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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 94/85

10:00 a.m., September 15, 1994

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Executive Board Attendance

M. Camdessus, Chairman
S. Fischer, First Deputy Managing Director
A. D. Ouattara, Deputy Managing Director

Executive Directors

M. Al-Jasser

H. Evans
K. P. Geethakrishnan
J. E. Ismael
D. Kaeser
A. Kafka

G. Lanciotti
K. Lissakers
R. Marino
H. Mesaki
A. Mirakhor

G. A. Posthumus

S. Schoenberg
A. S. Shaalan
D. E. Smee
E. L. Waterman

A. G. Zoccali

Alternate Executive Directors

A. A. Al-Tuwaijri
M. Sirat J. Bergo
J. Dorrington

K.-T. Hetrakul

A. V. Mozhin
J. Prader
N. Coumbis

B. S. Dlamini

B. A. Sarr, Temporary

Wei B.

L. Van Houtven, Secretary and Counsellor
C. Clarke, Assistant

Also Present

Central Asia Department: O. J. Evans. External Relations Department: S. J. Anjaria, Director; P.-M. Falcone. Legal Department: F. Gianviti, General Counsel; W. E. Holder, Deputy General Counsel; R. H. Munzberg, Deputy General Counsel; J. L. Hagan Jr. Middle Eastern Department: A. Jbili. Policy Development and Review Department: J. T. Boorman, Director; T. Leddy, Deputy Director; S. B. Creane, A. K. McGuirk, M. Tareen. Research Department: M. Mussa, Economic Counsellor and Director; R. A. Feldman, P. Isard. Secretary's Department: J. Boughton, A. Mountford. Treasurer's Department: D. Williams, Treasurer; G. Wittich, Deputy Treasurer; J. C. Berrigan, J. E. Blalock, J. C. Corr, L. U. Ecevit, R. H. Floyd, D. Gupta, H. G. Jepsen, D. K. Kar, A. Muttardy, O. Roncesvalles, T. M. Tran. Office of the Managing Director: S. Sugisaki, Special Advisor to the Managing Director; G. R. Saunders, Personal Assistant to the Managing Director. Advisors to Executive Directors: B. Andersen, M. C. B. Arraes, R. F. Cippa, S. K. Fayyad, T. K. Gaspard, R. Kannan, Y. Margoninsky, M. F. Melhem, P. A. Merino, M. J. Mojarad, T. Oya, B. A. Sarr, J. R. Suárez. Assistants to Executive Directors: S. Al-Huseini, J. M. Burdiel, A. G. Cathcart, J. A. Costa, D. Daco, D. Desruelle, G. El-Masry, A. Galicia, O. Himani, G. H. Huisman, K. J. Langdon, F. Moss, S. Narube, S. Rouai, A. Sighvatsson, V. Verjbitski, R. Von Kleist, S. Vori, Wang Y.

1. ACCESS TO FUND RESOURCES AND ALLOCATION OF SDRS - DRAFT REPORT TO INTERIM COMMITTEE; AND RELATED ISSUES

The Executive Directors continued from the previous meeting (EBM/94/83, 9/12/94) their consideration of a draft report of the Executive Directors to the Interim Committee on access to Fund resources and an allocation of SDRs on the basis of a revised text (SM/94/205, Rev. 1, 9/14/94). They also had before them an earlier version of the draft report (SM/94/205, 8/1/94); a memorandum on alternative wording proposed by a group of Executive Directors (EBD/94/146, 8/25/94); a staff paper on a draft fourth amendment of the Articles of Agreement (SM/94/216, 8/10/94) and an alternative draft amendment based on a proposal by two Executive Directors (SM/94/216, Sup. 1, 9/8/94); staff papers on illustrative calculations of an SDR allocation (SM/94/152, 6/17/94; Sup. 1, 7/5/94; and SM/94/206, 8/1/94); and statements by the Managing Director on access limits, SDRs, and cofinancing trust accounts (BUFF/94/66, 7/1/94; and BUFF/94/71, 7/25/94).

The Chairman noted that a proposal had been submitted the previous day by a group of Executive Directors (see Annex). The proposal had been received too late in the day, however, to be incorporated in the current version of the draft report to the Interim Committee. He suggested that Mr. Al-Jasser begin the discussion by introducing the new proposal.

Mr. Al-Jasser stated that the proposal that he had sponsored was not his own but a joint proposal of 11 Executive Directors, the group of Directors traditionally referred to as the Group of Nine (G-9). The proposal was the product of a long discussion by the group to see whether it could find a way to allay the concerns of some other Directors and to contribute constructively to breaking the impasse on the SDR issue in the runup to the Interim Committee meeting in Madrid. The group had taken note of the attempts of the Managing Director and of Ms. Lissakers and Mr. Evans to arrive at a solution that would not necessarily satisfy everyone but that everyone could live with.

As explained in the September 14 memorandum circulated by the group to Executive Directors, the centerpiece of the G-9 proposal was its emphasis on the issue of an equity correction, Mr. Al-Jasser remarked. However, the proposal also took into account the need to expedite that process and the process of extending the systemic transformation facility (STF) and raising access limits. In order to achieve those goals in an expeditious way, it had been recognized that all members of the group would have to compromise on either the wording or nomenclature used to describe the equity correction process. The group was also willing to consider, if it proved necessary to reach a compromise, the reinstitution of the reconstitution requirement.

Inevitably, perhaps, the precise language of the proposal was somewhat unclear in some areas, but he was confident that the spirit of the proposal had been conveyed clearly, Mr. Al-Jasser commented. Indeed, the proposal was very much the product of an intensive dialogue among individual Directors, acting in their capacity as Executive Directors of the Board

rather than as representatives of their respective countries and ministers, to further the process of preparing a report to the Interim Committee. With that in mind, it was to be hoped that the G-9 proposal would be viewed as a constructive step in moving the process forward.

The Chairman remarked that he, too, was confident that Directors would view the G-9 proposal in a constructive light.

Ms. Lissakers said that it was clear from both Mr. Al-Jasser's introductory remarks and the language of the September 14 memorandum that the G-9 proposal had been presented in the spirit of compromise, and as an effort to narrow the divisions that had marked the debate thus far. In that sense, she welcomed the proposal.

