January 30, 2006
Approval: 2/6/06

INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 05/94-1

10:00 a.m., November 7, 2005

1. The Multilateral Debt Relief Initiative (G-8 Proposal) and Its Implications for the Fund—Further Considerations—Supplemental Information; The Multilateral Debt Relief Initiative (G-8 Proposal) and Its Implications for the Fund—Further Considerations—Supplement on Financing Arrangements; Repayments to the Fund by 18 Completion Point HIPCs in the First Quarter of 2006

Documents: SM/05/353 and Supplement 1 and Supplement 2; and FO/DIS/05/127

Staff: Allen, PDR; Kuhn, FIN; Hagan, LEG

Length: 1 hour, 44 minutes

Executive Board Attendance

R. de Rato, Chairman
A. Krueger, First Deputy Managing Director

Executive Directors	Alternate Executive Directors
	A. Alazzaz (SA)
K. Bischofberger (GR)	G. Meissner (GR)
	B. Dumont (FF), Temporary
	M. Lundsager (UA)
	T. Miyoshi (JA), Temporary
	J. Prader (BE)
J. Kremers (NE)	
	P. Charleton (CO)
	P. Jenkins (CO), Temporary
	S. Rouai (MD), Temporary
	A. Herat (IN)
	R. Bannerji (IN), Temporary
	A. Lushin (RU)
P. Ngumbullu (AE)	P. Gakunu (AE)
	M. Stone (AU), Temporary
	A. Ismael (AF), Temporary
A. Sadun (IT)	
E. Loyo (BR)	R. Steiner (BR)
T. Scholar (UK)	A. Hauser (UK)
M. Schwartz (CE)	M. Dager (CE)
A.S. Shaalan (MI)	
J. Solheim (NO)	
	J. Silva-Ruete (AG)
	H. Ge (CC)
	J. Schaad (SZ), Temporary
	H. Ng (ST), Temporary

A. Linde, Acting Secretary
J. Morco, Assistant

Also Present
IBRD: L. Buntua, M. Koch, V. Nehru. African Department: B.V. Christensen, S. Gupta, T. Krueger, D. Nellor, R. Nord, M. Nowak. Asia and Pacific Department: T. Rumbaugh. External Relations Department: M. Bell, G. Bhatt, G. Ingham, S. Nardin. Fiscal Affairs Department: M. Verhoeven. Finance Department: C. Hemus, B. Keuppens, M. Kuhn, J. Lin, D. Ordoobadi, R. Price, A. Tweedie, N. Wagner. Legal Department: S. Hagan, Y. Liu, E. Mouysset, B. Steinki, R. Weeks-Brown. Middle East and Central Asian Department: A. Tahari. Office of Budget and Planning: P. Ganesh. Office of the Managing Director: O. Brekk, A. Kammer, L. Maldonado. Policy Development and Review Department: M. Allen,

P. Alonso-Gamo, A. Berg, T. Dorsey, M. Fisher, M. Guerguil, M. Hussain, H. Joly, R. Kincaid, M-H. Le Manchec, M. Plant, L. Redifer, M. Tareen. Research Department: J. Ostry, A. Spilimbergo, A. Subramanian. Secretary's Department: A. Blazejewski, P. Ramlogan. Western Hemisphere Department: P. Young. Senior Advisors to Executive Directors: G. Cipollone (IT), N. Conrado (CE), O. Hollensen (NO), J. Mafararikwa (AE), H. Mori (BR), R. N'Sonde (AF). Advisors to Executive Directors: A. Al Nassar (SA), A. Blazey (AU), C. Crelo (BE), J. Cuevas (AG), J. Haegeli (SZ), J. John (UA), J. Kwakye (MD), M. Lanz (SZ), H. Malothra (BE), F. Meyerhoefer (GR), S. Rottier (BE), J. Sipko (BE), D. Wang (CC), L. Whyte (UK).

