wide basis. Therefore, it would seem necessary to adjust the Article IV consultation process to take account of the new reality, which should include some form of regional surveillance over the monetary and exchange rate policies of EMU members; simply including a subchapter in every individual EMU member Article IV report did not address the issue appropriately.

Mr. Donecker pointed out that, as the staff report stated, the difference between the two approaches proposed by the staff would not differ substantially in the end. His preference would not be for a separate, small section in each EMU member Article IV consultation report on the views and policies of EMU, but a comprehensive discussion on euro-area-wide policies and a follow-up staff report issued for the information of Directors. At the conclusion of the comprehensive discussion on euro-area-wide policies, a PIN could be issued. Therefore, there would be ample opportunity for Directors to voice their opinions and discuss the issues that are of relevance.

Mr. Kiekens noted that Mr. Donecker had recognized that there was little substantive difference between the two proposed options. However, the first option was presented as an informal discussion, while the second option was considered as a more formal Article IV consultation. It was important to point out that, over the core areas of the Fund's surveillance, the Fund could not engage solely in informal discussions. Indeed, it would likely be inconsistent with the Fund's mandate to conduct firm surveillance over external policies and exchange rate policies. In that context, he asked the General Counsel whether it would be acceptable for the Fund not to conduct a formal Article IV consultation with the ECB.

Ms. Lissakers said that she agreed with Mr. Kiekens. She noted that the obligation ran both ways, and that one of the problems with Mr. Donecker's approach was that such informality suggested that there was no obligation on the part of the EMU to accept collectively firm surveillance by the Fund.

Mr. Donecker clarified that he would agree that there existed an obligation on the part of EMU members to fulfil all the obligations under the Articles of Agreement with regard to surveillance. However, it was important to recall that the membership of the Fund was composed essentially of member countries. Therefore, there did not seem to be any problems associated with an informal discussion between the Fund and the ECB, and he would welcome the participation of an ECB representative in the Fund's discussions on EMU issues.

The General Counsel stated that the principles involved in the matter were rather straightforward, but that the implementation might involve some complications. The first principle was that Article IV consultations, which were mandatory for the member countries, created a relationship between the member countries and the Fund. The second principle was that the European Central Bank was not a member country and therefore was not subject to an obligation to consult with the Fund. The third principle was that, since the monetary policies and exchange rate policies of the members of EMU would be in fact the responsibility of the European Central Bank, it was an obligation for the member countries to ensure that, in implementing and carrying out its mandate under Article IV, the Fund was able to engage in discussions with the European Central Bank as part of its consultation with member countries.

Mr. Kiekens considered that the General Counsel had advised Directors to accept the second option proposed by the staff, which was a common Article IV consultation with the member states in respect to the common policies under EMU.

Mr. Milleron made the following statement:

> I will try to be brief, because we have a very useful and clear reference with the preliminary statement that was presented by Mr. Prader and Mr. Kiekens.
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> I think that most of the issues that are before us today are, finally, related to the same basic problem; I mean the problem is maintaining a member state approach taking into account the euro as a whole.
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> Among all of those issues, some operational matters need to be addressed before the first of January 1999, namely the valuation of the SDR and the allocation of currencies among EMU members in the operational

budget. I may say that in all of these aspects, I support my colleagues' finding; Mr. Kiekens and Mr. Prader did an excellent job.

The other issue of major importance is surveillance. This is a process for which we need some general principles and a sufficient degree of flexibility when we have to go to the modalities. Indeed, the Fund will adapt its surveillance to a new institutional framework, and inevitably the surveillance over the euro area is going to evolve along with the EMU process itself.

However, we should have a clear starting point, and there are some principles that we should agree upon. In this regard, I fully share the general approach to surveillance favored by the staff and supported by Mr. Kiekens and Mr. Prader. Let me just mention two specific points.

First, it is of utmost importance that our institutions enlarge their current practice of including more actively competent institutions and bodies at the euro area level in the surveillance process itself. To a certain extent, the Fund could also help the EMU members to find the relevant approach, in particular as regards the assessment of macroeconomic and other policies from a euro area point of view. As a consequence, I fully support all initiatives aiming at associating the ECOFIN, the Economic and Financial Committee, and the euro-11 Council within the surveillance process.

Second comment or remark: as the staff and others, I have some preference for the formal approach referred to on page 4, as regards surveillance itself. But, in this context, the coverage by surveillance will have to be clearly defined. In particular, it has to be emphasized that, even if there are externalities at the European level, the fiscal and structural aspects have to be addressed without any ambiguity at the country level, and I think that is what my German colleague had in mind. However, this should not preclude the elaboration by the Fund of comparative studies, in the fiscal field in particular.

Finally, on the rights and obligations of EMU members in the Fund, I share the finding of Mr. Kiekens and Mr. Prader. Clearly, we shall have to come back to the issue of access to Fund resources by EMU members. My preliminary view in this matter is that an EMU member request for Fund resources would likely call for the consent of all EMU members and the ECB before doing so, but that is something we have to elaborate a little more.

Mr. Ono made the following statement:

It is clear that an Economic and Monetary Union (EMU), beginning in January of 1999, will affect the functioning of the international finance system. It is important that we discuss how the Fund, . ich mandated maintaining an international finance system, should be concerned with EMU. I welcome this Board meeting discussion.

The staff paper that focuses on legal issues and explains the legal relationship between the Fund and EMU is clear and informative.

First, I would like to comment on Fund surveillance. In this very concise and well-summarized paper, the staff addresses this issue from two points of view: how to conduct the Fund's regional surveillance over the euro area as a whole after establishing EMU; and how to continue the Fund's bilateral surveillance with each EU country. I endorse their approach. Given the importance of the effect of economic developments within the euro area on the global economy after the Monetary Union, it is clear to me that the Fund's regional surveillance of the euro area must be intensified both in its scope and frequency. As for the status of the Fund's discussions with EU institutions, the staff provides us with two options, one being more formal than the other. Although, to tell the truth, I had some trouble recognizing the effective difference between the two options after reading the staff paper, given the importance of surveillance of the euro area, my preference would be to ask the staff to follow the more formal framework

As for reporting to the Board, taking the prominent presence of the euro economy in the world into account, semi-annual reporting followed by a Board discussion seems desirable. Since it will be especially difficult to forecast the economic impact of EMU on other areas, at least for its first two or three years, I think we had better have intensive and frequent Board discussions on this subject during that time period.

Regarding the transparency issue, the need to enhance the transparency of the Fund's regional surveillance is as important as that of any standard Article IV consultation discussion. This chair, therefore, can accept option 3; that is to adopt a general decision applied to all regional surveillance.

The Fund's bilateral surveillance of individual members of the euro area can remain an integral part of Fund surveillance. I support the staff's instructions to continue this important activity. Having said that, it is evident that policy discussions on monetary and exchange rate policy, with some others possibly being added, will be covered mainly by regional surveillance activities. With the understanding that the Fund's resources are limited, I would like to ask management to take appropriate resources reallocation between regional and bilateral surveillance activities in order to make them effectively compliment each other.

The next point, regarding the representation of the EU Institutes in Executive Board meetings, both in regional surveillance of the euro area, and on Article IV consultation discussions of EMU countries, especially ECB, we would agree to allowing the representative of the Institutes to attend Board meetings on an observer basis in order to ensure efficient discussions. We should give them the right to speak in Board meetings on the same level as other observers, such as those from the World Bank. I think that giving observer status to ECB is critical in order to maintain efficient Fund surveillance, and to enhance transparency of the policy conducted by ECB.

To put an end to this surveillance issue, as mentioned in the last part of the staff paper, it is important that the Fund collect the necessary data covering the entire euro area In this context, establishing a system by which the

EU Institutes provide the Fund with useful information on the region is extremely important.

With regard to definition of "reserves" in EMU, the staff paper explained the issue relating to the use of Fund resources and the Fund's operational budget. The paper, however, did not mention this issue in relation to SDDS detail. I would appreciate it if the staff could explain the basic function of SDDS, such as what kind of data would be required for EMU countries to clear SDDS standards that are (have been) adopted by other countries. In any event, the SDDS requirement for EMU countries should be consistent with those applied to other countries.

The staff pointed out the issues to be addressed after EMU starts, issues caused mainly by the difficulty in defining reserves and balance of payments, which are described in the staff paper regarding the Fund's operational budget. I hope this issue will be addressed by integrating a clear definition through EMU development. We broadly agree with the staff's view on use of Fund resources. On the issue of allocations of currencies for transfers under the Fund's operational budget, we prefer the fourth option. This option would respond to the suggestion by some chairs to equalize burden sharing and meet the basic principle of the Fund's quota basis.

Mr. Grilli made the following statement:

It is quite clear that the inception of the European Monetary Union poses several challenges for both participants, the pre-participant countries and the international community at large, including this institution and this Board. But it is also quite clear that, as the Managing Director has noted in his speech at the conference on EMU that we had last year, EMU is an essential building block in Europe's growing political unity.

EMU is essentially conducive as a project to monetary stability and, as such, very much in tune with the broad goals of the Fund. There is really a constructive, inherent compatibility between EMU and stability as sought by the IMF. We should keep this in mind, because I think that it is the nature of things that largely determines outcomes and that the formalities, the procedures, can be worked out as long as this basic compatibility exists.

Monetary Europe is, however, neither perfect nor a complete construction. That is in the nature of things. It is also a sui generis construction. It is an attempt to have monetary integration ahead of fiscal integration. As such, it poses peculiar problems to our institution. But these are evolutionary problems and they are hopefully problems that will not change the desired ultimate outcome.

We have to bear in mind this when we try to address the institutional and operational issues that concern the relationship between the IMF and its EMU members. In this latter group of countries, the well-established paradigm of one country, one currency will soon be replaced by the other 11 countries, 1 currency paradigm. Monetary and exchange rate policies will no longer be under the control of the participant countries but will be exercised by the relevant European institutional bodies, where other policies, and especially fiscal policies, will remain in the realm of national governments. On the contrary, the IMF remains and will remain a country-based institution, I believe; in other words, the paradigm of one country, one member will continue to be generally valid.

The two, although different, do not seem to be incompatible; in fact, I think that they are not incompatible. However, they pose some questions; they pose some challenges over adaptation, mutual adaptation. These challenges need to be met and they need to be met in the spirit that I have tried to sketch out, and with pragmatism, with flexibility, and in some cases maybe with some innovations.

I think that I would not be as innovative as Ms. Lissakers and Mr. Newman, who suggested to consider the opportunity of a proper amendment to the Articles of Agreement, if not now in the near future. But I believe that most of the issues even in their statement can be dealt with in the context of the present Articles, but here we will have to wait and see. If it will be necessary to change, we should change, but we should change after we have gained some experience. I tend to agree with Mr. Cippà that some of the questions that have been raised have probably a rather limited practical relevance for the activity of the Fund, although they may be legally very complex.

In approaching the relationship between the Fund and the EMU members and their common institutions, the documents that the staff has provided seem at some point a bit asymmetric in the approach that they propose, broad approach. In dealing with the technical and operational issues, such as the use of euro in the operational budget and the SDR valuation, the staff applies a great deal of due caution.

In the case of surveillance, there remains perhaps the most sensitive issue. The staff becomes a little more activist and supportive of a more formal approach and perhaps also of a more active approach than is needed. I am not fully convinced yet that an Article IV consultation on monetary matters is necessarily the best thing to start with. I have already voiced the need for strengthening current surveillance activity by complementing the bilateral and the multilateral exercises with a broader and deeper policy analysis at the regional level.

I believe I was the first one that mentioned in this Board this need three years ago, and I incurred the wrath of both Mr. Mirakhor and Mr. Evans. It seemed to me at the time a fairly obvious point that we would have to go in that direction. But I think that in getting there, we have to learn a few things. We have to adapt to each other. For this reason, we ought to be a little more cautious.

I have the impression that the time is still not right for having collective, full-fledged, formal Article IV consultations on EMU issues, but this is not a very critical point at this stage. I think the important thing is to have sufficient consultations, sufficient surveillance, and to look at the substance of things. Why? First, Article IV consultations are, as my colleagues have already mentioned, only with IMF members, and are we going to have consultations with EU institutions under a somewhat misleading heading of joint Article IV consultation with the member countries. Second, not all the EU countries are EMU members. One could argue that in the new institutional settings, the pre-EMU countries may find a much stronger constraint and will find a much stronger constraint in setting their economic policies than before, than they did during the ERM. The question arises, however, whether or not to include them in this exercise of regional surveillance. It might be correct from an economic point of view, but it has very weak legal basis. Third, there is the problem of what should be the appropriate authorities to consult with. Here, we will have to sort things out at our level. The whole point is that the rein is not a smooth rein. There are some difficulties. Certainly, there is the necessity to learn. I think that we ought to be pragmatic. I think that surveillance is a process which is valuable for what it does. In a way, when I think of surveillance, I think of cats that catch mice. It is not really very important if the cat is black or white as long as it catches the mouse, and I think that the process is that type. I would focus on the substance of what we want to do more than on the framework, on the formal framework that we choose.

I do not think that being informal diminishes in any way or demonstrates in any way that EMU members have a limited willingness to discharge their obligations. I think that we have an obligation, as the General Counsel said very clearly this morning and he wrote in the paper, I believe that we have the obligation as member countries to make sure that Article IV consultations are, in substance, conducted fully and completely, so that responsibility we will have to discharge. But I would argue that there is merit in consolidating present practices and ensure that the precise terms of the procedures emerge from experience rather than from analogy in the transition period. This will be only for a certain period of time, a transition period during which both the Fund and EMU members learn and adapt to each other.

On other issues concerning the surveillance process, we agree with Mr. Kiekens and Mr. Prader. In particular, we would like to support the proposal to grant observer status to the ECB in the Fund according to modalities that this Board will deem to be suitable.

On the operational budget, we would also prefer option 4 for its transparency. I would like just to ask the staff how long should it be, in its view, the transition period to a full-fledged quota-based operational budget. We do not think that it should be too long.

In the case of the EMU members, I agree with the staff view that inclusion in, or exclusion from, the operational budget should be common to all members of the currency union, depending on whether the euro itself is deemed sufficiently strong. In doing this, the two fundamental criteria, strong balance of payments positions and reserve positions, should be maintained, although adapted to the new institutional setting. The assessments of the balance of payments should be made for the EMU area as a whole.