On the structure of the proposal, Ms. Lissakers commented, it was her understanding that the G-9 had proposed that an up-front portion of the equity allocation, equivalent to 10 percent of total quotas, be agreed under the existing Articles but on the basis of the equity issue. She wondered whether such an approach would be consistent with the existing Articles, which stated clearly that all decisions with respect to the allocation and cancellation of SDRs must be aimed at meeting a long-term global need.

Mr. Al-Jasser said that it might be useful to elaborate on the thinking of the G-9 on the issue raised by Ms. Lissakers. Indeed, most members of the group had raised the issue during the preparation of the proposal, but there had been a feeling among the group that its efforts should not be bogged down in the technical issues associated with the language of the Articles. The group was aware of that difficulty, and that was why it had wished to emphasize the equity issue. Given that starting point, he hoped that the legal language used would emphasize the equity aspect and the fact that, in order to expedite the process, a starting point must be agreed. He hoped that the Directors would not become bogged down in the precise language.

Ms. Lissakers commented that Mr. Al-Jasser's clear statement had greatly advanced the debate, in that it appeared that there was now a substantial majority in agreement that the main issue was the equity one, and that the main outstanding question was simply how to address that issue in a manner that was consistent with the Articles. That had been her position all along--the only way one could address the equity issue was through an amendment of the Articles.

The Chairman said that he wondered whether Ms. Lissakers agreed with the sense of the method favored by Mr. Al-Jasser--to expedite the process with an up-front immediate allocation.

Ms. Lissakers responded that she did not accept that aspect of the proposal. She was saying merely that, at the least, the Directors seemed to have agreed on the objective, if not on the method for reaching it.

The Chairman commented that, as he understood it, the G-9 Directors had not, through their current proposal, renounced the existence of a global need. They were on record as believing that the global need existed and a general allocation was necessary, and, in order to help their colleagues, they were ready to flag the problem of equity and to expedite a rapid solution to the problem under discussion.

Mr. Al-Jasser said that the Chairman's understanding was correct. There was a saying that delayed justice was no justice. Similarly, greatly delayed equity might not be equitable. It was in that spirit that the G-9 Directors were trying to avoid all the mine fields along the road to reaching a compromise in the days leading up to the Annual Meetings in Madrid.

Mr. Sirat remarked that, as Ms. Lissakers had suggested, it was difficult to disconnect the method from the aim by agreeing that the aim was equity and then discussing the method to attain it. Otherwise, the nature of the debate would be slightly changed.

Mr. Posthumus said that he wondered whether it was possible to have an advance general allocation based on an amendment that had not yet been approved.

Mr. Smee noted that the Managing Director had suggested a general allocation of SDR 20 billion, equivalent to 13.8 percent of quotas, although he had used the word "initial," instead of "general," in describing the allocation under the G-9 proposal. One could say exactly the same thing by mentioning a general allocation of SDR 14.5 billion, equivalent to 10 percent of quota. Whatever words were used, there was in fact no difference: under whatever name might be used, the proposal was for a general allocation. As he understood it, one would be broadening the definition of global liquidity need by including whatever might be the basis for the first general allocation of SDR 14.5 billion.

The Chairman remarked that some called it a "general allocation," others a "minimum allocation," and still others an "immediate allocation." Everyone was talking about the same issue, but using different names.

Mr. Smee said that it was wrong to suggest that there was some similarity across all three proposals currently under discussion--that there were only niggling differences between them. The proposals by the Managing Director and the G-9 used the current Articles to justify an allocation of SDR 20 billion and SDR 14.5 billion, respectively, based on a global liquidity need under Article XVIII. The Evans/Lissakers proposal would require an amendment of the Articles.

The Chairman said that, under his proposal, it was clear that a global liquidity need was thought to exist, which would permit, under the current Articles, an immediate allocation. He saw considerable merit in that argument. The weakness of the alternative method was that the required

amendment of the Articles would take two years or more and would run the risk of not being approved by the necessary majority, thus leaving the interested countries, including those in pressing need of SDRs, with no assistance after having waited several years in the hope of receiving it. It was because of that major risk that Directors should consider the possible avenues that would facilitate reaching a consensus on a package, including an immediate allocation.

Mr. Evans stated that he agreed with Mr. Smee: there was a major difference between an allocation based on a global need in accordance with the existing Articles, and an allocation that required a change in the Articles and did not invoke the global need criterion. That difference must be borne in mind. It seemed clear that the only way in which there could be an up-front allocation of whatever amount was through the invocation of the global need criterion.

Ms. Lissakers said that, of the three proposals on the table, two were different ways in which to address the equity issue--the approach favored by Mr. Evans and herself and the G-9 proposal--both of which addressed the equity issue but through two different methods. The third proposal, by the Managing Director, was for a general allocation based on the global need criterion. She looked forward to the staff's comments on the legality of the G-9's approach to the equity issue.

Mr. Mesaki welcomed the G-9's initiative to expedite an agreement on SDRs and appreciated the spirit of compromise in which it was made. However, he had two concerns about it. First, while the proposal said that Directors had strived to avoid the definitional problem raised by some members, the up-front allocation had to be made under the current Articles and, therefore, would be regarded as a general allocation based on a finding of global need. In that respect, he did not believe that the proposal would go far toward resolving the crucial, contentious issue of global need. Second, as had been emphasized during the previous Board discussion on the issues, his authorities found it reasonable to conclude that the Fund should make a special, equity allocation as soon as possible. From that standpoint, the new proposal might discourage incentives to accelerate ratification of an amendment of the Articles in those countries that had participated in all previous SDR allocations, because the 10 percent allocation was proposed to be made at an early stage. Therefore, his authorities wished to stick with the Evans/Lissakers proposal.

Mr. Kaeser noted that, in addition to the equity issue, there was a major difference in the various proposals, namely, the amount of SDRs to be allocated--SDR 36 billion according to the Managing Director, SDR 16 billion under the Evans/Lissakers proposal, and SDR 30.5 billion under the G-9 proposal. He wondered whether agreement could not be reached on a single figure, closer to the one suggested by the G-9.

The Chairman responded that the amount of SDRs he had proposed--

SDR 36 billion--was based on the precise objective of maintaining the amount of SDRs in the system at the average of the past 20 years. As the Fund had an undertaking to make the SDR the main reserve asset of the system, the allocation should at least maintain that average.