1. THE MULTILATERAL DEBT RELIEF INITIATIVE (G-8 PROPOSAL) AND ITS IMPLICATIONS FOR THE FUND—FURTHER CONSIDERATIONS—SUPPLEMENTAL INFORMATION; THE MULTILATERAL DEBT RELIEF INITIATIVE (G-8 PROPOSAL) AND ITS IMPLICATIONS FOR THE FUND—FURTHER CONSIDERATIONS—SUPPLEMENT ON FINANCING ARRANGEMENTS; REPAYMENTS TO THE FUND BY 18 COMPLETION POINT HIPCS IN THE FIRST QUARTER OF 2006

Mr. Kiekens submitted the following statement:

The staff proposals on the design and financing of the Fund's part in the Multilateral Debt Relief Initiative (MDRI) seem to be in line with the understanding reached in the IMFC in September. Successfully implementing this initiative will be a challenging task for the beneficiary countries, the donors and the Fund.

Fair and equal treatment of countries is a fundamental principle that must be adhered to for international cooperation to be effective and lasting. The discussions during the past few months have made possible some progress in this respect. Nonetheless, for many of us, the outcome falls short of what would be desirable. Several countries that are just as poor as those that are eligible, for debt relief, and with comparable needs and comparable quality of policies, remain excluded. The criterion to determine the amount of assistance, namely the amount of debt to the Fund at the cut-off date, is much narrower than the concept of "balance of payments need" that must guide the use of the resources of the Special Disbursement Account for the benefit of low-income members (see commentary on the proposed second amendment to the Articles of Agreement, page 47).

There still remains scope for the donor community to correct these shortcomings in the MDRI. In response to a call from the U.N. Secretary General, the World Bank has started to evaluate the (financial) needs of countries for reaching the MDGs. In his report on the Fund's Medium-Term Strategy, the Managing Director proposed that the Fund should report—frankly—about these assessments of the World Bank on the achievability of the MDGs under realistic macroeconomic scenarios and financing envelopes. Donors should use these assessments by the Bank and the Fund to allocate their grants and assistance according to the needs of countries and the quality of their policies. The Fund should use its influence with donors to ensure that ODA is allocated as much as possible according to the objective needs, thus enhancing fairness and cohesiveness in the international community.

Debt relief and scaling-up aid flows do not suffice to reach sustainable growth, significantly reduce poverty and reach the MDGs. As Peter Heller has explained so well in a recent article in Finance and Development (September 2005, page 9), debt relief (and more aid) is just the start of a complex set of decisions and tough choices. The recipient countries themselves must "own" and take charge of their development strategy. But, the effectiveness of the ODA should be closely monitored. As staff has said, countries receiving debt relief under the MDRI would benefit from continued close cooperation with the Fund. Adequate level of cooperation goes beyond the obligations under Article IV of the Articles of Agreement. I suggest that the staff clarify in greater detail the nature of these "post-debt relief consultations", and the related requirements for the country. When requesting assistance under the MDRI, countries should confirm to the Fund, in a letter of intent, their commitment to participate in such post-debt relief consultations during the period of debt service covered by the MDRI-assistance.

The financing of the debt cancellation will, over time, imply a significant weakening of the Fund's net income position. The Fund should, therefore, manage its resources even more carefully than before. The Fund should avoid accepting mandates that would risk overstretching available budget resources. Member countries should financially support the Fund with fair burden sharing among them. This will allow the Fund to continue performing its important responsibilities with the necessary high quality.

I would like to raise some specific points.

It would not be acceptable to reduce the threshold of US$380, income per capita, that determines eligibility for debt relief financed with SDA resources.

Could the staff clarify what interest rate it assumes for calculating the subsidy resources needed for continued PRGF operations?

The staff calculates that SDR 210 million additional donor contributions are needed to subsidies the interim PRGF loans. Could the G-8 Directors confirm and clarify their authorities' commitment to provide this amount of SDR 210 million as promised at the Gleneagles Summit?

Could the G-8 Directors confirm and clarify their authorities' commitment to finance the cost of HIPC assistance for the additional countries that would be included in the list of HIPCs under the sunset clause review?

Paragraph 26 of the staff paper clarifies that amending the PRGF lending instrument to allow restitution of resources from the subsidy account to donors requires (a) a decision by the Fund adopted by a majority of the votes cast and (b) consent of all contributors to the subsidy account.

Can the staff clarify whether, in the past, resources of the subsidy account have ever been restituted to donors? I remain unconvinced that such restitutions are possible under the trust instrument, except if the trust is being terminated. However, since the Fund is also a contributor to the subsidy account with SDA resources, consent of the Fund in this capacity would certainly be required. Such a decision by the Fund requires an 85 percent majority of the voting power.