The level of external reserves should include also those of the NCBs. Although some restrictions apply on the use of these assets by the NCBs, I agree with Mr. Kiekens and Mr. Prader's view that those reserves should be considered as belonging to the general pool of reserves. In fact, it should be recognized that among the EMU participant countries, it was established a system of central banks in which the ECB has a central role but the NCBs do not completely disappear. Therefore, when possible, we should refer to the system as a whole.

Mr. Daïri made the following statement:

We thank the staff for a very useful set of papers and welcome this discussion. The advent of the euro will have important implications for Fund surveillance. While the single monetary policy under the responsibility of the European Central Bank and the Stabilization and Growth Pact will undoubtedly affect the way member countries conduct their domestic policies, with the euro institutions exercising some of Fund traditional surveillance activities, a new important dimension will be added to the responsibilities of the Fund. In view of the role of the common currency in the international monetary system, which will very likely exceed the sum of its former national currency components, it will be essential that the Fund refocus its surveillance on the regional aspect. Moreover, domestic policies of EMU members will need to be more closely monitored since they may affect the way the common monetary and exchange rate policies are carried out even if the independence of the latter policies is forcefully reaffirmed.

To carry out its mandate, the Fund needs to rely on the strong legal basis provided by the Articles of Agreement. In this context, it is important to ensure that discussions with EU institutions are an integral and important part of the surveillance process with EU members and not a mere addendum to bilateral discussions with members. We therefore strongly support the more formal approach advocated by the staff as regards the status of Fund discussion. Only such an approach would ensure that domestic policies are indeed coherent with the common monetary and exchange rate policy. Discussions with the EU institutions should be included as a major component of the staff report on consultations with individual members.

We agree with the staff that, in addition to monetary and exchange issues, discussions with EU institutions will need to cover important topics, such as the overall fiscal position in the euro area, trade and competition policies, labor market developments and reforms, and the soundness of the euro-wide financial system. To ensure continuity and relevance of the surveillance process, as well as coherence with bilateral discussions, it is necessary to increase the frequency of discussions with EU institutions, as suggested by the staff. It is also important that the conclusions of bilateral discussions with members be shared with the regional institutions.

While we believe that discussions with the regional institutions need to be carried out twice a year, updated if necessary, and reported to the Board for discussion, we do not support the proposal that these discussions be concluded separate from the bilateral discussions with members. We are of the view that only bilateral consultations carried out on the basis of both the discussions with members and the regional discussions should be concluded. The PINs should also be issued for individual members and not for the regional surveillance. This is more in line with the fundamental principle that the surveillance is on members' exchange rate policies wherever these policies are formulated or implemented. The proposal that the consultations with the EU institutions be concluded separately would require that regional institutions become members of the Fund, which is not the case. Some clarification of the issue from the Legal Counsel is welcome.

We agree with the proposed content of bilateral surveillance discussions and the redirecting of priorities and staff resources. We also believe that at this stage bilateral discussions should remain under the annual cycle.

As regards the representation of the EU institutions' views during Board discussions, we have some reservation regarding the proposed observer status for the ECB. Attendance by World Bank or WTO representatives is limited to areas of common interest whereas the ECB may be interested in a much wider range of issues. There may also be areas where ECB views could differ from those of its members, which may create some confusion since the ECB is formally in charge of major policy matters of the membership. We would favor a system by which euro institutions would be allowed to express their views through one of the Executive Directors from the area. It is also important to avoid multiplication of observers, the status of which may be blurred over time. Another possibility would be that EU institutions circulate a statement prior to bilateral discussions with members. This being said, we have no problem joining a consensus, provided that the status of observers is clearly defined.

On issues relating to data and information provision, we do not see why less detailed national monetary statistics will be produced, unless the Board decides that such detail is not useful. We understand that intra-euro trade and financial transactions would become less relevant, but we wonder whether data provided by non-euro countries would still need to be detailed by individual euro countries, or should be provided for the euro area as a whole. We agree with the staff on the need to provide the Fund with euro-wide data since the regional surveillance would be an integral part of Fund surveillance on members. We agree with the proposal to provide the EU institutions with Fund documents, provided that they are ready to observe the guidelines on confidentiality with respect to documents relating to non-EMU members.

On use of Fund resources and use of the euro in the Fund's operational budget, we agree with the staff that, as a matter of principle, the EMU members should be eligible for use of Fund resources in case of balance of payments needs. However, we are not yet satisfied with staff proposals regarding the determination of such need. We would support the view that this issue be reconsidered at a later stage. Moreover, as indicated by Ms. Lissakers and Mr. Newman, the issue of conditionality for use of Fund resources in the case of euro members needs to be addressed. We concur with the staff proposal that inclusion in or exclusion from the operational budget should be common to all members of EMU. We suggest that the issue of the exclusion of a member on the basis of balance of payments need be discussed at a later stage once the basis for determination of such a need is further clarified.

As regards allocation of currencies for the euro area, we support the third alternative, which is to align it with the procedure used for the U.S. dollar. This is more in line with the characteristics of the euro as a potentially major reserve currency. We do not feel that this approach would raise questions about uniformity of treatment since there is already an exception to this principle as regards the U.S. dollar. The resulting allocation would also be in line with the relative importance of the euro in terms of quota shares.

Mr. Taylor made the following statement:

It is clear that the rights and obligations of individual members under the Articles and our existing procedures, practices, and habits of mind all sit uncomfortably with the logic of the economic integration under the European Union that has already occurred and which will grow over time. The areas that remain principally relevant to surveillance at the bilateral level mainly fiscal and structural, but as is clear from the reference in the annex of the relevant staff paper, the reference to the Stability and Growth Pact scope for discretionary fiscal policy is already somewhat constrained. And even the shape of budgets is somewhat constrained to the extent that there is a degree of harmonization in taxation, in particular, some forms of taxation.

This clearly poses very important questions about the effectiveness and efficiency of our procedures, but it raises a question even of the continuing relevance of the surveillance function, as well as, of course, as Mr. Ono reminded us, questions of the disposition of our resources. Mr. Donecker and others have said that this is a moving target in effect, and we need to be willing to experiment and adapt over time. So, for example, my answer to the second issue for discussion—do Directors have a preference between annual and semiannual papers—would be, we should have semiannual papers in the first 12 months and then move to an annual approach unless circumstances suggest otherwise. I am particularly concerned with the possibility that those with direct responsibility may not have the opportunity of presenting positions directly. This seems to be particularly important in the case of the ECB, where I would consider it essential that the regional authority be at the table for regional surveillance, and also, I think, for discussions on capital markets, at least. So, the title of observer is fine, but I would expect to hear directly from the observer and in those areas of primary competence. Like Mr. Grilli said, formal and informal approaches may be the distinction between black and white cats, but we need the mouse in the room and we need the mouse at the table.

On the matter of other institutions, like Ms. Lissakers I would agree with the staff that regional surveillance needs to extend quite widely across relevant institutions, and for this purpose the staff has to consult with the wide range of individuals and institutions at the regional as well as national level. It remains to be seen, I think, whether the reactions of other relevant European Union institutions or the ECB can adequately be communicated to the Board through a European Union Executive Director. I would be willing to try that approach and see how it goes.

Turning to the future of bilateral surveillance, this is where logic suggests that we should be able to find some streamlining of procedures and saving of resources which, however, is not so easy to prescribe as a practical matter. I would be willing to move now to a less than annual arrangement for formal consultations, but if that is not acceptable at this stage, then I would be looking for a shorter, less ambitious paper, innovation such as tighter grouping of members, possibly under umbrella papers that have been tried on one or two instances elsewhere in the world, and serious consideration of lapse of time procedures, where that might be possible.

On PINs and data and information provision, I would agree broadly with the approach in the paper.

On the operational budget, I agree with others that the quota-based approach for all is the most appropriate solution. As to whether there is a need for transitional period or not, I would not have thought so, but I can join any consensus on that.

Mr Harinowo made the following statement:

At the outset we would like to thank the staff for preparing interesting and informative papers for this discussion. This discussion is undertaken at the time when the world is facing a great uncertainty due to developments taking place in various parts of the world. Within that kind of environment, what might be just a minor procedural or legal matter in the ordinary circumstances, could become factors that may affect the confidence of the market. Against this background, the discussion of many operational aspects related to EMU should carefully weigh on the latest global developments. Any deviation from the current arrangements between the Fund and the EMU members, especially if the changes are significant, could lead to unnecessary distractions for the Fund, EMU members, as well as other countries. Therefore, on discussing this issue this chair would like to emphasize the need for continuing the present arrangements between the Fund and the EMU (members) as much as possible and leave any necessary modifications at the latter stage when the circumstances are more favorable. However, our chair certainly supports any modification that could strengthen the relationship without unduly burdening the parties involved.

On the issues of Surveillance (SM/98/215) particularly on the status of including the EMU as part of the Article IV consultation process with the EMU members, this chair can go along with the notion that a more formal surveillance of the entire region be carried out. This view is primarily based to the fact that formalizing the surveillance process could enhance the current practice of consulting the EMU Institutions during the consultation with the EMU members individually. Thus formalizing this process will enhance the credibility of the Fund Surveillance.

At the same time, the Article IV consultations with individual member countries remain an integral part of Fund surveillance with members but can be done on a somewhat more systematic way. In this context, we see merit on the staff's proposal to cluster consultations with member countries into two groups while undertaking semi annual consultations with the EMU institutions. This method could enhance the surveillance process by enriching the discussions with the EMU institutions as well as the discussions with the member countries because of the interaction resulted by simultaneous consultations with both parties.

On the timing of the consultations, arrangement can be made to set the consultations with each cluster of the members that can be discussed in the Board prior to the spring Interim Committee meeting and the fall meeting so as to provide a basis for a more up to date information on the region as a whole with a more accurate information at least on half of them. With this arrangement, the preparation of the WEO can also be facilitated by the information made available during the consultations.

On the subject of granting observer status to the ECB at the Executive Board and the appropriate means of representing the views of other relevant EU Institutions at board meetings, this chair needs the staff's clarification on the consistency of such proposed decision to the treatment given to other regional organizations of similar nature e.g. WAEMU. However, we could go along with other directors if the Board is considering to grant the status, given the importance of these institutions on the monetary and exchange rate policies of the EMU.

On the use of the euro in the Fund's operational budget (EBS/98/132), this chair is of the opinion that the current arrangement between the Fund and euro members need to be continued at least during the transition period. This view is primarily based on the fragility of global developments as well as the present level of the Fund liquidity. Any necessary modifications that will reduce the capacity of the Fund should not be considered at this time and need to be reconsidered until the environment is more favorable.

On the medium and longer term, however, this chair is of the view that the existence of euro as a reserve currency should be seriously considered. Thus we are in broad agreement with the proposal by the staff as well as further elaboration by Ms. Lissakers and Mr. Newman. Since euro will become a freely usable currency, EMU members will be able to meet the IMF obligations without experiencing exchange reserve losses. Thus the amount of external assets held by the members and the ECB is less relevant in assessing the capacity of the EMU members.

Since we are not entirely clear on the future outlook of the world economy, therefore we see merit on applying a transitional basis for the method of allocating currencies for the operational budget as mentioned above. This method can then be revisited along side with the consideration of the valuation of SDR.

Mr. Al-Turki made the following statement:

I thank the staff for this important set of papers. The issues addressed are, indeed, complex and have far-reaching practical implications for the Fund and its members. As all three papers underscore, the transfer of monetary powers by some European Union countries under the EMU has no impact on these countries' rights and obligations as members of the Fund. Therefore, the issue before us is how the EMU member will continue to exercise their rights and fulfill their obligations in the new environment. It follows that modalities in that regard are for the European Union members to propose with the Fund taking up any concern that may arise as to the adequacy of the proposals. Nonetheless, given the complexity of the issues, and the systemic importance of the EMU, I welcome the Fund's effort to help set out the options. Clearly, any adaptation of the Fund practices in view of the EMU could set a precedent for treatment of members that may agree to a comparable transfer of powers to a collective entity like the might.

Regarding the status of the Fund's surveillance of EMU, the best option is to make adaptation as needed of the existing arrangement for discussions with European Union institutions to complement the bilateral discussions. Here, I support the proposed formal inclusion of these discussions as part of the Article IV process. The joint Article IV consultation format has the merit of giving the staff the necessary flexibility with due regard to the requirement of the Fund consult with individual member countries, and not with members and institutions without whether national or supernational. The modalities can be revisited later for appropriate changes with the evolution of the EMU and increase in the Fund's regional surveillance experience.

Regarding coverage and counterparts, the watchword again is adaptation as needed of present practices regarding European Union and institutions with the lead given to the European Union members to suggest changes. Indeed, the issues cannot be fully foreseen at this early stage of the European Union early evolution. Here, we agree with the staff on the importance of regular contact with EMU and institutions. I broadly agree with the suggested reporting to the Board in the form of a staff paper on the annual visit to European Union and institutions. This could be supplemented by additional submission of informal reports as needed. I have no difficulty with the suggested ways to promote transparency with respect to the Fund's regional surveillance of EMU, including issuance of public information nose.

Regarding representation at Fund Board discussion, a distinction should be drawn between multilateral organizations such as the World Bank and the WTO and on the one hand, and regional entities, such as the EMU, on the other. Here, I agree with Ms. Lissakers and Mr. Newman on according observer status to European Central Bank for relevant Board meetings. Here, like Mr. Harinowo, I would appreciate the staff's views on the implication of such a move for potential requests for similar representation of other regional entities.

On the data transfer issue, I agree that the staff should make appropriate arrangement with European Union institutions for the relevant transfer of data on a regular and timely basis. The important point here is to stay within the parameter of members' data obligations under the Articles of Agreement. Finally, regarding implication for use of Fund resources and use of euros in the Fund's operational budget, it is premature to form any definitive view of the issues at this early stage in EMU evolution. Therefore, for the time being, proceeding on the basis of preserving the key features of current allocation system along the staff's suggested alternative two is the practical option. Such a basing of an indication of currency on the resource retained by national central banks can be revisited at a later date for appropriate change in light of gathered experience and the actual evolution of the EMU.

The Acting Chairman asked the General Counsel to respond to the question of what the implications would be of the new arrangement with the ECB for other regional surveillance exercises.