Mr. Marino said that it was important to bear in mind the facts of the case. The Directors were clearly stuck on the issue of a general allocation or some other allocation, and a large majority of the Board favored a general allocation. In addition, the Board wished to react expeditiously to the challenges facing the Fund, and to that end the Interim Committee had given the Board a mandate to use all the instruments at the Board's disposal. There was also a general desire to restore the role of the SDR in the international monetary system. The G-9 proposal was not perfectly transparent, but it was a compromise proposal. The few Directors who were still concerned about the global need and general allocation issues should show some flexibility and admit to the advantage that the G-9 proposal would have in terms of making an immediate response to the needs of many member countries.

Ms. Lissakers commented that the proposal she favored included an allocation of SDR 12 billion, and she had indicated a willingness to go up to SDR 16 billion. She did not agree with the Managing Director that there should be some presumption of a target of a certain ratio of SDRs to world reserves.

The Chairman noted the undertaking in the Articles that, at some unspecified time, the SDR should become the main reserve asset of the system. As Managing Director, he felt obliged to take that undertaking into account in his proposal, and, therefore, it would be difficult for him to propose anything that would reduce the average proportion of SDRs.

Ms. Lissakers remarked that the subject of the present discussion was the report from the Board to the Interim Committee. The Board had not engaged in any debate on making the SDR the leading reserve asset. Hence, there was no basis for including any reference to that matter in the report. The report should describe the discussion on the equity problem.

The Chairman said that he agreed with Ms. Lissakers up to a point. His proposal had been discussed and had the support of a large majority of the Directors. While some Directors might remain unconvinced of the argument in favor of his proposal and of the existence of a global need, it should be mentioned in the report to the Interim Committee.

Mr. Evans said that he agreed with Ms. Lissakers. Given the various shifts that had taken place in the positions of Executive Directors, he wondered whether management still wished to maintain the proposal of SDR 36 billion.

The Chairman commented that the Board would not have completed its work before discussing the merits and weaknesses of all the proposals on the table, including his own.

Mr. Lanciotti remarked that the G-9 proposal could be considered a variant of the Managing Director's proposal. In addition, it represented a step toward a compromise, because it emphasized the equity issue and because it included a smaller allocation--SDR 30 billion instead of SDR 36 billion. Therefore, he wondered whether, in order to make the debate more effective, the Managing Director's proposal could be put aside in order to focus the discussion on two proposals that were closest to each other. Under that approach, the report would require substantial rewriting.

The Chairman said that he welcomed the G-9 proposal and the debate on it. However, at the present stage he was not convinced that his proposal had lost all its merit; in particular, it pursued objectives and it had a cleanness in its technical and legal approach that he tended to favor. Hence, while he, too, hoped to see an agreement emerge on one basis or another, he wished to keep his proposal on the table. The Board was unlikely to agree on the precise wording of an agreement at the present meeting, but he hoped that it would make progress on bridging the differences among the various proposals on the table.

Mr. Schoenberg stated that his comments were preliminary, as the latest proposal had only just become available. The draft report incorrectly stated that Directors were agreed on the existence of a global need and on the need to make the SDR the principal reserve asset in the international monetary system. Nor did he agree with the claim for the Evans/Lissakers proposal that it would remove the requirement for a finding of a global need to supplement reserves and to maintain the appropriate role of the SDR in world reserves and in Fund operations.

The Chairman commented that he hoped that Mr. Schoenberg would be in a position to take a position on the occasion of the next discussion on the draft report. Meanwhile, it was useful to debate the pros and cons of the various proposals on the table.

Mr. Kafka remarked that he was surprised by the implication that the Managing Director was not entitled to make suggestions to the Executive Board. The Managing Director had clearly spelled out his case for a general allocation, and a number of Directors, including himself, explicitly or implicitly supported that proposal. He was also surprised by Mr. Schoenberg's opposition to the reference in the draft report to the role of the SDR, which, after all, was stipulated in the Articles.

Mr. Schoenberg commented that his difficulty with the text in question was that it reflected only part of the relevant Articles. The other part had to do with the global need for an allocation; in the absence of a finding of a global need, the objective of making the SDR the principal reserve asset could not be achieved.

Mr. Kafka remarked that the objective of making the SDR the principal reserve asset was not associated in the Articles with a particular point in time. It was a general objective. He wondered whether Mr. Schoenberg believed that there could ever be a global need for an allocation.

Mr. Schoenberg said that he concurred with Mr. Kafka's interpretation, but, in the case under discussion, the objective for the SDR was used to justify a general allocation.

Mr. Kafka noted that page 7 of the latest draft contained what could be characterized as a timeless phrase--"keeping in mind the objective to make the SDR the principal reserve asset." The proposal did not go beyond the Articles.

Mr. Kaeser said that Article XVIII and Article VIII, Section 7 were equally binding for the Fund. The report to the Interim Committee should mention the difficulty in reconciling the Evans/Lissakers proposal, an equiproportional allocation under an amendment, with the provisions of Article VIII, Section 7.

Mr. Evans commented that the so-called Evans/Lissakers proposal had taken on some undesirable accretions in the draft report to the Interim Committee.

Mr. Al-Jasser said that he agreed with Mr. Kafka's point about the role of management in making proposals and his comments on timeless nature of the goal of making the SDR the principal reserve asset.

Mr. Smee commented that an amendment of the Articles seemed to be a feature of all the proposals under discussion; hence, the need for an eventual amendment was clear. Apparently the only difference between the proposals by the Managing Director and the G-9 was the size of the allocations. Hence, it might be helpful, in trying to reach a consensus, to focus on the G-9 and Evans/Lissakers proposals.

The Chairman noted that his proposal appeared to have the support of some 14 Directors, more than the other two proposals on the table. At the present stage, it would seem odd to remove from the table the proposal that enjoyed the strongest support.

Mr. Schoenberg said that he was certainly willing to mention the relevant Articles in the report, such as the statement on page 9 that "all Directors affirm the objective in the Articles of making the SDR the principal reserve asset of the international monetary system." However, it would not be appropriate to cite an allocation criterion of secondary importance and leave out the criterion of principal importance, namely, the global need.

Mr. Geethakrishnan remarked that the previous discussion showed that the G-9 Directors had been solidly behind the Managing Director's proposal.