Mr. Misra and Mr. Srinivas submitted the following statement:

We welcome the revised paper providing fresh contours for implementing the G-8 proposal on debt cancellation. There is support for further debt relief by IMF as part of a larger international initiative for debt relief for low income countries. However we note that the Executive Board of the IDA has asked IDA staff to prepare a follow up paper that would assess in greater detail the financial and operational issues involved in implementation of the proposal. The status of discussions at the AfDF are not mentioned. Given that IDA and AfDF hold a dominant share in the debt proposed to be canceled could staff give a preliminary timeline on the status of discussions in these institutions.

The G-8 debt cancellation proposal would preserve the resources in the Reserve account of the PRGF Trust but fully drain the resources in the Special Disbursement Account (SDA) and significantly reduce the balance of the PRGF subsidy account. SDR 0.47 billion of the SDA is being moved to the PRGF subsidy account. A higher per capita income threshold could have been arrived at if the SDA were to be fully used for debt relief alone. This would deprive several similarly placed countries from similar treatment despite availability of resources. The burden of finding subsidy resources for the PRGF Trust has shifted from bilateral donors to the Fund resources itself.

In the discussion on the Exogenous Shocks Facility (ESF), the G-8 has recommended a fungible use of the PRGF Subsidy Account on the grounds that existing level of bilateral contributions contained therein, would adequately allow for an early activation of the ESF. If indeed there are sufficient resources in the PRGF subsidy account, then the first preference should be given to provide debt relief to all PRGF eligible IDA only countries. It cannot be that the PRGF subsidy account has enough resources to fund the ESF, but does not have any resources to fund widening of the debt relief proposal. A degree of consistency is required on the issue.

The G-8's commitments for debt relief has not been set in a specific time horizon. In past discussions, the G-8 commitment was to provide on a fair burden share basis up to US$350–500 million for the interim PRGF, and on the same basis, to cover the cost of debt relief for countries that may enter the HIPC process based on end 2004 debt burdens. Present projections indicate that an additional resource mobilization of SDR 210 million in subsidy contributions would suffice to fully implement the proposal. Despite G-8 contribution, the Fund has to find resources not only for the MDRI but also for future PRGF subsidy operations. It is now proposed that debt relief to non HIPCs below the threshold will be borne by SDA resources. Could the G-8 confirm their authorities commitment to finance the cost of debt relief for non HIPC beneficiaries of

MDRI. On the protracted arrears cases, special provisions to expedite their inclusion in the MDRI are necessary. Of the options being proposed limited grandfathering is preferable to the rights accumulation program. The case for graded debt relief has not been included. Could staff clarify.

On conditionality, although the last discussion did not see any degree of consensus the preferred view is for upfront and irrevocable debt relief to provide a predictable stream of resources. We could go with this view. Entry conditionality for completion point HIPCs and non-HIPCs who will benefit from MDRI should be similar. Assessment for determining compatibility of macroeconomic policies with maintaining fiscal sustainability and low inflation have long been part of Fund's work and is acceptable entry conditionality. For assessment of satisfactory implementation of PRSP, staff has been preparing JSANs on the Annual PRSP reports and these could be used to determine satisfactory implementation of PRSPs. A PRSP that has not been updated for five years, should be considered as outdated and the country would have to resume the PRS process. A lot of work has been done on strengthening Public Expenditure Management (PEM) Systems under the HIPC Initiative and an assessment of PEM systems should be an integral part of entry conditionality. For countries whose performance has lapsed in any of the above three criteria, clear evidence of improvement should be required before delivery of additional debt relief. These include
(a) macroeconomic performance criterion for a duration of six months
(b) satisfactory implementation of PRS for one year and (c) commensurate corrective action if lapse is of structural nature. The Fund and the Bank could explore ways to collaborate on a framework for monitoring and reporting on the use of resources freed by debt cancellation. Such monitoring on the Fund side could be included in Article IV discussions.

The cost of the proposal has come down following the use of differentiated country by country completion point dates as effective debt relief dates for 17 pre-completion point countries for whom the benefit of the proposal stands significantly reduced as they would be making significant repayments to the Fund before they reach completion point. The reduction in future demand for PRGF resources remains notional at this stage as the debt relief by the Fund is only part of a larger international initiative. It has been proposed that proceeds from the early repayment of the PRGF Trust loans in the context of debt stock relief under HIPC Initiative and MDRI could be used to make an early repayment to PRGF Trust lenders. There is a rationale for continued Fund lending to post completion point HIPCs depending on their financing needs. If there are shortfalls in PRGF lending then the G-8 commitments not to undermine the Fund's lending capacity must be fulfilled.