The General Counsel responded that it was difficult to talk of any precedent being established, given the different status, responsibilities, functions, and structure of various international organizations in monetary unions. Mention had been made of the West African Economic and Monetary Union, which had existed for many years. To his knowledge, there had not been a request from its central bank to become an observer in the Fund. If such a request were made, it would have to be assessed on its merits. While the establishment of observer status for the ECB would create a precedent in the sense that it would represent the first such arrangement, it would not oblige the Fund to extend observer status to other organizations; any request would be considered on its own merits.

Mr. Daïri thanked the General Counsel for the clarification, but he reiterated his view that it was necessary to establish clear criteria for the granting of observer status before the ECB case was considered.

Mr. Elhage made the following statement:

I will briefly address the issues identified for discussion. We concur with the more formal approach to Fund discussions with EU institutions. As the staff notes, this has the advantage of clearly recognizing the obligations of EMU members to consult with the Fund on the policy responsibilities that will be shifted from the national authorities to the relevant EU institutions.

We also agree that at least in the initial stage, of discussion with the EU institutions would take place twice a year. We can reassess this frequency after some experience is gained. Thus we favor having an annual visit complemented by a follow up staff visit. Clearly it would be helpful for such visits to coincide with WEO preparations. Papers should be presented to the Board after each visit.

On the coverage of consultations, we see no problem in the proposed focus of bilateral consultations on fiscal, financial and structural policies. Discussions on monetary policy should be centered on the impact of the stance of monetary policy pursued by the ECB on the national economy, and other issues pertaining to the implementation of monetary policy through the national central banks. We agree that more attention should be focused on structural reforms, particularly labor sector reform, and financial sector developments.

We have no objection to granting the ECB observer status at the Board when discussions of consultations with EMU members take place. We can also agree to any modality to be decided upon by the EU members for the communication of the reaction of other relevant EU institutions to staff papers.

We agree that the staff should make arrangements with the relevant EU institutions on the transfer of data on a regular and timely basis.

On EMU and the Fund—use of Fund resources—we appreciate and go along with the staff's proposal that whatever changes are finally agreed to, there should be a transitional period for implementation. It seems to us that the first option, namely to maintain the present system unchanged should be ruled out since it would result in an unjustified reduction in the contribution of the euro-area countries to the financing of the Fund.

A modification of the definition of 'reserves' to allow the allocation for euro-area members to be based on the external assets that will remain with the NCB's after the transfer of reserves to the ECB—may or may not be too problematic. Perhaps the staff could elaborate on the conceptual and practical issues that this would raise.

We have an open mind on options 3 and 4—but we have a preference for the third option, namely to align the allocation method for euros with the current method used for U.S. dollars while allocating contributions within the group on the basis of shares in the ECB. We believe we need a more thorough discussion before coming to a decision.

Ms. Wang made the following statement:

First, I would like to thank the staff for a set of concise and clear papers on the legal and operational issues concerning the relationship between EMU and the Fund, and welcome this opportunity to discuss these issues.

In regard to the main legal issues relating to rights and obligations of EMU members in the Fund, first, according to its Articles of Agreement, the Fund is a country-based institution, and therefore, the transfer of monetary power by members of the euro area to EMU institutions will not affect their relationship with the Fund. However, the implementation of the individual rights and obligations of members may be affected by such transfer, and according to the staff, it will be the responsibility of each member of the euro area to ensure that the institutions of the Community in charge of monetary and exchange rate policy live up to member's commitments under the Fund's

Articles. I have no objection to this statement, but just one question: is there any mechanism or arrangement within the EMU to ensure that individual members have the capacity to do so?

Second, on balance of payment data, we agree with the staff that Fund members of the euro area will need to continue to compile and report individually to the Fund on their balance of payment data.

On EMU and Fund surveillance, with the transfer of monetary and exchange rate policies from euro member states to EU institutions, if my understanding is correct, the conduct of euro area monetary and exchange rate policies will be outside the direct supervision of the Fund, because the Fund's Articles of Agreement are not applied to EMU, although they continue to apply to euro area members. However, given the mandate of the Fund to oversee the international monetary system, the envisaged impact of the economic developments within the euro area, and that in other countries, and the international monetary system more broadly, it is important for the Fund to consider the systemic aspects of the euro area in its surveillance. At this stage, it is premature to consider the application of the Articles of Agreement to any union, but we fully agree with the staff that discussions with EU institutions should be intensified to fulfill the Fund's surveillance mandate. In this context, we support the staff's proposal to give a formal status of the discussion with the ECB and include such discussion as part of the Article IV consultation process with EMU members. I agree with Mr. Grilli that what is important here is the substance of the discussion, but with the formal modality, I believe it will make it clearer to the cat that you have the responsibility to catch the mouse. Similar status of the discussions with other EU institutions is desirable; however, taking into consideration the practical difficulties, it might be more pragmatic to maintain the current informal nature of these discussions.

As for the frequency of such discussions, we share the view of Mr. Kiekens and Mr. Prader. Since most euro-area members release PINs, we believe that a PIN applying to regional surveillance of EMU should also be published, of course, on the condition that the concerned 11 members agree.

As for the Article IV consultation with individual euro-area members, it should remain an important part of the Fund's surveillance. We agree with the staff that the priorities of the bilateral discussions should focus on issues such as structural reforms and fiscal developments. However, it seems that the impact of regional policy on individual countries and vice versa should not be neglected by the regional or bilateral consultations.

As for the cycle of Article IV consultations with individual euro-area members, we believe the 12-month cycle is appropriate for most of the EU members, at least for the first few years of the EMU.

Turning to the effective representation of the relevant EU institutions' views in Executive Board discussions, we agree that such representation is important in enhancing the Fund's surveillance over the euro area, and have no objection to granting observer status to the ECB at the Board for selected

Board discussions However, taking into consideration factors such as the size of the Board, caution should be exercised when considering granting similar status to other relevant EU institutions, especially given that at the current stage, these institutions have no power regarding individual members' domestic policies, such as fiscal and labor market policies. So, is it possible for the ECB observer or one of the EU chairs to represent the views of other relevant EU institutions at Board meetings?

Finally, on data and information provision, we agree that the Fund should make arrangements, particularly with the ECB and EUROSTAT, on the transfer of a set of data on a regular and timely basis.

Turning to the use of Fund resources and use of euros in the Fund's operational budget, first, each member has the right to use the Fund's resources when it represents a balance of payment need. It is true that with the introduction of the euro and the transfer of monetary authority from the national central bank to the ECB, it is very difficult to apply the tradition criteria—the level of, or developments in, reserves, or the balance of payments position—in assessing such a need. With the talent of the staff, we are very pleased to note that such difficulties will not affect the exercise of a euro member's right in using the Fund's resources. We agree with the staff that first, the balance of payment need should be assessed for the euro as a whole, using the current criteria, and second, since it is quite possible that the situation in an individual euro member country might be different from that of the euro area as a whole, it is necessary to develop a new set of indicators to assess the situation of individual countries, which include, among others, the interest rate spreads in the presence of market segmentation, and the need for exceptional financing. We believe such a new set of indicators will be improved with the accumulation of experience under the new regime.

Second, on the use of euros in the Fund's operational budget, considering the difficulties in assessing the country-specific balance of payments strength, it seems reasonable that inclusion in, or exclusion from, the operational budget should be common to all members of the currency union. The staff also suggests that in the case of a euro member running into balance of payments problems, the Fund would not use its holdings of that member's currency for transfers in the operational budget. I guess what is behind the staff's thinking when making this proposal might be that the euro will always be included in the operational budget. Otherwise, I find the treatment here somewhat asymmetric. If the Fund can recognize the balance of payment needs of individual euro members by developing a new set of indicators, I believe similar measures should also be found for assessing balance of payment strength. Participation in the operational budget is the obligation of individual members, and the development of other members should not affect the fulfilment of this obligation by any member. Therefore, we believe that external strength should also be assessed at the individual member country, even if the assessment were to start with an evaluation of the balance of payments and reserve strength for the union, and developments in the exchange markets for the euro. We encourage the staff to develop a new set of indicators for such purpose.

Third, on the allocation of currencies under the operational budget, we would like to grant our strong endorsement for the fourth alternative, which is to base the allocation of the transfer of the operational budget for all countries on their share in the quotas of the members judged strong enough for inclusion in the operational budget. This is not because we have read from Table 1 of the staff report that transfer of the 11 EMU members will increase substantially under this method compared with the present one, rather that we believe this method is much more transparent, reasonable, and equitable, given the unique nature of the Fund as a quota-based institution. The fourth alternative is also the only one that is in line with the principle of uniformity of treatment for all Fund members.

As for the transitional period, we have no objection, but as Mr. Grilli, we do not think it should be too long.

We support the proposed decision Numbers 2, 3, and 4 concerning the valuation and interest rate basket of the SDR. As for the timing of the next revision of the valuation basket of SDR, we can go along with the view of Ms. Lissakers and Mr. Newman.

Mr. Askari-Rankouhi made the following statement:

On the surveillance issue, we agree that there should be annual staff assessments and both discussions of the euro area. However, it seems to us that the staff proposals run the risk of devoting more resources to the surveillance of the euro area than is currently the case for individual euro countries. In contrast, we believe that the adoption of the common currency and centralization of monetary policy should simplify the surveillance exercise in many respects.

We do not believe that a separate formal Article IV consultation for the euro area is necessary. An annual report by the staff focused primarily on monetary and exchange rate issues to be discussed by the Board would suffice. However, this does not preclude staff visits when necessary, but there is no need to have a Board discussion after each staff visit. as others have stated, the Board will have ample opportunities to discuss euro issues in the context of the WEO, WEMD and capital markets discussions. In summary, we would prefer informal surveillance of the euro area in addition to formal Article IV consultations for individual members.

On the PINs, we believe that given the importance of the euro, it is necessary to issue a PIN after the Board discussion of the euro area issues. The question of who would sign off on the PIN should be resolved among the euro members, but ahead of the Board discussion to prevent delays.

On the status of the ECB and other EU institutions, w have no objection to having an observer from the ECB present when euro area issues are discussed. But, we do not believe it is appropriate for the ECB to circulate statements in advance of the word discussion. Members of the EMU collectively or individually could reflect the views of the ECB and other EU institutions. We also don't think there is a need for observers from other EU institutions.

On the operational budget, given the practical difficulties of measuring balance of payments imbalances and reserves for individual euro area members, we believe that the strength of the external financial position of the euro area should be the basis for the inclusion of the euro in the operational budget.

On the issue of the allocation of currencies used on the transfer side of the budget, we could accept either the third or the fourth alternative, even though the quota-based system would lead to a sharp rice in Canada's share of the operational budget.

Mr. Eyzaguirre made the following statement:

As stated by Mr. Kiekens and Mr. Prader, the adoption by member states of the EC of common policies in the framework of EMU will require the Fund to adjust its surveillance to the shift of responsibilities this entails. While we may run the risk of work duplication, initially it is safer to ensure we will conduct an appropriate surveillance of the new decision-making bodies without paying less attention to the exercise of bilateral surveillance with each country. A further streamlining of the procedures may result through learning by doing.

As others we support the more formal approach, that is to include regional surveillance of EMU directly as part of the Article IV process. However, we would prefer annual papers, as it is the case of other large countries of systemic importance. With respect to coverage, it seems natural to encompass all aspects that follow under EU institutions' responsibilities, i.e. monetary and exchange rate policy as well as trade and competition policies. The fiscal position of the whole Euro area and the structural policies that are critical for the appropriate functioning of the EMU should also be discussed. We also welcome the issuance of a PIN after the Board discussions, with the consent given by all concerned members.

Notwithstanding the importance of the euro area, the bilateral Article IV consultations with individual members should remain a central element of Fund surveillance. We support staff views with regard to the coverage of consultations as outlined in Section III of the paper. Finally we can support extending observer status to the ECB for member states' Article IV consultations and regional surveillance of the euro Area. Other relevant EU institutions' views should be expressed through EU Executive Directors.

On the evaluation of external financial strength for the designation plan and operational budget, I share the staff's view that the inclusion in or exclusion from the operational budget should be based on an assessment of the financial position of the overall union. As it is well described in section IV of the staff paper, international reserves in the usual sense of the term, may not exist at the level of individual members, and the difficulties inherent in capturing intra union payments and capital flows may undermine the reliability of the balance of payments' statistics.

On the allocation of currencies under the operational budget, the staff suggests four different approaches to deal with the issues arising from EMU, including their share in the quotas of the members. As Ms. Lissakers and Mr. Newman, and Mr. Kiekens and Mr. Prader, I found this approach objective, simple and transparent, and that it will maintain over time the Fund's holdings of each member's currency close to the average of Fund holdings of all members and would therefore not raise issues regarding the uniformity of treatment. In the current situation, Fund holdings of nearly half the strong currencies are at or very close to the floor, with a consequent concentration of the Fund's holdings of usable currencies among a relatively small number of countries.

Turning to the third point of our agenda, the main legal issues relating to rights and obligations of EMU members in the Fund, the Legal Department has prepared a comprehensive and interesting document, which clearly explains the main aspects relating to the rights and obligations of EMU members under the Fund's articles. The key points that support the analyses are the fact that the Fund is a country-based institution, and that the transfers of monetary powers by members of the euro area to EMU institutions, will not affect their relationship with the Fund. Also, under the Fund's Articles, the creation of a monetary union with common organs does not create collective rights and obligations to the common organs of the union.

However, on the reserves of the euro-area members of the Fund, there are clearly several issues pending to be solved, in order for the Fund to decide whether and to what extent different assets are to be regarded as national reserves when calculating each euro-area member's reserve position. We would need to readdress these matters when the Governing Council finish adopting proper guidelines, prior to the functioning of the EMU on January 1, 1999.

Mr. Toribio made the following statement:

I will briefly explain the position of my chair in each one of the issues for discussion raised by the staff in the papers.

First, about the formality of discussions with the regional authorities of the European Union, yes, I would be in favor of a more formal approach than the one we have today, but here, I share very much the views of Mr. Grilli on the need to be pragmatic. The important thing is not how formal those discussions are, but how efficient they are and how deep they are in practice. I very much accept the analogy of the cat and the mouse that Mr Grilli proposes on this question

I do not have any preference between having an annual or semiannual paper on the discussion with regional European Union authorities. But, I think that to begin with, semiannual papers would be better, perhaps one paper very formal and the second one being only a follow-up of the first one, being discussed close to the World Economic Outlook in this Board. That would be a very good alternative. Should those discussions end up in a PIN, yes, I think that it is very logical that we publish a PIN on the discussions of this Board, and the PINs related to the European unions should be handled in my opinion as any other, so depending on the acceptance of the Executive Directors involved in that.