They continued to give first preference to the Managing Director's proposal, but given the impasse in the discussions, the G-9 had proposed what they felt was a genuine compromise. In all likelihood, only one of the three proposals on the table would be found in the final report to the Interim Committee. Meanwhile, all three remained on the table. Alternatively, all three could be reported, or the Managing Director's proposal could be reported, with the full backing of the G-9.

It was important to recognize that the G-9 proposal differed from the Managing Director's proposal not only in terms of the absolute size of the allocation, but also because it fully addressed the equity problem, Mr. Geethakrishnan said. The Managing Director's proposal addressed that argument in a partial sense; some inequity would remain, as was the case with the Lissakers/Evans proposal. Furthermore, the G-9 proposal addressed the issue of reconstitution.

The General Counsel recalled that Mr. Posthumous had asked whether an advance allocation could be made on the equity basis before the amendment providing for such an allocation entered into force. The answer was that it would not be possible to give effect to an amendment that was not yet in force, and that perhaps never would enter into force; there was no assurance that an amendment would be adopted. Therefore, any allocation before the amendment was in force would have to be proposed to the Board of Governors on the basis of the present Articles; that was why the Managing Director's proposal explicitly referred to Article XVIII, which would require a finding of a long-term global need. Once that finding was made, then the objective of making the SDR the principal reserve asset became relevant in deciding whether or not an allocation would be proposed.

The G-9 proposal included a reference to equity, the General Counsel noted. Of course, that could be a guiding principle for the discussion, but obviously the first installment of the proposed allocation would be made pursuant to a resolution of the Board of Governors, not to an amendment. Therefore, Article XVIII would also apply in that case, and a finding of long-term global need would have to be made. The difference between the proposals was that the G-9's proposal placed greater emphasis on the concept of equity, but, legally, the conditions for an allocation would be the same.

Several Executive Directors had raised the question of the relationship between Article XVIII and the objective of making the SDR the principal reserve asset, and the qualitative aspect of the concept of principal reserve asset, the General Counsel continued. All those issues had been discussed in a Board paper circulated about one year ago that explained both the meaning of the concept of making the SDR the principal reserve asset and the relationship of that concept to the finding of long-term global need.

The Chairman said that he wondered what legal steps should be taken if there were to be a consensus around the G-9 proposal.

The General Counsel responded that substantively the sequence of events would be the same as those required to implement the Managing Director's proposal. The only difference would be presentational: the description of the G-9 proposal would emphasize the equity objective.

Mr. Evans said that the General Counsel's comments seemed to confirm that there were two elements in the G-9 proposal--a general allocation based first on an assessment of global need and, some time later, on an amendment of the Articles. Those elements were essentially the same as the Managing Director's proposal, except that the amount of the initial allocation was smaller under the G-9 proposal, and in presentational terms the G-9 proposal placed greater emphasis on the equity objective. A significant difference between the G-9 and the Managing Director's proposals, on the one hand, and the Evans/Lissakers proposal, on the other, was that the latter was a one-step procedure, not a two-step procedure.

It was useful to broaden the discussion to consider where to go from the present stage, Mr. Evans remarked. An interesting feature of the previous discussion was the attention given to the precedent that the Evans/Lissakers proposal would create for future allocations based on a global need, and an attempt had been made to meet the concerns in that area through suggested language for the communiqué. One of the most interesting suggestions was Mr. Autheman's idea that there could be language in the Articles themselves that would be neutral with respect to future allocations, but that would also reassure those who were most concerned about the precedent set by the type of scheme that he and Ms. Lissakers had suggested.

In considering what to do next, Mr. Evans said, Directors should bear in mind the lessons that some of them had tried to draw at the previous meeting, one of which was that a large number of Directors, representing a substantial portion of the voting power, were not prepared to go along with any general allocation. That conclusion had to be taken seriously in the context of the proposals on the table, and the report to the Interim Committee should mention it, along with the suggestion that there was not a necessary link between the SDR allocation and the suggested change in access. It would be welcome to reach an agreement, but one should not pretend that the link was essential.

The present discussion was not the occasion on which to make detailed comments on the drafting of the report, but a few comments on the text might be helpful, Mr. Evans considered. The section on SDRs was long and controversial and could usefully be much shorter by eliminating most of the argumentation, and it should present the facts of the various proposals. Table 1 incorrectly stated that a purpose of the Evans/Lissakers proposal was to maintain the appropriate role of the SDR in world reserves and in Fund operations. In addition, there was an incorrect reference to an amount of SDR 21.7 billion as being part of the proposal. Moreover, the table should include a clear reference to the phasing under the various proposals.

The Chairman suggested that time could be saved if the description of each proposal were to be written by the proponents themselves. The next draft of the report should be as concise as possible and cover the three proposals that has been made thus far.

Ms. Lissakers remarked that the figure of SDR 21.7 billion mentioned on page 14 was not a part of the Evans/Lissakers proposal. The Chairman's comments were somewhat worrying, as they seemed to imply that he had abandoned hope of reaching a consensus recommendation by the Board to the Interim Committee on at least the format of an SDR allocation as a component of the so-called package. The Chairman himself had made a compelling case for reaching such a consensus; it would not be possible for the Interim Committee to resolve the technical issues with which the Board had been grappling. If the Board could not close the gap at least on the format of an allocation, it should recommend to the Interim Committee that it consider the separate components of the package and not address the SDR issue. Directors seemed to be moving toward a compromise. As the General Counsel had noted, the equity proposal put forward by the G-9 Directors was not viable unless there was an acceptance of a global need, which did not have the support of the required majority. Hence, it seemed best to explore the possibility of the Evans/Lissakers version, or some variant thereof, to address the equity issue. A majority of the Board accepted the premise that whatever was done with respect to the SDR had to be based on the equity issue, not the global need issue.

Mr. Kafka considered that the Evans/Lissakers proposal would not maintain the integrity of the mechanism of the SDR allocation. In addition, while Mr. Evans opposed a link between STF access and the SDR allocation, others favored the link, which should be a factor in the report and in any compromise.