We note that the use of SDA corpus under the G-8 proposal would not have an immediate effect on the GRA balance sheet or the GRA income position. The option of a transfer of the SDA corpus to the GRA or transfer to the GRA of investment income of the SDA would be permanently removed.

Legal Considerations

Uniformity of Treatment

The Legal Counsel has clarified that the principle of uniformity of treatment is applicable among the developing countries to whom SDA assistance may be provided and a per capita income threshold can be used. On September 21, we had said that the G-8 proposal is given a semblance of equity by designing a threshold of US$380 to conform to 'uniformity' and 'capacity to pay' by bringing two countries from IDA only LICs into the fold. This we feel is a conceptual manipulation, legally indefensible and at best tenuous as it leaves behind several IDA only LICs with similar economic status while covering HIPCs with higher income levels. A further component i.e., alternate scenarios with income thresholds of 270, 380 and 400 have been evolved but HIPC debt cancellation out of PRGF subsidy resources and thereafter replenishment of the PRGF Trust by transfer from SDA is a jugglery that IMF itself will consider a poor banking practice. It would increase the Fund's share in subsidy resources from the present 14 percent to nearly 50 percent. Mitigating the all or nothing consequences of a single threshold by providing graded debt relief to some LICs above the threshold has not been examined.

Protected Provisions—Section IX of the PRGF Trust Instrument

The Legal Counsel has opined that the Fund has never interpreted Section IX of the PRGF Trust as meaning that the protected provisions could never be amended. Only unilateral amendment by Fund is prohibited and the protected provisions can be amended with consent of all third party contributors.

There are several aspects of this interpretation that we are not comfortable with. Firstly the Legal Counsel is indicating that the PRGF Trust betrays a lack of careful drafting in that there are differences between the amendment provisions of the PRGF Trust Instrument and the PRGF-HIPC Trust Instrument while it was not intended to be. The edifice of the PRGF Trust is built upon the concepts crystallized in the Purposes and the role of the Fund has been outlined in Section VII. Exercise of unlimited power of the Fund are limited by the provisions of Section IX. If by a majority decision we were to destroy the avowed purpose of Section IX and inter alia Section VII of the PRGF Trust, the decision would be looked upon as a measuring rod of the extent of the amending power of the Fund's Executive Board.

The Legal Counsel says that the protected provisions of the PRGF Trust Instrument have been amended in the past. However we note that the amendments were for, transfer of resources from reserve account to subsidy account, and not for transfer from subsidy account to donors. Could the Legal Counsel give us a citation whether amendment to the protected provision has covered restitution to donors beyond the principle of uniformity of treatment.

The validity of each new amendment must be judged on its own merits. We fear that amending the PRGF Trust to specifically identify countries to provide debt cancellation on a non uniform basis would be damaging the basic structure of the Trust and therefore outside the amending power of the Fund. The consequence of this exclusion would be a limitation on the power of the Fund to breach principles of uniformity of treatment. If we were to use the limited amending power conferred upon us, we would be converting it into an absolute and unlimited power and it would have been meaningless to have placed a limitation on the original power of amendment. Uniformity of treatment remains mandatory and we cannot alter the basic structure of the PRGF Trust by amendment of Section IX.

Mr. Solheim and Mr. Hollensen submitted the following statement:

We thank staff for the informative papers which have been produced for this meeting. We welcome the progress on the MDRI and look forward to an early approval of the arrangements enabling debt relief as soon as possible.

We reiterate our support for setting a per capita threshold of US$380 to meet the principle of uniformity of treatment. Moreover, we support the qualification criteria for post-completion-point HIPCs and entry conditionality for non-HIPCs. We will underline the need for including governance and transparency issues in the public expenditure management systems.

We emphasize the need for remedial actions before delivery of debt relief in cases where countries have had lapses in their performance with respect to meeting these criteria. Prudent debt management is also important.

Proper and transparent post-debt relief monitoring is needed. We underline especially the importance of debt sustainability, implementation of PRS and good governance. It is essential that lapses in performance are addressed thoroughly by Fund staff in order to ensure that debt cancellation achieves its fullest potential.