Article IV discussions with members of the EMU could in principle, in my opinion, continue being annual in character. We would have time in the future to change to every two years, a consultation every two years. I agree, however with Mr. Taylor on the idea of making those consultations or the paper resulting from those consultations more brief than they are today, since an important part, that part related to monetary policy, would have been discussed already. So that we could pay attention to this point

On the question of the representation of the European central bank, I think the idea of giving the ECB an observer status is the most pragmatic one at this moment since in my opinion it does not preclude any other alternative we may consider in the future, but to begin with this observer status seems to be the most appropriate alternative. I do not object to Mr. Daïri's observation that perhaps the Legal Department could be study with some depth if this means a precedent or what the criteria should be for the future in general, on the appointment of observers at this Board. To begin with, given this status on the European Central Bank seems to be very appropriate.

I do not have any objections for the staff to make arrangements with the ECB and Eurostat on the transfer of data on a regular and timely basis on the contrary, I think it would be a very appropriate.

Finally, with regard to the operational budget, it well known that this chair has been always very much in favor of using the quota as the main criteria for the inclusion of a currency in the operational budget, so we welcome very much the option 4. Frankly, I do not see the need for any transitional period in that, I think the use of quotas, the time for that is long overdue, but if there is going to be a transitional period, I would ask it for it to be as short as possible.

Mr. Lehmussaari made the following statement:

I welcome this opportunity to discuss what I see as a very important set of EMU related issues. Let me start by addressing the topic of the use of the euro in the operational budget. On this point, I can fully support the views of Mr. Kiekens and Mr. Prader presented in their preliminary statement. In particular, on the allocation procedure, we prefer option 4. On this matter, I have only one additional remark to make.

Assessments on balance of payment need and the strength of individual members of the EMU are difficult to make and will require more reliance on partial and supplementary indicators. Since the international reserves can only be measured in a comprehensive way for the euro area as a whole, the inclusion or exclusion from the operational budget should be common to all members of EMU. At this stage it is unclear to me in what kind of circumstances, if any, a single euro-area country can be "excused" from participating in the operational budget. This issue clearly needs further clarification and I look forward to future discussions on this matter.

This leads me to a more general point. The different role of reserves, and definition of reserves for the euro members, further highlights the need to have a second look at this criteria for identifying countries that are sufficiently strong to participate in the operational budget. Furthermore, some of us have stated during earlier discussions on the operational budget, that, in principle, one should introduce a presumption that all members, with reasonable exemptions, would contribute to the budget. Each country's contribution could, in this case, also be based on quotas. Against this background, I look forward very much to the upcoming review of the guidelines regarding the allocation of currencies in the operational budget.

Let me now turn to the next issue, EMU and Fund Surveillance. On this point, I can also, to a large extent, associate myself with the views of Mr. Kiekens and Mr. Prader. I just have a few additional remarks on the outlined issues for discussion.

The first issue is the form of future consultations with the members of the euro area. Here, I believe that, with Fund membership resting on an individual country basis, bilateral surveillance of single country members through Article IV consultations will remain the cornerstone of the Fund's surveillance. I therefore agree that these consultations should be retained at the present frequency for euro members. At the same time, I recognize that the Board will have to broaden its deliberations about individual European countries to include regional surveillance. Like the staff, I believe it is important to keep the regional surveillance process as a separate item on the Board's agenda. On the frequency of these regional discussions, I could imagine that an annual consultation with a following Board discussion would be adequate, but I am also open to the suggestion of Mr. Kiekens and Mr. Prader implying an additional follow-up visit.

Finally, as regards issuing PINs, this would indeed be a new form of communication in a regional context. However, the role of PINs in regional surveillance is an issue which will require some further thinking. For instance, publishing of "euro-PINs" could be a useful step in increasing transparency, but they probably would not have the same "peer pressure" effect in a regional context as with individual countries. Thus, if "euro-PINs" are issued, questions such as ownership and the procedure with respect to editing before publication must be further clarified at the European level.

Mr. Lushin made the following statement:

In regard to EMU and Fund surveillance, regional surveillance of the euro area will be a matter of great importance for the Fund. Therefore, I favor a more formal approach to the surveillance of EMU as a part of the Article IV process, as this would be more consistent with the Fund's mandate. Concerning the frequency of such consultations, I would generally favor having them on an annual basis, which is already an established standard. However, in view of the systemic importance of EMU for the world economy, I think that initially a closer monitoring of its performance by the Fund would be warranted. In this light, bi-annual consultations may be appropriate during the first one or two years of the EMU's existence. Finally, I think that PINs should be issued regularly to reflect the summing up of Board discussions on EMU, subject to the collective consent of all the EMU members.

Bilateral Article IV consultations with the individual EMU countries will remain an integral part of Fund surveillance. I agree with the staff's proposals on the adaptation of the bilateral consultation process so as to concentrate it on fiscal, financial and structural policies.

I agree that the ECB be given observer status at selected Board meetings. As for the ways other relevant EMU institutions can represent their views at Board meetings, I think that we can be flexible with regard to the existing alternatives.

I also agree that necessary arrangements should be made between the Fund and the appropriate EMU bodies for the regular and timely transfer of data.

As regards The Fund's operational budget, I agree with the staff's proposal that inclusion of the euro in the operational budget should be common to all members of EMU and derived from an assessment of the financial strength of the overall union.

With regard to allocation of the euro to the operational budget, my preliminary judgement is in favor of options 3 or 4. The staff's illustrative calculations show that both these approaches would result in the same allocation for euros and U.S. dollars, but differ considerably with respect to the allocation for other currencies. Therefore, the final decision on the allocation scheme, if made between these two options, would require a broad consensus among all the members whose currencies are included in the operational budget.

On the valuation of the SDR and SDR interest rate, I share the staff's view that no changes should be made at this stage to the method of SDR valuation. The simple substitution of the Deutsche mark and the French franc by the euro is an explicit and robust move which ensures the continuity and consistency of the Fund's approach. At the same time, it requires minimum modifications to the existing rules and regulations. The similar country-based approach should be applied to the SDR interest rate basket, given its identity with the SDR valuation basket. Specifically, I favor using national interest rate instruments in the basket.

I agree with the rationale behind the staff's proposal to reset the five-year cycle for the revision of the SDR so as to coincide with the start of EMU. Such a resetting would allow enough time for the assessment of the role of the euro in the international financial system and for the development of the relative importance of currencies. We also agree that an earlier revision might be necessary if warranted by circumstances.

This said, I support Decisions 1 through 4 as suggested by the staff.

Mr. Wijnholds made the following statement:

Turning to the operational budget first, I believe it has been clear for some time that the level of reserve holdings does not adequately reflect the ability of Member countries to contribute to the budget. The allocation of currencies within the operational budget has been a source of much contention and debate, and I am glad that there seems to be broad support for changing the allocation mechanism. I agree with Mr. Kiekens and Mr. Prader that the guiding principle of any system should be that it is simple, transparent and equitable. I also agree that these considerations unequivocally point in the direction of a quota-based operational budget (option 4), which I would fully support.

Let me now turn to the surveillance issues.

First, I support a continuation of the current approach towards regional surveillance, while agreeing with the staff that the scope could be somewhat broader than that of the recent report on the euro area, although I consider that report a successful pilot-project. In my opinion, we could have a full-fledged discussion on EMU once a year, with perhaps a follow-up staff visit six months later, so as to provide some context to the bilateral Article IV consultations.

Second, I do not see much value added in calling our regional surveillance exercise a "joint Article IV". There is no precedent to label regional surveillance reports joint Article IV's among the other monetary unions in the Fund's membership. It comes across to me as a somewhat artificial way of underlining our obligation to consult with the Fund, certainly in light of the fact that EMU countries already endorse the need for regional surveillance. Moreover, it could create confusion about the status of the existing Article IV's for which I envisage no significant changes. As Mr. Kiekens and Prader point out, many smaller European countries, including my own, have not had an independent monetary policy for some time. Therefore, I do not expect the 1998 Article IV report to be significantly different in its coverage of economic issues from the 1999 Article IV report.

While I can understand the wish to streamline surveillance with individual EMU members, I would point out that the Fund, as a neutral arbiter, can play a very useful role in vigorously monitoring the progress in the fiscal and structural areas.

Third, I would welcome the presence of an ECB observer at the table when we discuss monetary policy issues. I believe the Board should try to formalize the modalities of such an observership as soon as possible.

Fourth, as regards the publication of PINs or a summing up of the Board discussion, I could support either. The publication of any kind of Board opinion would of course be voluntary and depend on the consent of the European/EMU countries concerned.

On the legal issues, I think we need to come back to this later.

As regards the provision of information to the ECB and vice versa, I agree with the staff's proposals.

Finally, it is probably useful to clarify the matter of the definition of reserves where there are some differences of views. I believe including the reserves of NCBs is logical. Only a limited amount of reserves will be transferred to the ECB. This buffer may turn out to be too limited in a turbulent world. The EU Treaty takes this into account by stipulating in Art. 30 of the Protocol on the ESCB that "the Governing Council shall decide upon the proportion [of NCB reserves] to be called up by the ECB following its establishment and the amounts called up at later dates."

Ms. Lissakers asked whether, in the case of Board discussions on noneuro-area countries' monetary and exchange rate policies, the euro-area Directors would take their guidance from the ECB or their respective national central banks.

Mr. Wijnholds responded that he did not officially receive instructions from his constituency's national authorities. However, in general, national central banks in his constituency would forward to him some background material and views. Nevertheless, he personally believed that the ECB would not, at the current stage, wish to convey strongly its views to individual euro-area Directors.

Ms. Lissakers commented that it was possible to encounter a case in which the ECB announced one opinion on the appropriate monetary policy of a noneuro-area country, but one or more euro-area Directors took an opposite view in the Board. It was relevant to the policy deliberations of the Fund to know which views should be taken into consideration on fundamental third-party issues.

Mr. Wijnholds said that Ms. Lissakers had raised an interesting point, but he pointed out that the matter was part of an ongoing process. However, as long as he was a Director elected by a number of countries, he would continue to express the views supported by his constituency.

Mr. Donecker agreed with Mr. Wijnholds. His positions in the Board would continue to reflect the views of his national authorities, which would take account of the ECB's views in its areas of competency

Ms. Lissakers commented that the matter raised the question of why the ECB needed to have observer status on any issue.

The Acting Chairman asked whether Ms. Lissakers favored including the ECB observer on Board discussions of large country Article IV consultations, as well as EMU-related issues.

Ms. Lissakers replied in the negative. She pointed out that the position of the United States had consistently been that another permanent chair should not be added to the Board of the Fund. What she had highlighted was a potentially anomalous situation in which the central bank of a large group of European countries would have no voice in Fund deliberations on international monetary affairs because there would be only individual Directors present speaking for their own national central banks. If she were to speak, in the context of a review of Japan's monetary policy, on behalf of only one of the regional constituent parts of the U.S. Federal Reserve Bank system, it would not be considered particularly useful in terms of the Fund's assessment. Clearly, the issue would need to be resolved by euro-area members at an early date

Mr. Grilli considered that such matters would likely present less trouble in practice than Ms. Lissakers had suggested in theory. Once it was accepted that the monetary policy of a group of countries would be conducted on a common basis, the communication of a common set of views on relevant issues would become clear.

Mr. Taylor believed that Ms. Lissakers had raised an important question that should be considered carefully. While he agreed that adding a twenty-fifth chair to the current Board was not desirable, it was difficult to see how the matter of incorporating the ECB's views on monetary and exchange rate policies could be adequately resolved without de facto adding another permanent chair. The ECB observer would have to be available, present, and involved in any useful discussion of issues in the ECB's specific areas of competency. For example, if there was an issue between the ECB and the United States on monetary policy or exchange rate management, it was unclear how the matter could be addressed without the full availability of the ECB observer. Recently, there had been some interesting informal exchanges between the German and American chairs on the behavior of interest rates. In the future, those exchanges would need to be between the ECB and the United States.

Mr. Wijnholds stated that the matter was somewhat more complicated than Mr. Taylor had presented. The problem was that some Directors hailed from central banks, and some from other institutions or ministries. Therefore, a variety of views would need to be considered. Clearly, the matter would need further reflection.

Mr. Donecker pointed out that Germany had been living with such a dualism at least since it had become a member of the Fund. The German central bank was strong and independent, and in the past it had voiced its comments and ideas—sometimes in contrast to the government—to the German Executive Director. In the end, it was the Director who represented a united view on each question. Therefore, in a hypothetical case of a United States Article IV consultation, it was less a question of contending euro-area views on the U.S. policy approach, than whether there was a need for any additional comment from an ECB observer with regard to the monetary policies of the United States. That question would be for the Board as a whole to decide.

Mr. Milleron recognized that the matter raised by Ms. Lissakers was important, and he fully agreed with Mr. Donecker. Clearly, the matter would need further consideration, and he expressed his appreciation for the patience displayed by other Directors as the euro-area members reflected on the issue.

Ms. Lissakers reiterated that the matter would need a timely resolution. For example, in the discussion of a Chairman's summing up of a Board discussion of the U.S. or Japanese Article IV consultation (which would be the basis of a PIN), the ECB's views on monetary and exchange rate policies would not be known and reflected in the Fund's assessment, except as individual EMU members chose to reflect the ECB's views—something that would not be clearly evident. Also, in a discussion of the policies of an EMU member country, the ECB would have observer status and might be asked to speak. She wondered whether the summing up would reflect the intervention by the ECB observer. Such issues were important because, since a PIN reflected the views of the Fund, the precise role and status of the ECB remained unclear.

Mr. Wijnholds pointed out that, for a German or Dutch Article IV consultation, the views of the U.S. Federal Reserve Bank were not clearly communicated to the Board.

Ms. Lissakers responded that her office consulted with the Federal Reserve Board, and there was a single U.S. view presented in the Board. However, the views of individual euro-area members on monetary policies would not necessarily be the views of the European Central Bank.

Mr. Daïri considered that the preceding discussion corroborated his contention that granting observer status to the European Central Bank might create some confusion, and that the matter should be reviewed more carefully.