Mr. Geethakrishnan stated that he agreed with Mr. Kafka. During the previous discussion on the issues at hand, he had drawn attention to the fact that many Directors had clearly favored retaining the integrity of the Fund by making a general allocation. There seemed to be some doubt about whether those Directors had given up on that proposal. The G-9 proposal stated in part that the up-front portion of the equity allocation would coincide with the expeditious extension of the STF with an increase in access limits to more fully address the most immediate challenges. That position was not being abandoned. An up-front allocation would be a precondition for the approval of the entire package. Hence, while there might be a majority to block the up-front allocation, there was also a majority to block the rest of the package. Given those extreme positions, there was in effect nothing to report to the Interim Committee. It might be best not to submit a report, and to ask the Interim Committee to discuss the matter.

The Chairman said that he hoped that the Board would be able to avoid asking the Interim Committee in Madrid to call an exceptional meeting in November to tackle the issues under discussion.

Mr. Schoenberg commented that, to meet Mr. Kafka's concern regarding potential implications of an equity amendment for the integrity of the SDR system, he was prepared to accept an additional sentence in the Evans/Lissakers proposal saying in effect that the one-time action would be without precedent with respect to the rules governing the SDR system.

Ms. Lissakers said that the Evans/Lissakers proposal did not include any language about the integrity of the SDR, because, as Mr. Schoenberg had remarked, the suggested amendment would be a one-time amendment for a one-time allocation to deal with a specific anomaly. The amendment would be without prejudice to the existing Articles, which addressed fully the role of the SDR, and it would in no way be either prejudiced or diminished by the amendment required to meet the need for an allocation created by the sizable expansion of the Fund's membership.

It would be useful to have some clarification of Mr. Geethakrishnan's latest comments, Ms. Lissakers said. She had understood that the primary concern of the G-9 Directors was that the special equity allocation would somehow diminish the role of the SDR. To that end, she had been prepared to consider Mr. Autheman's proposal. However, in his latest remarks, Mr. Geethakrishnan seemed to be saying that the issue was not the role of the SDR or its viability, but whether there would be an up-front allocation. She wondered whether he was concerned about a matter of timing rather than any principle with respect to the SDR.

Mr. Geethakrishnan responded that he wished to protect the integrity of the Fund. Whatever language might be used for an amendment--however small it might be--of an Article to permit an up-front allocation, a precedent would certainly be set. Any statement that a precedent would not be set would not itself be credible. The present solution to the equity issue should not set the stage for a possible inequity later on. The G-9 proposal took the equity issue to its logical end and suggested that resolution of that issue be part of a package that included a general, traditional allocation at the outset. Hence, he would address the equity issue much more squarely than would the Evans/Lissakers proposal. The integrity of the Fund required that the equity issue be addressed together with an allocation that was made within the framework of the existing rules. There was no room in which to compromise on that point.

Mr. Posthumus noted that, with the exception of the up-front portion of an equity allocation in the G-9 proposal, that proposal was not much different from the Evans/Lissakers proposal.

Mr. Kafka said that he continued to be concerned that the Evans/Lissakers proposal would undermine the integrity of the allocation mechanism.

Mr. Kaeser commented that the problems facing the Directors might have arisen because of the failure to promote international surveillance and international liquidity according to Article VIII, Section 7. A number of

Directors believed that there was no global need for an allocation not because there were too many SDRs, but rather because there were too many reserves that were borrowed freely with no economic conditionality and outside international surveillance by more or less creditworthy countries in order to delay the adjustment process. The synopsis of the Evans/Lissakers proposal mentioned that one of the aims of the proposal was "to maintain the appropriate role of the SDR in world reserves and in Fund operations." He wondered whether that part of the proposal had originated with Mr. Evans and Ms. Lissakers.

The Chairman remarked that, as he understood it, Mr. Autheman had proposed an amendment to the Evans/Lissakers proposal. He wondered whether that understanding was correct, and whether Mr. Evans and Ms. Lissakers could accept the amendment.

Mr. Sirat recalled that, at the previous discussion, Mr. Autheman had said that the Evans/Lissakers proposal was not a compromise but rather a basis for discussion. In effect, the Evans/Lissakers proposal served to keep the SDR alive. That idea was reflected in the text that Mr. Kaeser had mentioned. Directors clearly attached importance to maintaining the integrity of the Fund, but a compromise was obviously needed. The General Counsel's comments on the legal aspects of the G-9 proposal suggested that, in effect, the proposals on the table were fig leaves, and the fig leaf in the form of the G-9 proposal might be more transparent than the fig leaf of the Evans/Lissakers proposal.

Mr. Evans said that, while he did not accept the precise text that Mr. Kaeser had mentioned, he was willing to consider other versions of it that might serve the same purpose.

Ms. Lissakers commented that she was willing to consider language that would explicitly say in effect that the purpose of ensuring the participation of all members in the SDR instrument was to preserve the SDR as a reserve asset.

Mr. Smee said that he welcomed Mr. Autheman's suggestion, which should help to meet the concern that the Evans/Lissakers proposal would somehow be inconsistent with the possibility of future general allocations based on global liquidity need. Instead of trying to state that the proposed solution of a one-off allocation would not set a precedent, it would be better to narrowly define the specific purpose it was designed to accomplish. The relevant text could state that the aim was to ensure that all members took part in the SDR system, which would have the effect of a reaffirmation of the role of the SDR and, therefore, of the system governing the SDR. It would be clear that the goal was to ensure that every country had the right to be a part of the SDR system.

Mr. Marino commented that, in legal terms, the Evans/Lissakers proposal looked like a two-track procedure involving an 8 percent general allocation and a topping up to 24 percent. To an outsider, it might have the air of a

purely legal device to justify an 8 percent general allocation and an equity amendment. The G-9 proposal was based on equity considerations but would make use of currently available instruments to reach the same final point at which the supporters of the Evans/Lissakers proposal were aiming. Most members--especially the newer members--would probably wish to have the allocation sooner rather than later and would favor equity in a global sense.

Mr. Bergo made the following statement:

I agree very much with Ms. Lissakers, not on the global need or the lack of it, but that we should continue to explore the common ground that has been found. We must probably accept that it is not possible at this stage to make all the ground a common one, but in what we do, we should not preclude that such an agreement might be reached in the future.