The debt relief will be financed in part by using the PRGF subsidy contributions. It is important that the PRGF instrument is sufficiently equipped with resources to meet projected future demand. The principles of additionality and fair burden sharing are of utmost importance. Countries in our constituency have already contributed significantly to the PRGF Trust Fund. We look forward to contributions from other donor countries. We stress the importance of the G-8 countries delivering on their commitments. In view of such contributions, some countries within our constituency will consider a contribution.

We look forward to consider the paper envisaged by staff with further analysis on possible alternatives to deal with the arrears clearance and debt relief to the protracted arrears cases. Staff has already discussed a couple of preliminary options and considerations under the headings Limited Grandfathering and

Modified RAP Approach in Annex 1. We would appreciate further comments by staff on other possible options, including the possible implications of extending the cut-off date for the three protracted arrears cases.

Mr. Ngumbullu and Mr. Mafararikwa submitted the following statement:

The staff should be commended for a quick and thorough analysis of the implications of the Multilateral Debt Relief Initiative (MDRI) for the Fund and the financing arrangements that are necessary for the Initiative to become effective. We particularly appreciate the priority being accorded to approval of this Initiative before the end of the year, given that a list of completion point HIPCs distributed by staff, with obligations falling due to the Fund beginning January 2006 could benefit. We will focus our comments on these issues for discussion.

Uniformity of Treatment Requirements

The staff paper adequately addresses issues of uniformity of treatment under the G-8 proposal and we concur that a per capita income threshold is a relatively neutral indicator for choosing potential beneficiaries. However, the challenge is to choose a threshold of per capita income that cover all the HIPCs as targeted by the G-8, while allowing those other non-HIPCs that meet the same per capita income criterion to benefit from the MDRI. It appears the US$380 threshold comes close to meeting the G-8 objective. This criterion will allow both the 35 HIPCs as well as, for reasons of equality of treatment, two non-HIPCs to benefit from the common pool of the Special Disbursement Account (SDA) resources in the context of implementing the MDRI debt relief using the financing modalities proposed by staff. Having said this, some heavily indebted countries will still be left out by this threshold and we welcome suggestions made by staff to mobilize bilateral contribution to provide some debt relief for these countries.

Qualification Criteria for Post-Completion Point HIPCs

As we have stated before on this issue, a reinstatement of conditionality, including a Fund arrangement for post-completion point HIPCs to benefit from MDRI would be counter-productive. Nevertheless, we acknowledge that at any point in time, it is in the interest of any country to have satisfactory macroeconomic performance, good public expenditure management systems, policies and strategies to reduce poverty. It is important to check whether these areas have not deteriorated since the completion point. We therefore support the conditions set out in paragraph 11 for post-HIPCs as they are in the best interest of the countries themselves. In the event that these conditions have seriously deteriorated since the completion point, it is reasonable to allow time for corrective action before delivering additional debt relief.

Criteria for Inclusion of Non-HIPCs

Broadly speaking, non-HIPCs could be comparable to post-completion point HIPCs and should therefore not be subjected to the same conditionality as pre-completion point HIPCs. We therefore concur that the three entry conditionality outlined for post-HIPCs should also be applied to non-HIPCs. However, some of the generalization in the staff report needs to be considered more carefully.

(i) In the case of post-completion point HIPCs, the staff suggests a delay in MDRI debt relief delivery if the conditions set-out in paragraph 15 of EBS/05/353 Supplement 1 have deteriorated since the completion point. However, in the case of non-HIPCs, it is not clear what will be the way forward if those same conditions are not satisfactorily met; will the staff limit themselves to proposing remedial action or debt relief will be delayed until those remedial actions are implemented. We welcome staff clarification.

(ii) The PRSP should not always be the gauge for poverty reduction efforts. Non-HIPCs may not have a I-PRSP or full PRSP in the standard format known in the BWIs, but could have very strong poverty reduction efforts ongoing under alternative domestic frameworks. In some of such countries, mounting efforts to produce I-PRSP or PRSPs could be a major effort that, depending on country circumstances, could strain limited administrative capacity for them to quickly benefit from MDRI. The Fund should show flexibility by not insisting on a standard PSRP process but should instead seek to strengthen existing domestic frameworks to ensure that debt relief is used to advance the cause of poverty reduction.