The Acting Chairman noted that, as Mr. Wijnholds had pointed out, occasionally there might be differences of views between a government and a central bank on an issue, but the Executive Director would take account of those two views in formulating an intervention. So, even in that national system, there was a potential for disagreement, but that would be managed. In the case of the European Central Bank, as the membership was composed of many national governments, there might be the further possibility of conflicting views, which was why the U.S. chair wondered whether the ECB views could be coordinated among all the member states participating in the ECB. Clearly, the matter could not be resolved at the current meeting; it was an evolving process. The consensus in the Board appeared to be in favor of granting the ECB observer status in Board discussions on the issues relevant to the ECB. Beyond that, the Board would revisit the issue as the process evolved.

Mr. Pickford made the following statement:

> I hesitate to follow the discussion we have just had, especially given our rather ambiguous status as regards EMU. For the record, I think where you have interpreted the view of the Board is a sensible place to be in this situation. We agree with the ECB having observer status for the relevant Board discussions. We also agree that this is an important issue, and it raises important considerations of principle. We think we will have to keep it under review and sort out the details on a fairly pragmatic basis as we go along. As Mr. Milleron said earlier, we need flexibility in the modalities to respond to changing circumstances.
>
> On surveillance, we also do not see any need for formal arrangements at this stage. We prefer the first option, set out in paragraph 6 of the staff paper. We do so because we think it is more important to get the policy

coverage of surveillance right rather than to worry too much about the formal mechanisms, which could well be reasonably inefficient and resource intensive. I liked Mr. Grilli's cats. I was reminded of another animal which had some interest a few years ago—the so-called duck test. I guess our view is that if surveillance walks like, talks like, and looks like surveillance, it is surveillance.

I will try to be as brief as possible on the remaining issues, with one exception.

On the frequency of discussions and whether the consultations with the ECB and other EU institutions are semiannual, it is not clear, to our view, that we need more than one annual discussion in the Board, but it is right, nevertheless, that the staff should report to the Board on its discussions. So, like others, we like the idea of an information paper which we could take up briefly in the WEO discussion.

On PINs, we think that in this case there should be a PIN, also, and we reiterate our view that we think publication of PINs should be mandatory for all surveillance discussions. So if this looks like a surveillance discussion, we think there should be a PIN.

I would like to say a few words on the operational budget. Let me say, first of all, that I agree with the staff that, while a balance of payments need for an EMU member may seem an unlikely event, again we will probably be able to recognize it if it ever occurs. As such, I agree that the Fund should be able to provide balance of payments assistance to EMU members in just the same way it provides financing to other members when they get into difficulties.

Second, on the question of selection of currencies for transfer operations in the operational budget, I support the staff's proposal that inclusion or exclusion of EMU countries should be common to all members of the currency union, depending upon whether the euro itself is deemed to be sufficiently strong. It seems again to be a pragmatic and sensible approach to take, given the uncertain information that national reserves data will provide about a country's balance of payments position. This chair has argued for some time now that the Treasurer could safely include a larger number of currencies on the transfers list. We therefore are glad to see the staff partially recognizing this approach in its proposed framework for the nonuse of an EMU country with a weak balance of payments position even though the euro itself is deemed to be sufficiently strong.

On the vexed question of the allocation method of currencies under the operational budget, my authorities could accept either the third or the fourth option. If it were up to us to choose between those two alternatives, we would, for fairly obvious reasons, prefer Option 3, because the use of sterling for transfers under that option would be considerably less. But we do also accept the case put forward by other Directors that Option 4 has merit because of its objectivity, simplicity, and transparency. So, if acceptance at this Board of Option 4 would open up a general consensus in favor of full publication of the Fund's operational budget then we could also accept this approach rather than Option 3. Regardless of which allocation method is chosen, like others I would prefer some form of transition period, as suggested by the staff. No doubt, the key factor in determining how long that transition period has to be will be the size of future drawings by members.

More generally, going down this route on the allocation method would mark a significant movement toward greater symmetry in members' rights and obligations, as many others have pointed out this morning. I welcome this development, and I would like to highlight another area, which is the so-called system of norms, where in our view there continues to be inequity in the Fund's financial arrangements. At present, the United Kingdom has one of the largest unremunerated reserve strength positions relative to quota of any IMF member. The cost implications of this variation diverge strongly from the general principle that quotas should form the basis of members' financial relations with the Fund. I would very much like the Board to revisit the idea that we put forward a couple of years ago of a uniform norm for all members in the near future.

Mr. Morais made the following statement:

First, on Fund surveillance. The elements identified as essential for strengthening Fund surveillance in the EMU appear quite comprehensive, and I can agree with the staff's proposal regarding the coverage of surveillance and counterparts for the purpose of consultation discussions with the EU institutions. I also find its suggestions on frequency and timing reasonable.

Regarding the status of discussions with EU institutions, I recognize that, in terms of substance, there should be no difference between the two options proposed by the staff. Nevertheless, my preference is for the second approach. Since individual EU member countries continue to be members of the Fund, they, rather than the EU, are bound by the obligations of Article IV, Section 1, notwithstanding the fact that they will have surrendering authority for monetary and exchange rate policies to EU institutions.

I have no strong view on whether reports on follow-up staff visits should be issued to the Board for information or for discussion. I think the informal country matters framework should be broadly appropriate in this respect if there are developments requiring the Fund's response. As regards reports on regional surveillance, a Board discussion seems necessary so that the Board can appraise the regional stance of monetary and exchange rate policies and convey its views to the competent EU authorities. The bilateral consultation with members would no longer be the appropriate context for discussing these policies.

On transparency, two issues are raised: how to address the concluding statement of the Board discussions and the competent authority to decide whether it should be made available to the public. There are the related questions of the competent authority regarding PINs. The pragmatic solution seems to me to be to leave these decisions to EU institutions to determine.

Regarding Article IV consultations with individual members of the euro area, I can broadly agree with the staff's views. Specifically, on the issue of the frequency of consultations, while I agree with the staff that annual consultations are likely to remain appropriate, it should be left to the individual members. The suggestion to cluster consultations around staff visits to EU institutions is very useful.

On the important issues of how the views of ECB and other EU institutions can be best represented in the Board discussions, I can agree with the general idea of observer status, provided that objective criteria be in place to decide upon such representations, as suggested by Mr. Daïri.

Concerning the Fund's operational budget, it would appear from the staff paper that the most simple and equitable solution is to have a uniform approach that would use Fund quotas as the distributive criterion.

Mr. Ismael made the following statement:

At this stage of the discussion, I will state briefly the position of this chair on the principal issues and submit my full statement for the record.

On surveillance, I join others in noting that, due to the fact that economic and financial policies will be made at both national and regional levels, it is important that we establish a proper framework to conduct our surveillance exercise. Therefore, on the status, our preference is for the formal approach, which would include a joint consultation to be held periodically with the institutions that have responsibility in certain areas of economic and financial policies. As noted by the staff, certain areas of policies will remain under the responsibility of national authorities, but as some of these policies would also impact on the euro area as a whole, it would be necessary to address them in a regional context for the consultation.

On frequency and timing of discussion, as well as publication of information, our views are similar to those expressed by Mr. Kiekens and Mr. Prader in their buff statement. On representation of the Board, we can agree with observer status for the EU. However, like Mr. Harinowo, we note that it may raise similar requests from other regional organizations. On data information provision, we can agree with the staff proposal.

Turning to the issue of the use of Fund resources and the use of euros in the operation budget, as has been noted by previous speakers, the main difficulty is with regards to our considerable balance of payments and reserve position. We agree that these difficulties raise some problems regarding the diminishing balance of payments needs for individual countries. While the measures described are helpful, it is clear that more work will be needed to develop a set of criteria to estimate the balance of payment needs and reserve strength of each country. However, we agree with the staff that the balance of payments need, if it arises, will be recognized and appropriately dealt with.

Similarly, the difficulties create some problems as regards the assessment of individual countries' financial strength for the designation plan in the operational budget. However, it would appear that the assessment of balance of payment and reserve strength for the euro area as a whole does not pose major difficulties. Therefore, we would agree that the inclusion of the euro in the operational budget should be common to all members of the union and that this inclusion will deepen the strength of the euro.

As to the principle that could govern the allocation for transfers under EMU, here also there are difficulties. The staff has proposed four alternative approaches. Option 2 can be acceptable, although we note that, for reasons of simplicity and equity, the fourth option has merits.

In conclusion, in view of the unique challenge that the euro will pose, we agree with Directors that we will need to proceed with caution and that a certain amount of flexibility and pragmatism will be required in our approach, especially during the transition period.

Mr. Karunasena made the following statement:

Like other speakers, I would like to thank the staff for preparing useful papers, with the set of proposals on the relationship between the Fund and the EMU. At this stage, I will be very brief and give our comments with regard to the major issues for discussion today.

On the Fund's surveillance, we are of the view that continuation of emphasis on the individual contributors is useful. Hence, we consider it maybe not necessary to have a separate formal Article IV consultation with the EMU. However, the Fund mission can discuss with the ECB when it undertakes the Article IV consultations with the member countries of the EMU.

With regard to the proposal giving observer status, we have no objection to granting permission to the ECB to participate in the discussions relevant for the EMU members. However, we also consider, like Mr. Daïri, that it is useful to consider and define some guidelines or criteria for granting observer status for the regional organizations before making any final decision on this matter.

With regard to the operational budget, we prefer the proposal based on the quota basis. Therefore, we are supporting Option 4.

The Deputy Director of the Policy Development and Review Department, in response to questions and comments by Executive Directors, made the following remarks:

Let me start with the area where the competition between the two teams was the most sharp—the area of regional surveillance of EMU—with those in favor of informal surveillance, perhaps we can call them the legal minimalists, captained by Mr. Donecker, on the one side, and then the legal maximalists, in favor of Article IV governing these regional surveillance meetings, perhaps captained by Mr. Kiekens. I thought there were a few points that possibly needed some clarification.

First, the argument that the Fund being a member-based institution militates against having Article IV govern these regional surveillance meetings is a red herring. As paragraph 6 of the staff report makes clear, these would be joint consultations, with the set of members with respect to the particular topic. I think that was clarified also by the General Counsel.

The argument that we would cover much the same material whether it was formal or informal—as some referred to it, if it walks like a duck and quacks like a duck, then it is a duck—also requires some clarification. In substance, perhaps we would likely discuss the same topics, but I think there would be a substantive distinction about the clarity with which we would pursue our mandate under the two different sets of rules. In other words, it may be a duck, but whether we are allowed to shoot it depends on whether we have a hunting licence. That is perhaps the distinction. Let me try to clarify that more.

Article IV spells out the Fund's mandate to oversee the international monetary system. It also stipulates members' obligations to consult with the Fund to that end. Monetary policy in the EMU area will be formulated by the ECB, not by the individual member countries, and it will almost certainly have a systemic influence. The question is: how do we capture that discussion of that systemic influence under Article IV? If we have a bilateral Article IV discussion with Ireland, for example, I suppose that we will discuss the implications of EMU monetary policy for Ireland. But with whom will we discuss the formulation of EMU monetary policy, and how will we capture that under the Article IV process, which is central to our mandate to oversee the system? That, I think, is an important distinction.

Article IV also entails specific procedures, including provisions on coverage and frequency of discussions, timeliness of reports, and notification of delays. These are broad parameters within which, I think, we will be developing specific procedures as we go along; and I do see an argument for some flexibility as we define our relations with the European institutions more clearly.

On the question of frequency, I would guess that our surveillance over EMU issues, much the same as our surveillance over the policies of the U.S. Federal Reserve and other major monetary institutions, will be continuous. We might have a once-a-year formal meeting. We might submit a report for the information of Directors at some other time in the year. If there were important issues that arose in that second report, Directors might wish to call a Board meeting and turn that into a more formal procedure. I would guess, though, that when we do have a meeting, even if it is on the secondary consultation with the ECB, as it were, it would be different from the WEO, in that whatever comes out of that meeting would have the weight of the institution behind it, and not be simply a staff document that Directors discussed.

On Mr. Harinowo's remarks on surveillance of other regions, clearly we have been enhancing our regional surveillance over time. We have had recently a discussion of the CFA franc zone, and a paper on issues relating to Fund's regional surveillance more generally is under preparation. I think there is an important distinction to make. EMU is unique in terms of its potential systemic influence, and quite distinct in that respect from the CFA franc zone or some other regional groupings.

Mr. Ono has asked about the SDDS and how EMU would impinge on it. This, as we mentioned in the paper, will be discussed in the second review of the SDDS, which is scheduled for later this year. Our statisticians are working with the ECB and EUROSTAT to try to define money and banking terms, consumer price index coverage, and other definitions. I think the most likely outcome will be that we have euro-area statistics on the page for each of the individual countries rather than having an EMU page per se. But I would not like to anticipate what comes out of that later paper.

The staff representative from the Treasurer's Department, in response to questions and comments by Executive Directors, made the following remarks:

I would like to focus my remarks on the questions of the need for and use of Fund resources by the EMU countries and the operational budget issues that have been raised.

The staff had considered that, as the paper made clear, the likelihood of an EMU country coming to the Fund for the use of Fund resources as was very low. Nevertheless, the possibility exists in principle and should continue to be considered. By the same token, while it is quite difficult to have an individual country assessment of external strength at the level of an individual country, and the staff therefore proposed that the assessment of external strength for the euro should be done for the union as a whole, one could conceive, again theoretically, a possibility where one particular country was not strong enough. In the staff's view, however, this was very unlikely, and the staff did not believe that it required a new set of indicators, as Ms. Wang had suggested.

On the assessment more generally, reserves might very well be more difficult to define in the context of EMU, and work is still ongoing in this regard. Nevertheless, the Articles of Agreement required reserves to be taken into account as part of the assessment process, and the staff would intend to include the reserves of the NCBs in the assessment of the euro area as a whole.

As regards the key for the allocation of currencies in the operational budget, Directors' comments have been very clear and very helpful for the forthcoming more comprehensive review of the allocation method which will be undertaken after the Annual Meetings. A change in the key away from reserves toward quotas would, of course, obviate many of the difficulties that arise with the definition of reserves within EMU or, for that matter, the definition of gross reserves for many other countries.