The inclusion of language in the Evans/Lissakers proposal along the lines suggested by Mr. Autheman could help ensure that such a future agreement, on what is not common ground now, is not precluded. It makes sense on its own--there is a need to maintain an appropriate role for the SDR. I have heard no one disagree with that. To the contrary, I have heard a number of Directors--including Ms. Lissakers--say very clearly that this is partly the purpose of the exercise.

I would not draw the connection between the STF and the SDR, but I note, and I suspect, that others do. However, I would find it extremely unfortunate if the end result should be a zero outcome on all accounts. That would not be a zero result for this institution, but rather a negative mark on the report card for all of us.

Mr. Al-Jasser considered that the wording in question, on maintaining the appropriate role of the SDR in world reserves and in Fund operations, was of less importance compared with the provisions of Article VIII, Section 7, and Article XXIII. In effect, that proposed extra language was merely restating the obvious in a weak manner and for no good reason. Hence, the proposal created major conceptual problems with respect to the integrity of the SDR and the Articles. If the intention was to allay concerns, the outcome was almost the opposite.

Mr. Geethakrishnan said that, as Mr. Al-Jasser had implied, the proposed wording change would not amount to even a fig leaf. The possibility of a regular allocation was enshrined in the Articles, but the fact of it was clearly being disguised in the form of a solution that would supposedly benefit all member countries through an amendment of the Articles. It was not helpful to suggest that an amendment to the Articles was necessary to make possible an allocation that was to benefit all members.

Mr. Mesaki said that Mr. Autheman's initiative was a welcome way in which to meet the concern about maintaining the integrity of the SDR. With that initiative, a consensus might be possible, as the substance of the G-9 proposal was not much different from substance of the Evans/Lissakers proposal.

Mr. Zoccali stated that he fully agreed that there was no global need for an allocation, not because there were too many SDRs, but rather because too many reserves were being borrowed freely without conditionality, which had a direct bearing on the effectiveness of Fund surveillance. In essence, the present discussion was aimed at trying to arrive at a clean technical conclusion based on a major distortion in the system. Mr. Smee had mentioned the need to find a common ground. The Board would not be fulfilling its mandate if it was unable to agree on a technical solution. The Articles already foresaw an alternative that also ensured that all members participated in the SDR system. That was the only way to ensure that all members participated. An amendment was by no means a 100 percent safeguard toward that end. If the amendment solution was pursued, even with the constructive language proposed by Mr. Autheman, the Board would be arriving at the unfortunate conclusion that, if there was no global need at present, then, for all practical circumstances, there would never be a global need in the absence of a worldwide depression. The differing views on the same principle made it necessary to arrive at a consensus on a package.

Ms. Lissakers said that she agreed with Mr. Zoccali that the Articles provided that members that had become participants after a basic period could receive an allocation, but new members could only actually receive SDRs if a new basic period had been triggered by a decision of the Board on the basis of a finding of global need. Hence, the finding of global need had to be a prior condition in order to accommodate new members. There was not the requisite support for the finding of global need. If Directors continued to argue about that point, then a compromise would not be possible.

The fig leaves issue was really a misrepresentation, as the supporters of the Evans/Lissakers proposal had nothing to hide, Ms. Lissakers continued. It seemed illogical to conclude that an amendment to permit all members to participate in the SDR system was somehow designed to weaken the SDR.

There appeared to be common ground and room for compromise, Ms. Lissakers considered. As Mr. Posthumus had pointed out, except for the issue of an up-front allocation, there was little difference between the G-9 and Evans/Lissakers proposals. The staff had noted that the G-9 proposal required a finding of global need, for which there was not the requisite support. Hence, that particular variant of the equity proposal was foreclosed and, for the purpose of seeking common ground, there was no point in further discussing it. The Board should discuss the possible common

ground and how to reach a consensus on a proposal, at least on the format, and, ideally, on the size as well.

Mr. Moss said that the Board should reach a consensus, and the G-9 proposal was constructive. In the Board's continuing horse-trading efforts on the SDR, it had all along been dealing with a special kind of horse: its genetic qualities were still hotly debated among the traders and, hence, it was impossible to establish a price for the animal. It would have been welcome if the Board could have cleared up at the present meeting the philosophical issue of whether there should be a general allocation up-front, a delayed general allocation mingled with a specific one, or a very special allocation containing a general element. Each type of allocation would have its proper set of motivations, yet they ultimately all revolved around the question of how to address the equity issue. The Evans/Lissakers proposal was a clear attempt to move in that direction, but it did not go quite far enough. The G-9 proposal aspired to address the equity issue fully, as Mr. Geethakrishnan had observed, but the way in which it tried to accomplish that aim was apparently not yet agreeable to some Directors.

There would be a few more opportunities to try to establish enough common ground for the Board's report to the Interim Committee on the SDR, but as time went on, it appeared likely that the Board would have to call in other horse-traders to work out both parts of an SDR deal: the presentational part, which included the timing element, and the quantity part, Mr. Moss continued. The horse traders belonging to the G-7 and G-9 stables were not the only traders in town, a point Mr. Kafka had made. In fact, the remaining traders were the ones representing 26 out of the 37 clients who had never owned a horse before. That observation should not be interpreted as a hint at yet another proposal, however. It was merely an invitation to all concerned to continue their discussion in order to bring the issue to a successful end sooner rather than later.

Mr. Kaeser said that he wondered whether it would be useful to explore the possibility of combining both the G-7 and G-9 proposals in such a way that the equiproportional part of the Evans/Lissakers proposal could be given up-front, together with a formal agreement to cancel it when the amendment came into force.

The General Counsel said that it was important to consider what form of agreement Mr. Kaeser had in mind. A gentlemen's agreement--which, of course, would not be enforceable--would be feasible. If Mr. Kaeser had in mind a legally enforceable agreement, then Mr. Kaeser's proposal would be highly problematic. If the amendment did not, after all, enter into force, then the power to cancel SDRs would be governed by the present Articles, under which SDRs could be canceled only if there was a finding that there was no longer a need for them to exist.

Mr. Posthumus noted that the G-9 Directors considered that the integrity of the general allocation was at stake. The idea of an equity allocation seemed to be accepted. At present, the disparity in

SDR allocations as a share of quotas was substantial; it would be reduced under the Evans/Lissakers proposal, which was put forward as a one-time proposal. Perhaps it could be made a permanent feature of the Articles, so that an allocation would be possible on the occasion of a new review of quotas to reduce the disparity gradually.