(iii) The staff paper indicates that low debt ratios in non-HIPCs signals relatively sounder economic management policies. While we agree that in the final analysis, the quality of policies matter, the conclusion in the staff paper requires closer analysis on a case by case basis. Debt ratios are a product of a country's starting point and the policies pursued thereafter. Some countries may have started without any debt and therefore low debt ratios, yet the policies being pursued could result in high debt ratios down the road, hence the need to look beyond the numbers. We welcome staff view on these observations.

Treatment of Protracted Arrears Cases

The G-8 made a commitment to extend MDRI to protracted arrears cases and to provide the resources for this purpose. In order to fulfill this commitment, we suggest that an exception be granted to the deadline and cut-off date under the MDRI to enable these countries to qualify. We suggest a simple procedure that will not involve fundamental changes to our current policy for clearing arrears, considering that we will be discussing some of these cases soon, unlike the proposal of staff in Annex 1 of the paper. Our major concern remains that the protracted arrears cases in question are also post-conflict countries where a peace dividend is long awaited and its translation into economic well-being of the population will contribute to long-term social, economic and political stability, hence the importance of substantial up-front resources for human rehabilitation, economic growth, employment creation and poverty reduction. Our call still remains valid for innovative mechanisms to clear arrears for some of the more complicated cases and to pave the way for the Fund and donors to provide new money as quickly as possible as some of these cases will be coming to the Board for discussion soon. We therefore welcome the commitment of the G-8 to ensure the debt overhang of these countries is dealt with.

Post-Debt-Relief Monitoring

It is important to monitor developments on macroeconomic policies and poverty reduction following the delivery of MDRI in the context of surveillance or other Fund signaling. The Fund should stand ready to provide technical assistance where it is needed.

Timing of the Implementation of the MDRI

As we have mentioned earlier, there is expectation out there that countries will start benefiting beginning January 2006. We urge the international community to adopt the necessary mechanisms and financing arrangements to unroll this Initiative.

Collaboration with the World Bank

Finally, as under the HIPC Initiative, collaboration with the World Bank and other institutions remains important, even though the financing arrangements for the Fund are different. We welcome staff clarification on what implication there is to the World Bank in particular, for the decisions of the Fund related to the eligibility criteria especially for post HIPCs and other related matters.

Mr. Silva-Ruete and Mr. Cuevas submitted the following statement:

We thank the staff for the set of informative papers, which allow us to discuss the implementation of G-8 proposal. The Multilateral Debt Relief Initiative (MDRI) would be an important instrument for the G-8 debt cancellation proposal to become effective.

Uniformity of Treatment

In SM /05/353 the staff states that two “entry” criteria have been used to limit developing countries’ eligibility or qualification to receive balance of payments assistance from SDA resources on concessional terms: (i) per capita income, and (ii) nature and extent of the balance of payments problem. According to this provision, we understand that a country must accomplish both criteria at the same time in order to access to SDA resources. Therefore, the inclusion of non-HIPC countries in the MDRI is not clear, even if they fulfill the per capita income criteria. Moreover, the Fund has specific criteria to determine if a country is HIPC or not. We would appreciate an additional clarification on this issue.

Qualification Criteria for Post-Completion-Point HIPCs

We support the three criteria to qualify for the MDRI for post-completion-point HIPCs: satisfactory macroeconomic performance, satisfactory implementation of poverty reduction strategy (PRS), and sustained improvements in public expenditure management. However, further flexibility is needed in their assessment. In this regard, when a country with an ongoing arrangement with the Fund completes its reviews, it is unnecessary that the staff evaluates if the criteria was fulfilled. Indeed, a program is endorsed by the Executive Board because the macroeconomic performance has been at least satisfactory and structural targets under the program have been observed. One of these structural targets, in most cases, is related to improvement of public expenditure management system.

We agree that remedial actions would be needed prior to the delivery of MDRI debt relief in case of lapses of performance in any of the three criteria mentioned above. Nevertheless, once again, more flexibility is crucial since current economic conditions could differ from when the PRS was envisaged. For instance, if the current growth is lower than projected due to exogenous shock, the country could face balance of payments difficulties and problems to finance the fiscal deficit. In this situation, the debt relief could be crucial for the country; however, completing remedial actions could be lengthy since they would imply a strong adjustment that requires political support.