On the question of the changeover to a new allocation key and length of the transition period, Mr. Harinowo has rightly pointed out that the first priority should be to secure the smooth financing of the Fund's operations. The change to a different allocation key could be done relatively quickly, but a particular key also implies a particular harmonization principle. Given the current relatively wide disbursement of the Fund's holdings of members' currencies in terms of quota, one would need to take into account the implications for moving within a reasonable time frame toward a reasonable harmonization of positions. So the transition has to be understood as involving a dynamic medium-term element, and not simply a question of how quickly a new allocation key could be implemented in a given operational budget. Again, these issues will be taken up after the Annual Meetings in the context of specific operational proposals.

Mr. Daïri said that he did not fully agree with the earlier comment that the Fund's role in bilateral discussions with EMU countries would be to ensure that policies were consistent with the common monetary policy of EMU. That was more the responsibility of the European institutions themselves. The Fund's role was to ensure consistency of both domestic policies and the common monetary policy with the obligations of members under the Articles of Agreement. In that context, the discussions with European institutions should be formal, but not to the point of making those consultations separate from the bilateral discussions, because there could be only one consultation for any member. The official conclusion of the bilateral discussion would be with the members in light of their policies and in light of the common monetary policy as discussed with the European institutions.

Mr. Donecker said that he was not convinced by the Deputy Director of the Policy Development and Review Department's argument on the need for formal discussions. The Article IV process was between the Fund and the member—a bilateral process. The member had certain rights and obligations. At the moment, it would be more appropriate to continue to develop the current, informal process with respect to EMU surveillance—which a number of Directors had supported—and then to review whether, in the light of experience, a need existed for a more formal approach. Clearly, the focus should remain on the substance of the surveillance in the regional context, with close contact and discussion with the ECB.

Ms. Lissakers said that she believed that part of the problem in the current debate was the fact that EMU entailed a transfer of sovereignty over monetary policy to the ECB, and there seemed to be a certain amount of reluctance on the part of the individual EMU members to accept the ramifications of that transfer.

Mr. Grilli said that he disagreed with Ms. Lissakers. He had argued for pragmatism and a type of learning-by-doing approach because it was difficult to realize, ex ante, all the important issues that would need to be considered. Surveillance of monetary and exchange rate policies of EMU as a group had two aspects. First, there were the effects of that common monetary policy on the member countries, which could be addressed in the annual consultations with the various members. Second, there was the aspect of the systemic impact of EMU-wide monetary policies. It remained unclear how best to address that external aspect of EMU, but it was clear that it would be preferable to pursue the current process: the Fund staff should hold discussions with ECB officials on the systemic impact of an EMU-wide monetary policy, and then prepare a report that would serve as a basis for a Board discussion. If the consequences of that common policy were deemed to be important, then the EMU members—individually and collectively—would be responsible, as members of the Fund, to ensure that any concerns were properly addressed. Therefore, the matter of a formal or informal approach to surveillance over the EMU was not essential; the substance of the process of surveillance remained central to the whole exercise of the Fund's mandate.

Ms. Lissakers said she agreed with Mr. Grilli that many issues remained unclear. However, it appeared that Mr. Donecker had argued that the definition of sovereign state was unchanged by the advent of EMU. Indeed, the Legal Department also seemed reluctant to address the matter fully in the paper they had prepared. Nevertheless, the fact could not be ignored that a partial transfer of state sovereignty was involved in the creation of EMU. She asked that, in the context of the next discussion of EMU-wide policies, the staff analyze in greater detail such issues.

The General Counsel noted that the staff paper stated clearly that a transfer of certain attributes of sovereignty did not mean a loss of sovereignty. The members of the European Monetary Union remained sovereign states. The fact that they had established an international agency that would be in charge of monetary policies was not unprecedented. Indeed, it had been mentioned earlier that for a number of years the West African Economic and Monetary Union had had a central bank in west Africa, similar to the one in central Africa, which was an international agency. The Fund had conducted consultations with those member countries along the lines of what some Directors had referred to as the minimalist approach. Clearly, the staff was not saying that one or the other approach was legally required or illegal. He would agree with those Directors who said that it was a matter of judgment and opportunity for the Board to decide how best to conduct its Article IV consultations with the members of the European Monetary Union.

Mr. Donecker said that there had been an interesting exchange of views, and it would be best to reflect further on the important issues. It would be useful to inform the national authorities on the various positions expressed by Directors, and to remain open-minded about the various approaches, which was what the General Counsel appeared to be advising.

The Acting Chairman said that he believed that all Directors agreed on the substance of surveillance, namely, that the substance was important, and that the Fund had to be engaged in surveillance vis-à-vis the European Central Bank, in order to be faithful to the mandate outlined in the Articles of Agreement. As to how to fulfil that role, it appeared that, notwithstanding the views of the Deputy Director of the Policy Development and Review Department, the matter would need to be regarded as an evolving process.

Mr. Kiekens concurred that all Directors agreed on the substance of surveillance over the EMU. It was the obligation of the Fund to conduct surveillance, and the obligation of the member states to participate in such surveillance; those obligations were contained in Article IV of the Articles of Agreement. If that were accepted, then discussing the various modalities of the process of surveillance was less important.

After adjourning at 1:00 p.m., the meeting reconvened at 2:30 p.m.

The Acting Chairman made the following concluding remarks:

> Directors welcomed the comprehensive set of papers prepared by the staff on the main legal issues and operational implications for the Fund of the

move to the third and final stage of European Economic and Monetary Union (EMU). They noted that the introduction of the euro will represent an important milestone in the evolution of the EU and the international monetary system, that the advent of EMU will have important implications for the Fund, and that a number of relevant questions have still to be explored more fully. Accordingly, Directors noted the preliminary nature of a number of the Board's considerations, and they looked forward to further discussions before January 1, 1999. Moreover, Directors recognized that, as work on Fund-EMU relations proceeds and as EMU itself evolves over time, the Board may have to come back to a number of aspects subsequently.

Regarding the legal issues that arise in the context of EMU, Directors noted that the Fund is a country-based institution and that the transfer of monetary powers by members of the euro area to institutions of EMU will not affect their legal relationship with the Fund under the Fund's Articles of Agreement. euro-area members will continue to be members of the Fund in their own individual capacity as countries. All rights of membership will continue to be available to each individual member, and all the obligations that membership in the Fund entails will continue to bind each of them individually. Nevertheless, Directors noted that the exercise of the individual rights and fulfilment of the obligations of members may be affected by the adoption of a common currency and the transfer of competencies to common institutions within the euro area. Directors agreed that legal issues may need further consideration.

Directors noted that EMU, and particularly the adoption of a single monetary policy under the responsibility of an independent European Central Bank (ECB), will have important implications for Fund surveillance. Economic policies of the euro area will have important effects on other countries, and Directors agreed that the Fund's responsibility to conduct firm surveillance over members' external and exchange rate policies would require intensifying discussions with EU and euro-area institutions, especially the ECB. Regarding the modalities of the Fund's surveillance over the euro area, however, views differed. Many Directors supported including surveillance of EMU directly as part of the Article IV process, noting that this would explicitly recognize the obligations of EMU members to consult with the Fund in this context. Some Directors, however, saw advantages—at least for an initial period—in a less formal approach. Taking into account the views expressed at today's meeting, we will need to finalize at an early date the modalities of surveillance over the euro area.

Directors remarked that, in light of the changes in policy responsibilities under EMU, the coverage required for conducting surveillance would need to be broadened and deepened. Discussions with the ECB would pay particular attention to monetary and exchange rate policies. While fiscal policy for each member of the EU remains under the authority of national authorities, most Directors noted that discussions at the EU level would also need to evaluate the fiscal position of the euro area as a whole in order to assess the stance of monetary and exchange rate policies and the coherence of macroeconomic policies, as well as developments and policies in structural areas, including labor markets, relevant to the Fund's surveillance over the euro area as a whole.

While regular dialogue would be required with the ECB, regular contacts could also be appropriate with ECOFIN and representatives of the Economic and Financial Committee once it had become operative. Discussions with the staff of the European Commission also would be needed, given the Commission's role in many of the areas to be covered, but a number of Directors emphasized that the nature of these discussions should be somewhat different.

Directors supported regular reporting to the Board on developments and prospects in the euro area and the EU more generally. Several Directors questioned the need for semi-annual stand-alone Board discussions, noting that in the case of individual Article IV consultations there is typically only one Board discussion annually and there would also be an opportunity to discuss developments in the euro area in the context of the WEO. Some Directors considered that semi-annual discussions were warranted given the need to provide adequate context for bilateral consultations with euro-area members. On balance, Directors supported one annual consultation with respect to the euro area, supplemented by a follow-up visit, which should produce a paper for Board information and provide adequate context for bilateral consultations.

With respect to the Fund's transparency on its surveillance of EMU, Directors agreed that, subject to the consent of the members concerned, PINs could be issued following the conclusion of the Board discussion on surveillance in the euro area.

With respect to the Fund's bilateral surveillance, Directors emphasized that consultations with individual Fund members would remain central to the Fund's surveillance activities also under a single currency. However, these discussions should focus on fiscal, financial, and structural policies, with discussions on monetary policy centered on the impact of the stance of ECB policy on the national economy, as well as issues pertaining to the implementation of monetary policy operations through the national central banks. Directors also saw merit in clustering, to the extent possible, the individual discussions with the Fund's surveillance over the euro area to allow for a broader assessment of EMU-wide developments and ensure timely input to the bilateral consultations. Some Directors noted that some redirecting of staff resources away from bilateral surveillance of euro-area countries to surveillance over the euro area could be warranted.

Directors agreed that effective communication of relevant EU institutions' views in Executive Board discussions will be important for enhancing the Fund's surveillance over the euro area. They supported making arrangements with the ECB to grant it observer status at selected Board meetings. Directors noted that the detailed modalities would need to be worked out over the coming months. However, some Directors would have preferred that criteria to assure uniform treatment of similar institutions be developed. In addition, a few Directors supported inviting other relevant EU institutions or bodies to circulate a statement in advance of the Board's discussion on the surveillance of the euro area; however, most Directors felt that these views should rather be expressed by a designated Director from an EU country.

Directors highlighted the implications for national and regional data and information provision to the Fund from the move to the euro. They directed the staff to make the necessary arrangements, particularly with the ECB and EUROSTAT, on the transfer of a set of data on a regular and timely basis.

The Board also examined the implications of the possible use of Fund resources by members of a monetary union, notably with respect to EMU. While the identification of balance of payments need is likely to be more difficult than in the case of a member with its own currency, Directors noted circumstances could arise where such a need could be discerned, based on various indicators such as exceptional financing and movements in interest rate premia. However, Directors agreed to come back to this issue.

Directors also had a preliminary exchange of views on the use of the euro in the operational budget. With respect to the selection of currencies to be included in the operational budget, Directors agreed that assessments of balance of payments and reserve strength of individual euro-area members should normally be based on the external strength of the euro area as a whole. If the euro area was considered sufficiently strong, it would normally be expected that all euro-area members would be included in the operational budget for transfers. Regarding the measurement of reserves, Directors felt that they should be assessed on the basis of reserves held by the European System of Central Banks, including those held by the national central banks.

Directors noted that the allocation of currencies under the operational budget raised important issues for the financing of the Fund. They agreed in principle that, given the change in the role of reserves in the system and also the need to respect uniformity of treatment, the method of allocating currencies should be based on members' quotas. Given the current wide dispersion of Fund holdings of currencies in relation to quotas, Directors generally felt that a change in the method of allocating currencies would need to be phased in over a period of time, although views differed regarding the length of the transition period. A few Directors would have favored an allocation mechanism for the euro parallel to that for the U.S. dollar. Directors will come back to the operational aspects in the context of a comprehensive review of the guidelines for the allocation of currencies in the operational budget after the 1998 Annual Meetings.

Mr. Newman noted that the Acting Chairman's concluding remarks had pointed to a number of issues that would need to be revisited, including the precise meetings at which the ECB would be an observer, how currencies would be allocated in the operational budget, and how to determine a balance of payments need for an EMU member state that might want to draw from the Fund's resources. Those were important issues that would need to be addressed as soon as possible—preferably before the launch of EMU on January 1, 1999.

Mr. Wijnholds agreed that a number of issues would need to be considered further. In that context, he would not yet draw definitive conclusions on the matter of whether a more formal approach to regional surveillance over EMU was preferable.

Mr. Donecker agreed with Mr. Wijnholds that the precise modality of regional surveillance would need to be discussed further, especially the legal issues surrounding the matter.

Mr. Grilli agreed with Messrs. Donecker and Wijnholds. He also considered that the concluding remarks were extremely important—especially for EMU countries—and he would appreciate reviewing the concluding remarks before they were issued.

Mr. Toribio concurred with Mr. Grilli that it would be useful to review the concluding remarks before they were issued.

Mr. Taylor believed that the concluding remarks were even more important for non-EMU members. He considered that little was achieved by drawing a firm conclusion regarding the formal and informal approaches to regional surveillance. The key remained a fully effective surveillance process, which would require direct contacts and communication with the institution holding the responsibility for monetary and exchange rate policies—the ECB. It was still unclear how that communication could be best achieved. Clearly, the situation would evolve and the matter—along with many other important items—would need to be revisited.

Mr. Newman considered that the suggestion of Messrs. Grilli and Toribio of circulating the concluding remarks for Directors' review before their issuance would set a counterproductive precedent. He reiterated his belief that a number of important issues would need to be clarified as soon as possible.

The Deputy Director of the Policy Development and Review Department explained that there had already been a preliminary discussion on the range of issues during last year's regional surveillance discussion of the European Union. Moreover, the Interim Committee had requested an update on progress in clarifying the relevant issues for its upcoming meeting. Accordingly, the staff had hoped that, on several important matters, understandings could be reached beyond the preliminary stage. The surveillance process envisaged by the staff would entail a joint Article IV discussion with all the members of EMU, which would not represent an additional Article IV consultation. The comprehensive discussions would cover the issue of common exchange rate and monetary policies, which would form the basis of the individual Article IV consultations with each EMU member.

The Acting Chairman concluded that several issues would need to be revisited in the near future, and that those issues that received broad support would be advanced. Clearly, there had been no disagreement on the need to deepen and broaden the discussions with the European Union institutions in their relevant areas of competency. The concluding remarks would be finalized to take account of Directors' views and issued shortly.

2. EUROPEAN ECONOMIC AND MONETARY UNION AND THE FUND—SDR VALUATION AND THE SDR INTEREST RATE

The Executive Directors considered a staff paper on the European Economic and Monetary Union and the Fund—the valuation of the SDR and the SDR interest rate (SM/98/221, 9/1/98).