Mr. Sirat remarked that one of the main issues at hand was whether the Board could keep open the possibility of a future general allocation without approving one forthwith. He had favored a general allocation but had noted the strong opposition to it, and, therefore, his chair had suggested a possible compromise through the Evans/Lissakers proposal. Apparently a compromise was possible if Directors would agree that the amendment would not preclude any future general allocation based on Article XVII, and provided the amendment was, in effect, made so as to maintain the role of the SDR in world reserves.

Mr. Wei stated that an up-front allocation was at the core of the G-9 proposal and was therefore not negotiable.

Mr. Mirakhor commented that the G-9 proposal was meant to make a significant contribution toward reaching a compromise. It had not been easy for G-9 Directors to move away from their original position in favor of the Managing Director's proposal to allocate SDR 36 billion. The G-9 Directors had attempted to bring their proposal very close to the Evans/Lissakers proposal. It seemed likely that, in order to simplify the situation, the Managing Director's proposal should be dropped. It was important to bear in mind that the Articles stipulated that the SDR was the principal reserve asset, and any wording that did not do so would be a move away from reaffirming the integrity of SDRs under the Articles.

Ms. Lissakers considered that the difference between the Evans/Lissakers and G-9 proposals was greater than Mr. Mirakhor had suggested, in that the former would provide a topping up of SDRs by a certain amount, or a minimal allocation of a certain amount, but not both, as would be provided under the G-9 proposal. If the issue of a general allocation on the basis of global need was non-negotiable, then the Board should suggest that the Interim Committee address the issue of access and the extension of the STF on a stand-alone basis, and it should say that there was no consensus on an SDR allocation. The Board should either find a consensus on some sort of SDR allocation, or agree that a consensus could not be reached and recommend that the Interim Committee consider the access and STF issues on their own individual merit.

The Chairman remarked that the G-9 proposal usefully included the possibility of reintroducing a reconstitution requirement. He wondered whether other Directors were willing to support that idea.

Mr. Al-Jasser commented that the G-9 Directors had made a considerable effort to reach a compromise in the form of their new proposal. Indeed, even the Managing Director's proposal had initially not been seen as

sufficient by some G-9 Directors, who now realized the need to be pragmatic about the SDR allocation issues, including the concern about rekindling inflation and the wish to agree on an overall rationale for the allocation based on the need for an equity correction. The G-9 proposal did not mean that the G-9 Directors had given up their belief in the existence of a global need for an allocation. It had not been easy for the G-9 Directors to move away from their original position to the proposal now on the table, including a reconstitution requirement.

Mr. Kaeser considered that reconstitution should not be reintroduced.

Mr. Schoenberg remarked that a reconstitution requirement would of course affect the quality of the SDR as a reserve asset in that SDRs would be regarded as being available only temporarily; the SDR would not be seen as a full-fledged reserve asset. In addition, it would seem that a reconstitution requirement should be considered only in the event of a finding that there was an excess of international liquidity. There was an inherent conflict between a finding that there was a global need to allocate SDRs and a requirement to reconstitute SDRs. He doubted whether a proposal on reconstitution could be implemented.

Mr. Kafka considered that it was important to make the distinction between the need for reserves to hold and the possible need for reserves to spend. Liquidity to be held would not be compromised by a reconstitution requirement, and that was why it had been in place from the beginning of the SDR system.

Mr. Schoenberg commented that, presumably, countries would not consider the SDR an acceptable reserve asset if they could only hold it.

Mr. Kafka responded that a reconstitution requirement would not prevent a member using its SDRs in the event they had a need to use reserves.

The Director of the Research Department commented that, in considering the differences between the proposals on the table, it was useful to note that there was an analytical equivalence between the amendment under the Evans/Lissakers proposal, in terms of the distribution of SDRs that it would finally achieve, and the combination of a method three benchmark amendment and a general allocation--mathematically, the final outcome would be the same. There were obviously key differences between the two approaches, as Directors had noted. Under a general allocation plus a method three amendment--the essence of the Managing Director's new proposal and of the G-9 proposal--the general allocation would come into effect relatively quickly or could be phased, depending upon the decision with respect to the general allocation under Article XVIII. In contrast, the method three component would clearly depend on ratification in two senses: it would not come into effect until ratification was achieved; and should ratification fail for any reason, that component would not come into effect. In contrast with the Evans/Lissakers form of amendment, the G-9 solution would be

delayed and would either succeed or fail as a package; it would not be possible for part of it to succeed and part to fail.

Under the combination of a general allocation and a method three amendment, the general allocation would need to be justified under Article XVIII on the basis of a finding of long-term global need, the Director continued. The amendment of the Articles would be justified on the ground that the Board wished to amend the Articles because that action per se was seen as a good idea; the amendment per se would have nothing to do with global need. Presumably the report of the Executive Board to the Interim Committee and the Committee's communiqué should say something about the reason for seeking an amendment of the Articles. Therefore, it would be important to reach a consensus on the wording to be used for that purpose, even though it would not be included in the amendment of the Articles itself. There would obviously be interest in why the amendment was being sought, and, therefore, the report should provide some justification. There seemed to be fairly broad agreement that the issue of equity should figure prominently in such a justification.

The General Counsel commented that the justification for an amendment could be provided in three places: in the text of the amendment itself; in the Board of Governors' resolution proposing the amendment; or in the report of the Executive Board to the Board of Governors. If the justification were given in the text of the amendment itself, then the question would be asked why any justification was required in view of the justification in the enabling provision of Article XV, including the reference to the exercise of a power by the Executive Board and then the Board of Governors. When organs of the Fund had to make decisions, the criteria that had to guide their actions had to be specified, and the purpose of their actions had to be made explicit. In the present case, however, the initial allocation and subsequent allocations would be purely automatic; there would be no exercise of power by any organ of the Fund. Therefore, there would be no need to guide the actions by stating purposes and criteria. Hence, while it would be possible to include statements on purpose and justification, they were not really necessary in the case under consideration.