Conditionality for non-HIPCs

We agree that the entry conditionality for non-HIPCs should be similar to the criteria applied to post-completion-point HIPCs. However, to require that a non-HIPC member have a poverty reduction strategy in place seems excessive. An assessment to determine if the implementation of the PRS was satisfactory, as in the case of post-completion-point HIPCs is sufficient. We would appreciate the staff’s comments on this issue.

Post-Debt Relief Monitoring

The main objective is that the G-8 Proposal (through the implementation of the MDRI) becomes effective until end-2005. An update to the Board before the Spring or Annual Meetings on the status of the debt relief is basically a formality, albeit it would help in decision-making if problems arise during the implementation process.

The proposal that staff reports for Article IV consultations and program reviews provide country-specific information on the use of additional resources provided by debt relief would be inconsistent with the staff recommendation of delivering a full stock relief. In addition, in the document SM/05/284 the staff doubts on the effectiveness of the monitoring stating "Another issues is weather it is feasible to monitor the use of the resources freed by debt cancellation given the fungibility of funds. Experience with assessments of public expenditure management systems shows the difficulty of establishing a one-to-one link between debt relief and specific government spending decisions, as well as judging how much the spending meaningfully contributes to poverty reduction." We wonder if there are enough resources (human, budget, and time) to carry out this monitoring, thus at this stage, we cannot support this issue.

Other Issues

We support the two staff's recommendations, that debt relief under the MDRI should allow the early repayment of the full stock of obligations, and that the early repayment of debtors' PRGF obligations should be accompanied by the early repayment of lenders' outstanding loans to the PRGF Trust, except for those lenders whose borrowing agreements provide loans at below-market interest rate. These recommendations would avoid to incur in administrative costs and risks associated with maintaining these obligations.

Finally, we would appreciate if the staff can elaborate a timetable that includes the sequence and the length of the next most important steps to implement the MDRI.

Mr. Kremers submitted the following statement:

I thank staff for the follow-up papers on the multilateral debt relief initiative (MDRI), which tackle a number of outstanding questions and issues raised at the previous Board meeting. This additional information provides sufficient basis to move forward in the process of actual decision-making.
I confirm my support for the general approach set out in the main paper and elaborated in the supplements, e.g., with regard to the US$380 per capita income threshold, the proposed conditionality for post-HIPCs and non-HIPCs and the proposed modalities for the funding and provision of debt relief and early repayment to lenders. I also subscribe to the procedures for remedial action and monitoring (both pre- and post-relief), under the assumption that the staff and the Board have discretion to delay debt relief in individual cases—e.g., to assess whether remedial actions in case of post-HIPCs entail a more permanent improvement of a country's policy performance, or in case a program review completed a while ago provides insufficient assurance of satisfactory performance for non-HIPCs. Staff's confirmation of this assumption would be appreciated.
Finally, I am open to considering specific modalities for the treatment of

protracted arrears cases in due course, building on the possible approaches set out in the annex.

However, four issues require further attention and/or clarification.

First, I note that protracted arrears cases and sunset HIPCs have not been included in the analysis of country coverage and costs. While this is understandable from the viewpoint of uncertainty and timing, it does hinder well-informed judgment on the MDRI. First, it leaves uncertainty about the total costs involved. Staff repeats the G-8 statement that donors are committed to provide the extra resources necessary to cover these costs, but at the same time such a discussion has yet to take place. Could staff indicate to what extent firm commitments have been given by countries? Second, it raises confusion about what earmarked resources would be used to cover these costs—i.e., SDA, current PRGF subsidies and/or additional donor resources. Do I understand correctly from staff's approach that in principle the financing and delivery of debt relief (both under the HIPC and MDR Initiatives) to the arrears and sunset cases will be dealt with separately, i.e., through a new account to be funded by new bilateral contributions? Could this lead to legal complications in case the SDA and earmarked subsidy resources are at some stage depleted, and sufficient donor resources at that stage have not been forthcoming to cover subsequent qualifying HIPC / MDRI cases—either from the 'current' or 'future' list? This question pertains in particular to sunset cases that would appear entitled to SDA resources for debt relief under the HIPC Initiative, but also under the MDRI if GDP per capita is below US$380.