Mr. Kiekens and Mr. Prader made the following statement:

> The staff's proposals for adapting the SDR to the introduction of the euro are welcome.
>
> The present SDR valuation method can be left intact and the euro can replace, on January 1, 1999, the present currency shares of the deutsche mark and French franc in the SDR basket. Also acceptable are the staff's conversion and rounding proposals for ensuring that the December 31, 1998 value of the SDR, calculated on the basis of euro currency share will be the same as the value of SDR for that day calculated on the basis of the currency shares of the deutsche mark and French franc.
>
> Not acceptable, however, is the proposal to delay the next review of the SDR basket until 2003. Box 2 reminds us that for the sake of continuity, revisions of the method of SDR valuation should only occur "as a result of major changes in the role of currencies in the world economy." The introduction of the euro as the single currency of largest trading area in the world is clearly a major change and calls for reviewing the SDR basket no later than the end of 2000, as presently scheduled.
>
> By the same token the three-month EURIBOR, the reference interest rate for the euro interbank market, should be used in the SDR interest rate basket, rather than some combination of the market yield of three-month French Treasury-bills and Germany's three-month interbank deposit rate, as proposed by the staff. There is no need to seek proxies for the short-term reference interest rate in the euro market when the reference rate itself exists.
>
> Finally, the Euro/U.S. dollar reference exchange rate announced daily by the European System of Central Banks should be used for SDR valuation. This should be acceptable to this Board, since it will be a representative spot rate for the U.S. dollar as required for the valuation of the SDR in the Fund's Rules and Regulations.

Mr. Donecker made the following statement:

> The statement of Mr. Kiekens and Mr. Prader on the review of the SDR valuation interest rate basket paper has made my job of commenting on the staff's proposal very easy. In the interest of an efficient conduct of our Board discussion, I simply want to state that we fully support Mr. Kiekens and Mr. Prader's respective comments and proposals. As to the method of calculating the daily value of the SDR in U.S. dollars, an issue that has not

been addressed in the staff paper, allow me to add that we would favor as a matter of principle that this determination of the daily SDR value should be based on exchange rates taken from one major foreign exchange market.

On the composition of the SDR interest rate basket, my authorities have quite recently indicated to the staff that they prefer to use the EURIBOR as the more relevant interest rate for the euro for the purpose of calculating the SDR interest rate basket.

Mr. Elhage made the following statement:

On SDR valuation and the interest rate on the SDR basket, we can support the proposal to substitute the euro for the Deutsche mark and french franc in the valuation basket with the current weights as a transitional period.

For the reasons raised in the preliminary statements of Ms. Lissakers, Mr. Newman, Mr. Kiekens and Mr. Prader, we would prefer a somewhat shorter interval than 2003 proposed by the staff for considering the next revision of the valuation basket.

On the SDR interest rate basket, we can accept the staff's proposal.

Mr. Hendrick made the following statement:

Regarding proposed decision 1, this chair would favor a shorter interval than suggested by the staff, possibly in 2001/2.

On proposed decision 2, we agree with the staff's recommendation that no change be made in the method SDR valuation or in the SDR interest basket at this stage. We can also accept that the euro replace the current currency amounts of the Deutsche mark and the French franc in the SDR basket. Similarly, the staff's conversion and rounding proposals give continuity to the value of SDR. We would be sympathetic, however, to giving further consideration in the future to reducing the number of currencies in the basket to three, namely the euro, the Japanese yen, and the U.S. dollar, as such a move is more likely to contribute to the robustness of the basket over time.

In addition, it is clear that the introduction of the euro will have an impact on the current method of valuing the SDR in the future, calling into question the one-to-one relationship between currency and member country inherent in the current method of SDR valuation. We see merit, therefore, in a comprehensive review of the method of valuing the SDR to better assess the relative importance of currencies rather than members in the international financial system.

Finally, we have no objections to the proposed decisions 3 and 4.

Ms. Wang made the following statement:

We support proposed decisions 2, 3 and 4 concerning the valuation and interest rate of SDR. As for the timing of the next revision of the valuation basket of SDR, we can go along with the view of Ms. Lissakers and Mr. Newman.

Mr. Bernal made the following statement:

We broadly agree with the main conclusions of the staff document on Valuation of the SDR and the SDR Interest Rate. Therefore, we can support the proposed decisions. However, given the importance that the euro will have in the international monetary system, it would be absolutely necessary that the Fund remains vigilant of the developments that occur in the process of consolidation of the currency union, and provision for an early revision of the SDR basket should be made to address any situation that could arise.

Mr. Daïri made the following statement:

On the issue of valuation of the SDR, we support the staff proposal that no change be made at this stage and that the combined weight given to the DM and the FF be given to the euro. This is in line with the main principles governing SDR evaluation and is further corroborated by the finding that exports from the euro area (excluding intra-euro trade) are more or less equal to exports from Germany and France. We also agree with the proposed decision on the conversion and rounding procedures.

As regards the SDR interest rate basket, we are somewhat uncomfortable with the proposal that the same currency—the euro—will be represented by two different interest rate instruments, i.e., the three-month interbank rate for Germany and the three-month Treasury Bill for France. We wonder whether these instruments will remain broadly representative of the range of financial instruments available to investors in the euro market since by definition the market will have no boundaries between member countries. Moreover, it is not clear to what extent will the interest rates of the two instruments reflect the euro-wide liquidity position and the direction of monetary and exchange rate policies of the euro area. Some indication on the historic differentials between the two instruments is welcome. This being said, we can support Mr. Kiekens and Mr. Prader's proposals to use the EURIBOR for the euro instead of the two national instruments.

As regards the revision of the valuation of the SDR, we encourage an earlier revision to take stock of the early developments in the euro, as suggested by Ms. Lissakers and Mr. Newman. Such an early revision may also be warranted not only as a result of a possible participation by the United Kingdom in the EMU, but also in view of the growing role of China in the world economy.

Mr. Al-Turki made the following statement:

I have no difficulty in accepting the staff's proposal to substitute the euro for the deutsche mark and the French franc in the SDR basket with no change to their current weights. I also agree that the next revision of the SDR valuation basket take place no later than 2003 and that a shorter period may be considered if warranted by new developments.

With regard to the SDR interest rate basket, the determination of the SDR interest rate is country based. Therefore, I can accept the proposal to continue using the same financial instruments in the SDR interest basket.

Mr. Askari-Rankouhi made the following statement:

We support decisions 2, 3, and 4. On SDR valuation, we support the staff's proposal of no change in the method of SDR valuation as a consequence of the introduction of the euro. However, we cannot support the decision to postpone the next review of this matter until 2004. There are some uncertainties, and I think it would be prudent to come back to this issue earlier.

We can also support the staff's proposal concerning the financial instruments in the SDR interest rate basket, but I do not think short-term instruments in France and Germany will carry different interest rates, so the inclusion of both French and German interest rates seems unnecessary. If there is a euro instrument that is appropriate, we would agree to that. Perhaps the staff could explain a little bit about EURIBOR and whether that is an appropriate instrument or not.

Mr. Toribio made the following statement:

This chair supports entirely the proposals of Mr. Kiekens and Mr Prader in their preliminary statement. That means that we agree with keeping in tact the valuation method for the SDR and the substitution of the euro for the French franc and the deutsche mark. However, we do not think it is prudent to delay the next review of the SDR basket until the year 2003, and we would prefer to keep the review of this basket to no later than the end of the year 2000, as initially scheduled.

Finally, it means that we are also in favor of using the three-month EURIBOR instead of this combination of the three-month French treasury bill rate or Germany's three-month interbank deposit rate.

Mr. Newman asked for an explanation of the differences between the approach proposed by the staff and the approach proposed by Messrs. Kiekens and Prader. The staff proposal simply assumed that the euro was the domestic currency of France and Germany, whereas the Kiekens/Prader approach used the euro more generally and not necessarily associated with either France or Germany, despite the fact that the euro would be the common currency for all EMU members.

The Acting Chairman asked the Treasurer to explain the ramifications of using the EURIBOR rate.

The Treasurer responded that the staff had followed the approach of using the relevant members' instruments in the various baskets which, in the valuation basket, happened to be the same currency. In the interest rate basket, however, the French treasury bill would continue to exist—even though it would be denominated in euro—as a prime asset representative of the French money market, consistent with the inclusion of the U.S. treasury bill and the U.K. treasury bill. Therefore, the staff believed that it would be logical to maintain that prime asset in the interest rate basket. There had never been a German government treasury bill representative of the short end of the market in Frankfurt for various reasons, and the German banks' interbank offer rate had been used. That rate would also continue to exist, but it would be denominated in euro. Again, following the principle that they were the members' instruments in the basket, the staff considered that consistency was called for.

EURIBOR was set to become the offer rate of transactions between various banks, which would take an index of 57 banks, most of them within the euro area, but also several international banks, the Treasurer continued. There was not, however, a spot rate quoted at present. However, as a measure of risk, EURIBOR was clearly going to be higher than the French treasury bill rate and probably the Frankfurt interbank offer rate. Currently, for example, the ECU interbank market rate was about 15–16 basis points, on average, above the French treasury bill rate and the interbank offer rate in Frankfurt. It was not yet clear whether the ECU-EURIBOR rates would be parallel, particularly in view of the unique way that the EURIBOR rate would be calculated.

Another element that would need to be considered was the fact that, from January 1, 1999, there would be minimum reserve requirements imposed in the euro area, which would have a further impact on commercial bank interest rates, the Treasurer explained.

If decision No. 3 were changed to refer to the EURIBOR for both the French franc and the deutsche mark elements, that decision would need a 70 percent majority in the Board, because it would directly affect the rate of charge on the use of the Fund's resources, the Treasurer stated.

Mr. Giustiniani considered that the participation in the valuation of the SDR and the SDR interest rate should be currency based.

Mr. Newman reiterated his request for clarification of the ramifications of the approach suggested by Messrs. Kiekens and Prader. Under the staff's proposal, it was assumed that France and Germany had a currency called the euro, and their export weights would be used in calculating the SDR value; by coincidence, they happened to provide the same result as the use of euro weights. Under the Kiekens-Prader approach, countries were not used as the basis, but simply the currency used by 11 members. He wondered whether that was a fundamentally different approach and whether that had ramifications regarding the appropriate weights that should be used.

The Treasurer responded that the matter of how the various weights were used would need to be discussed further at a future meeting. Currently, as it happened, the external trade for Germany and France was about equal to the netted-out trade for the euro area. Therefore, it added to the plausibility of maintaining the current weighting system for France and

Germany in the basket. But, what happened in the future and how the Board wished to approach the issue of the euro in the broadest sense would need to be considered later.

Mr. Newman recalled that the weights of the various currencies in the valuation of the SDR were based primarily on the value of the members' exports, but also on the amount of official holdings of the currency. If the Kiekens-Prader approach were adopted, because the euro was not yet held in any country's reserves, it would appear logical to assume that the weight would go down even though the exports shares happened to come out the same. Therefore, a different weight might be needed.

The Treasurer noted that there were cross holdings of deutsche marks and French francs within the euro area partners at the moment and outside the euro area. Those holdings were falling quite sharply as various euroland countries were converting out of deutsche marks and French francs into something else in order that the reserves did not disappear when they become euros on January 1, 1999. But there would likely still be holdings of euro by noneuro-area members in place of their deutsche marks, French francs, and other currencies in the euro area. Thus, the eventual precise financial variable weight remained unclear; however, he would agree with Mr. Newman that, intuitively at the moment, it would likely be smaller. That was one reason why the staff had proposed resetting the next review of the valuation, in order to see how those holdings, among other things, would evolve.

Mr. Toribio considered that there was no difference between the two approaches, as, at present, the weights of the French franc and the deutsche mark in the SDR basket would remain intact. That was one reason why he believed that the review of the method determining the composition of the SDR should not be postponed. An earlier date would permit the full consideration of any fundamental changes that might occur.

Mr. Newman said that he disagreed with Mr. Toribio. The Prader-Kiekens approach appeared to say that the weight for the euro was not the weight for Germany and France, but the weight of the whole euro area. While the figures might be similar at present, it would represent a substantial change in principle, because the weight of the euro in the SDR basket would be based on the trade of the 11 members of the euro area.

Mr. Hendrick said that he agreed with Mr. Newman, and he reiterated his support for the staff's proposal.

Mr. Lehmussaari said that he supported the views put forward in Mr. Kiekens and Mr. Prader's preliminary statement.

Mr. Lushin made the following statement:

> I share the staff's view that no changes should be made at this stage to the method of the SDR valuation. The simple substitution of the deutsche mark and the French franc by the euro is an explicit and robust way which ensures the continuity and consistency of the Fund's approach. At the same time, it requires minimum modifications to the existing rules and regulations. a similar approach should be applied to the SDR interest rate basket, given its identity with the SDR valuation basket. Specifically, I favor using national interest rate instruments in this basket.

Secondly, I agree with the rationale behind the staff's proposal to reset the five-year cycle for the revision of the SDR so as to coincide with the start of EMU. Such a resetting would allow enough time for the assessment of the role of the euro in the international financial system and for the development of the relative importance of currencies. However, we also agree that an earlier revision might be necessary if warranted by circumstances. This said, I support decisions 1 through 4 as suggested by the staff.

Mr. Houtman made the following statement:

I can fully associate myself with the preliminary statement on this subject by Messrs. Kiekens and Prader.

I would have a preference for sticking to the existing revision schedule of the valuation of the SDR. This will allow for a timely incorporation of the effects of the introduction of the euro on the international financial system. I do not think we should wait for a possible participation of the United Kingdom in the EMU. Anyway, an extension of the review period by three years seems unnecessary long to me. This implies that I cannot support the proposed decision number 1.

For the record, proposed decision numbers 2, 3 and 4 have my full support.

Finally, I would like to reiterate my support for the use of Euribor as the appropriate reference interest rate, a solution which I understand now has the support from the French and German authorities, as well as for the use of the daily dollar exchange rate as announced by the ECSB. It seems logical to use a common interest rate when using a common currency. In the case of Germany, the interbank rate will be replaced by Euribor anyway. While I acknowledge that in the French case this interbank rate does not reflect a government-backed instrument, I do not fear that the use of Euribor would have a significant upward effect on the SDR interest rate. I suspect the difference would only be marginal, also given the fact that it only concerns the French part of the basket, which amounts to 10 percent. However, I do not have very strong feelings on this issue. If there remain serious doubts concerning the appropriateness of Euribor for the interest rate calculation, I would suggest that the staff further investigate this issue, in consultation with the European monetary authorities, before we take a final decision. This decision might also include a certain transition period, which would allow us to get somewhat more certainty on these factual issues.