To the extent that justifications and purposes were thought to be useful, they might have an impact later with respect to the interpretation of the relevant provisions, the General Counsel continued. That was why, for example, there were difficulties with the finding of long-term global need. Therefore, if to the new provision for automatic allocations a sentence was added to the effect that the aim was to achieve fairness, one might question later whether the allocations alone were actually achieving fairness, and whether additional measures might not be needed to achieve the desired objective. In other words, a justification might not be needed and might open the door to future challenges with respect to the implementation of the provision containing the justification. A general principle of legislative drafting was that statutes should not include unnecessary provisions that could cause problems.

If the justification were included in the Board of Governors' resolution, then there would have to be a consensus, because the resolution would have to be adopted by all the Governors, the General Counsel commented. If the justification were placed in the Executive Board's report to the Interim Committee, the situation would be totally different, because the relevant provision could reflect the view of the majority; in other words, the justification could be mentioned even if there was a division of views among the Directors. Hence, it might be easier to agree to place the justification in the Board's report rather than elsewhere.

A question had been raised about the role of equity in the G-9 proposal, the General Counsel recalled. Some emphasis could be placed on that concept in the G-9 proposal. However, the proposal would have to be consistent with the present Articles. In practice, the Managing Director, under the relevant existing provisions, had to satisfy himself that the provisions of Article XVIII, Section 1(a)--concerning the finding of a long-term global need--were met. Accordingly, that finding would have to be made and then accepted by the Board of Governors; there was no way in which that finding could be ignored. Equity could be an additional consideration in support of a proposal, but it was not a substitute for the finding of long-term global need.

A question had also been raised about the apparent two-track approach under the Evans/Lissakers proposal, the General Counsel noted. Obviously, it would be odd to have a proposal that was consistent with the relevant provisions of the existing Articles but would nonetheless require an amendment. There would be nothing wrong in having an amendment the purpose of which could not be achieved under the present Articles. That would not constitute a circumvention of the Articles. However, the proposed amendment of the Articles did not raise the issue of circumvention.

It had been suggested by Mr. Posthumus that the equity concept might require taking one step further by having a permanent provision in the Articles to the effect that, whenever a quota increase took place, an adjustment would also be made in the SDR allocations, the General Counsel commented. The staff had been considering that issue, although it had not put forward a proposal. Two comments should be made in that connection. First, the proposal on the table was not to have a permanent equity feature built into the Articles, which would parallel the provision on allocations based on findings of long-term global need. As he understood it, the proposal in question was an ad hoc proposal made in view of the present circumstances. Second, if there were to be a permanent linkage between quota increases and SDR allocations, the nature of the discussions on quota increases would be totally transformed. The consequential SDR allocation would become relevant to the discussion on quota increases. Hitherto, the idea had been to separate the two discussions and to assess the merits of quota increases by themselves.

The Chairman commented that there was clearly a strong desire among Directors to provide the Interim Committee with a report on the basis of

which the Committee could make final recommendations. To that end, the staff would circulate shortly a revision of the proposed report by the Board. The present discussion had shown that the various groups of Directors would have to move away from their present positions and toward a compromise--which would require approval by an 85 percent majority--if the Board were to be able to and reach a consensus.

There seemed to be considerable common ground, the Chairman remarked. Everyone wished to maintain an appropriate role for the SDR, and there was a broad willingness to move forward along the line of an equity correction. To that end, Directors needed to overcome their difference of views on the issue of global need. Directors must make the effort to do so; if they did not, the Ministers would certainly have to do so in Madrid. The Ministers would recognize the importance of settling the equity issue, and they would recognize the wish of a large number of constituencies to implement a solution soon, in order to meet the need for an agreement as soon as possible. In that connection, they would also wish to avoid, if possible, having to go to their parliaments as a part of the implementation of an agreement.

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/94/84 (9/14/94) and EBM/94/85 (9/15/94).

2. EXECUTIVE DIRECTORS' OFFICES - TRAVEL TO CONFERENCES AND SEMINARS

The Executive Board approves the recommendations of the Committee on Executive Board Administrative Matters concerning travel of members of Executive Directors' offices to conferences and seminars as set forth in EBAM/94/152 (9/9/94).

Adopted September 14, 1994

3. APPROVAL OF MINUTES

The minutes of Executive Board Meeting 94/28 are approved.

APPROVAL: November 15, 1996

LEO VAN HOUTVEN
Secretary

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To: Executive Directors

September 14, 1994

From: M. Al-Jasser
K. Geethakrishnan
J. Ismael
A. Kafka
R. Marino
A. Mirakhor
L. Mwananshiku
C. Santos
S. Shaalan
M. Zhang
A. Zoccali

Subject: SDRs and the Package

The Madrid Annual Meetings are approaching and we need to conclude our deliberations over the package of measures to address the challenges facing the membership at this historical juncture.

It is therefore important that we transcend our semantical and definitional differences and try to reach a workable compromise that we all can live with. The proposals of the Managing Director and Ms. Lissakers and Mr. Evans have contributed positively to this process. It is in this spirit of compromise that we make the following proposal with the hope that it will generate the necessary consensus in the Executive Board.

Our proposal centers around the recognition that, at this juncture, the emphasis should be on an equity correction allocation of SDR. In this context, Ms. Lissakers and Mr. Evan's proposal was most helpful in that it envisages a two-step allocation. Our new proposal, which is quite a compromise from our initial position, is predicated on the need for a two-speed equity-based allocation. The first part is a modest 10% upfront allocation to all members to initiate the equity correction process. This upfront portion of the equity allocation shall coincide with the expeditious extension of the STF and an increase in the access limits to more fully address the most immediate challenges. The balance of the equity correction, however, will follow the ratification of the fourth amendment of the Articles to achieve a benchmark of 35.8% of quotas for all members. This way, we will have solved the issue of inequity for all members.

With this proposal, we have strived to avoid the definitional problem raised by some members while at the same time not prejudice the future role of the SDR in the international monetary system. It is our sincere hope that this spirit of compromise will be seen in the

light of our desire to break the impasse we find ourselves in on the eve of the Madrid meetings. As it stands, our proposal is a significant compromise from our previous aspirations in qualitative and quantitative terms.

In the same spirit of compromise, and in order to ensure the broadest possible support for this proposal, we are willing to consider the reinstitution of the reconstitution requirement. This should help allay the fears of those of us who are concerned about the possible inflationary consequences of an SDR allocation.

cc: Managing Director
Deputy Managing Directors
Mr. Gianviti
Mr. Boorman
Mr. Mussa
Mr. Williams