Mr. Brooke made the following statement:

For the record, my authorities have no problem in accepting the staff's proposed decisions in all four counts. In responding to the issues raised by Mr. Kiekens and Mr. Prader, in general, we would not view any of these issues to be of fundamental importance that we would resist to the final degree his suggestions, but we do have some concerns with them and generally would favor the staff's position in each case.

Of the three, I think the one issue which we feel most strongly about would be the issue that we have been discussing, and that is the choice of the interest rate to be used. I think I would agree here with Mr. Newman and other speakers that if we were to adopt the EURIBOR, this would in some sense be a fundamental change in our approach, in the sense that, even with the existing approach for Germany, using the interbank rate, at least that is wholly representative of German bank dealings, whereas the EURIBOR, as we have already heard from the Treasurer, would be representative of 57 banks from 15 different countries, as I understand it. So that would be wider than just the EMU countries, which would be representing the euro.

So I think one should not take this step lightly. There are some quite deep conceptual issues to consider before we were to adopt that approach. If we were to revisit this issue, I certainly would like the staff to look at the possibility of the euro LIBOR, which as I understand it at least would be representative of the EMU countries, rather than extending beyond the EMU countries. More generally, as I said, I think I would prefer the staff's proposal, as set out in the paper, to continue to use the French treasury bill rate and the German interbank rate.

On the exchange rate quotes to be used, I think I would agree strongly with Mr. Donecker's remarks that the most important consideration here would be to take the quote from the most liquid market, and that to the extent possible all of the exchange rates should be taken from the same market at the same time. Not surprisingly, therefore, my authorities would favor the existing practice of using the quotes from the London market.

Mr. Giustiniani, speaking on behalf of Mr. Grilli, made the following statement:

Let me say something on the SDR valuation. Let me here express my disagreement with the views of Ms. Lissakers and Mr. Newman. They emphasize that the current rules on SDR valuation and interest rates are country-centered rather than currency-based, reflecting the basic orientation of the Articles of Agreement. I may be wrong, but if I understood correctly, in determining the currency weights in the SDR baskets, the value of exports of the member countries issuing these currencies is used as a proxy of the importance of these currencies in international trade and payments. Furthermore, always in determining the currency weights, we do not refer to the reserves of the member countries issuing these currencies but to the amounts of these currencies held as reserves by all Fund members. Therefore, I believe that SDR valuations tend to reflect the relative international position of the currencies of which it is composed. Hence, the mere replacement of the French franc and the deutsche mark already implies a significant underweighting of the euro in the new valuation basket. a postponement of the next valuation of the SDR basket would exacerbate this underrepresentation of the euro.

As far as the issue of the interest rates, we support the use of the EURIBOR. The use of the three-month rate bills of national governments cannot be regarded as representative of the area as a whole.

There seems to be a fundamental problem on what is the exact interpretation of the SDR, and whether this is, as the U.S. chair mentioned, a country centered rather than currency based asset. For that reason, also, we certainly support the substitution of the French franc and the deutsche mark with the euro, but we certainly cannot support the postponement of the next valuation of the SDR basket. Consequently, we can also discuss this issue more thoroughly in that case. Therefore, for the reasons expressed above, we support the use of EURIBOR, since in our view the use of the three-month bills of national governments cannot be regarded as representative of the area as a whole. As for the euro-U.S. dollar reference exchange rate, I would be inclined to support Mr. Donecker, but I recognize the preference expressed also by the ECB, and I wonder whether during this interim period in which we have to settle a lot of the issues between the two institutions this might be one of those.

The Acting Chairman asked the Treasurer what the deadline was for a decision.

The Treasurer responded that, on the valuation and interest rate baskets, a press release was normally issued announcing to the market the decision of the Board 90 days before any change was made. Therefore, ideally, a press release of the Board's decision should be made at the end of September or the beginning of October 1998.

Mr. Taylor made the following statement:

I think the exchange between Mr. Newman and the Treasurer makes it clear that there is a fundamental distinction between the staff and the Kiekens/Prader approach. I think we should probably move to the Kiekens/Prader approach around the year 2001, which is when the next review should be, in my view. If that adjustment were made, I could support all decisions as proposed.

Mr. Belay made the following statement:

The staff paper provides helpful discussion of the issues stemming from the formation of the European Economic and Monetary Union (EMU) for the valuation of the SDR and the determination of the SDR interest rate. On the issues proposed for decision, we would support the staff's recommendation that no changes be made at this stage to the method of SDR valuation, as a result of the introduction of the euro on January 1, 1999. We would also support the proposal to replace the deutsche mark and the French franc by the euro in the SDR basket. As regards the timing of the next revision, we can go along with those Directors who favor an earlier period than that suggested by the staff. We concur with the staff that the introduction of the euro will have an impact on the current method of valuing the SDR in the future, making it necessary to carry out a comprehensive review of the method.

Mr. Kpetigo made the following statement:

Based on the information provided in the staff paper, I can agree that no change be made at this stage to the method of SDR valuation as a consequence of the introduction of the euro and that the deutsche mark and the French franc could be automatically replaced by the euro. I also share the views expressed by Mr. Kiekens and Mr. Prader regarding interest rate valuation. Concerning the period of the next review of the SDR basket, I support the staff proposal.

Mr. Ogushi stated that, on the valuation of the SDR and SDR interest rate, he supported the proposal in the staff paper. In terms of the timing of the next revision, he would prefer a shorter interval.

Mr. Karunasena said that he supported the proposed decisions 2, 3, and 4. With regard to decision 1, he would prefer to have a review earlier than the year 2004.

Mr. Fremann noted that, as Mr. Milleron had stated during the previous agenda item, his authorities favored the approach outlined by Mr. Kiekens and Mr. Prader. It was clear from the staff report that, at least by 2004, the Fund was moving to a currency approach. Thus, using the EURIBOR rate would anticipate that.

Mr. Hendrick noted that, in contrast to Mr. Fremann's statement, the staff report stated that the French authorities considered that the three-month rate of French government obligations continued to be the most appropriate rate for inclusion in the SDR interest rate basket.

Mr. Fremann explained that there had been a misunderstanding on the part of his authorities at the time that the Treasurer's Department had asked about the three-month T-bills in France. While the instrument was representative in the case of France, if the Fund were moving to a currency-based approach, as Mr. Newman was questioning, it would be difficult to say that the French T-bill was representative of the euro. That was the reason he supported his euro-area colleagues' position to move to the EURIBOR.

Mr. Newman wondered whether the Kiekens-Prader approach would require an 85 percent Board majority rather than a 70 percent majority, as it involved a change in the valuation method.

The Treasurer responded that the General Counsel would address Mr. Newman's question specifically, but it would appear that, because there would be only a four currency basket, an 85 percent majority would be required. As the staff had followed the country-based approach, rather than the currency-based approach, it was determined that a 70 percent majority was required.

Mr. Fremann noted that the staff had suggested postponing the discussion on the weight of the euro in the SDR basket until 2004 in order to allow for sufficient time to analyze the relative importance of the euro in the world economy and financial system. Basically, that was a currency approach, and it was unclear why the staff considered that the country-based approach would be maintained.

The Treasurer responded that the Fund was not moving to a currency-based approach, if Mr. Kiekens and Mr. Prader's approach could be summarized in that way. The staff had suggested resetting the cycle to a new five-year period for three reasons, which were outlined in the staff report. The first reason was to see what happened in the event that new members joined EMU and to see what decisions would take place after 2001. The second reason was to keep the current cycle which meant, essentially, that the staff would be presenting a paper on the reweighting system with only one year's experience of EMU—that is, 1999—because the Board would need to discuss any changes in the method of valuation by September 2000 based on data from mid-2000, not a significant amount of time. The third reason was related to the issue of the current structure of the SDR valuation basket—namely, exports on one side plus foreign holdings of the currency on the other. It would seem that more time was needed to see how the euro was developing as a major reserve currency in the sense of holdings by noneuro-area countries. Clearly, the matter was in the hands of the Board, but the next time one seriously looked at the valuation of the SDR, a number of complex issues would likely arise, including the Kiekens-Prader approach compared with the country currency approach.

Mr. Donecker clarified his position that, currently, the Fund should not deviate from the staff proposal of a country-based approach which required only a 70 percent majority. It was clear that the other approach entailed complex issues that needed more time to discuss, and, until that time, the staff proposal should be adopted. However, he reiterated that the timing of the next review should not be changed.

The Acting Chairman asked the Secretary to indicate the tallies on the four draft decisions.

The Secretary remarked that decision No. 1 did not have the required majority; thus the present review date of January 1, 2001 would remain. On decision No. 2, there was near unanimity in favor. Decision No. 4 also had the required majority. Decision No. 3—as revised by the Kiekens-Prader proposal—required a 70 percent majority, because of the change in the reference rate; that majority was not present. The Board was almost equally divided on the issue. He asked the Treasurer to comment on the consequences of that situation vis-à-vis Rule O-1 and T-1(c).

The Treasurer clarified that, as proposed in the staff report, the draft decision required a 50 percent majority. However, an insertion of the EURIBOR into Rule O-1 and Rule T-1(c) would appear to require a 70 percent majority. If that majority were not present, then the Board would have to come to some decision at an early date, if only to leave the basket unchanged.

The Secretary asked the General Counsel to explain what would happen to the existing rule if the required majority to change it were not available.

The General Counsel responded that, if the proposed change was not amended, the current interest rate formula would continue in effect. In other words, the existing rules and regulations would remain unchanged until the Board decided to change them by a 70 percent majority. If the Board agreed that the French franc and deutsche mark would be replaced effective January 1, 1999 by the euro, it was only a question of interpretation to decide that, in the existing rules and regulations, the words "deutsche mark" and "French franc" would be replaced by "euro." That did not appear to be controversial. What was controversial was whether, in addition, the interest rate, which was based on the French treasury bills and the German rates based on the interbank rate, should be changed to the EURIBOR. For that, the required 70 percent majority was not present. Therefore, the present formula continued as under the current rules.

Mr. Brooke noted that, if no decision were reached at the current meeting, it would be sensible to continue the current practice.

Mr. Giustiniani asked the General Counsel to comment on Mr. Newman's remarks that, in the consideration of the composition of the SDR, countries and not the currencies were considered. He believed that the currency was the more relevant consideration.

The General Counsel responded that, for the time being, the formula adopted by the Board was based on countries. The currencies of the five countries specified in the decision constituted the SDR basket. Therefore, if the Board wished to move to a currency-based basket with, for example, four currencies, that would constitute a change and not an interpretation of the existing decision. A change in the method of valuation would require a majority of 70 percent, unless it were regarded as a change in the principle of valuation or as a fundamental change in the application of the principle in effect.

Mr. Prader asked the staff to analyze the differences between the staff proposal and the proposal he had made with Mr. Kiekens. Also, perhaps some consultation between the staff and the European Central Bank on the issue should be undertaken. It was surprising that the staff had not considered such issues more carefully before presenting their proposal, as the introduction of the euro had been planned for some time.

After further brief discussion, the Acting Chairman concluded that, because the Board would not take a decision on the timing of the review, the current review scheduled for before 2001 would remain. The Board had agreed to maintain a five-country approach to the valuation of the SDR. Also, because the Kiekens-Prader proposal to use the EURIBOR rate did not have the required 70 percent support, the current practice of using the French treasury bill rate and the German interbank rate would continue.

The General Counsel explained that, pursuant to the Acting Chairman's conclusion, in Rule O-1, where there was the list of currencies that constituted the SDR basket with the respective weights, the words "deutsche mark" would be replaced by "euro as the currency of Germany" with the same weight, and below instead of "French franc" there would be "euro as the currency of France" with the same weight. Then in Rule T-1(c), where there were the interest rates, there would be the same substitution; instead of "deutsche mark" there would be "euro as the currency of Germany" and the three-month interbank deposit rate in Germany, because that had not been changed, and instead of "French franc" there would be "euro as the currency of France" and the three-month rate for treasury bills as again that had not been changed.

The Executive Board took the following decisions:

SDR Valuation Basket—Decision No. 11073-(95/92) G/S—Amendment

With effect on January 1, 1999, references in Decision No. 11073-(95/92) G/S, September 25, 1995 to the deutsche mark and the French franc shall be replaced by references to the euro as the currency of France and Germany, respectively. (SM/98/221, 9/1/98)

Decision No. 11801-(98/101) G/S, adopted
September 21, 1998

SDR Valuation—Amendment to Rules O-1 and T-1(c)

With effect on January 1, 1999, references in Rule O-1 and T-1(c) to the deutsche mark and the French franc shall be replaced by references to the euro as the currency of Germany and France, respectively. (SM/98/221, 9/1/98)

Decision No.11802-(98/101) G/S, adopted
September 21, 1998

SDR Valuation Basket—Guidelines for Conversion into Currency Amounts of Euro of Currency Amounts of Deutsche Mark and French Franc

The Fund notes that with the introduction of the euro on January 1, 1999, the currency amounts of the deutsche mark and the French franc in the SDR valuation basket will be automatically replaced by the euro as the currency of Germany and France respectively, and decides that such conversion shall be made in accordance with the principles set out in the guidelines for the calculation of the currency amounts in the SDR valuation basket established by Decision No. 8160-(85/186) G/S, adopted December 23, 1985. (SM/98/221, 9/1/98)

Decision No. 11803-(98/101) G/S, adopted
September 21, 1998

DECISION TAKEN SINCE PREVIOUS BOARD MEETING

The following decision was adopted by the Executive Board without meeting in the period between EBM/98/100 (9/18/98) and EBM/98/101 (9/21/98).

3. RULES AND REGULATIONS AMENDED SINCE 1997 ANNUAL MEETING

The Executive Board approves the letter to the Chairman of the Board of Governors submitting for review by the Governors the texts of amendments to the Rules and Regulations adopted since the 1997 Annual Meeting and the proposed resolution for the Board of Governors, as set forth in EBD/98/93 (9/15/98).

Adopted September 18, 1998

APPROVAL: January 24, 2000

SHAILENDRA J. ANJARIA
Secretary