Second, staff confirms that, even if discounting for the authorization of the use of remaining SDA resources for PRGF subsidy purposes, the initiative will lead to a SDR 0.21billion subsidy gap in the interim PRGF. Given the limitations of the G-8 commitment, the question remains how this gap is to be filled, and what the consequences will be if it is not filled.

Third, the staff paper sets out the necessary process of consultations with donors on requesting the initiative and amending the PRGF Trust Instrument. At the same time, the supplements leave aside interrelated issues of financing, i.e., regarding the subsidy gap in the interim PRGF, the costs of arrears and sunset cases and the overall financing need of the self-sustainable PRGF and ESF following the debt relief initiative. While I have sympathy for concerns of complexity, I think such a fragmented approach could well backfire, as many donors will not understand why the Fund would come back to them on several occasions for specific modifications and financing needs.

Thus, I would propose that, following the necessary MDRI decisions, the process of contacting bilateral contributors to the PRGF subsidy account is broadened to other potential donors and tackles the wider financing issues. This would enable the establishment of the ESF and secure sufficient PRGF/ESF financing for 2006-11, where donors could also be consulted on the use of the current subsidy account for both facilities—an option supported by many Directors. To that effect, the Board should have the opportunity to consider the MDRI draft decisions in conjunction with the ESF decisions as well as with an integrated assessment of overall PRGF / ESF financing needs—building on the September paper. The financial assessment would preferably also give more detail on the modalities and potential costs associated with the arrears and sunset cases. These could be flagged to donors to give a more transparent overall picture of the costs of the MDRI, but would not need specific follow-up at this stage.

Finally, I note that staff judges the impact of the full use of the SDA on the Fund's balance sheet as limited to the finding that it would reduce 'flexibility,' having no identified consequences, e.g., for the rate of charge. This staff judgment is reassuring and provides crucial ground for the Board to support the full use of the SDA. However, in light i.a. of the outstanding issues of the non-reimbursement of PRGF administrative costs and the mitigation of the off-market gold sale, a general modernization of Fund asset management will have to be considered at some stage, including using the annual income stream from an investment account replenished with the proceeds from a market sale of a small part of the Fund's gold

Mr. Ondo Mañe submitted the following statement:

We would like first of all to express our appreciation to management and staff for their quick response on this important issue as requested by the IMFC and this Board. The papers circulated for today's discussion address well the issues raised during previous Board meetings on the debt cancellation proposal or Multilateral Debt Relief Initiative (MDRI), and we thank staff for the supplementary information provided as well as their analysis regarding the implications for the Fund in the area of financing arrangements.

To address the issue of uniformity of treatment, we agree with the approach proposed by staff, namely the choice of a per capita income eligibility criterion of US$380, as it seems to fit closely the financial arrangements envisaged under the G-8 proposal. We also agree with this threshold as it would help to balance the use of resources in the SDA and in the PRGF Subsidy Account, as explained by the staff, in a way that minimizes the need for additional resources, while ensuring that the Fund will be able to continue its concessional lending to low-income countries.

On conditionality,

- for pre-completion point HIPCs, reaching the completion point should qualify them for debt relief under the HIPC Initiative and the MDRI;

- for post-completion-point members, we agree that continued satisfactory macroeconomic performance and satisfactory implementation of their PRS would qualify them for the MDRI. The staff has added one more condition for post-completion countries, that is "a determination that public management systems had not deteriorated since the completion point." In our view, the determination of satisfactory macroeconomic performance should be enough. Could staff explain what they mean by this condition, and how it will be implemented? We also do not think that a Fund arrangement should be a condition for benefiting from the MDRI. However, if a country's performance has lapsed, and remedial measures are needed, we would like to know in what context these measures would be implemented? Will it be under an SMP or other informal arrangement? Staff has mentioned Article IV Consultation as one vehicle for the remedial measures, but if a country had had a recent Article IV Consultation, does that mean it would have to wait a full year to know if it qualifies for MDRI? Staff comments will be appreciated. In any case, we think that once the remedial measures have been taken, the country should qualify immediately for MDRI. We would like to emphasize that there should not be additional conditionality beyond that of the HIPC Initiative.

As regards non-HIPCs, which are not in programs, we share the view that their lower debt ratios make them closer in circumstances to post-completion point HIPCs, and would thus qualify under the same conditions as post-completion point countries.

We agree broadly with the Post-Debt Relief Monitoring modalities in Section C of the staff report. However, we would emphasize that since the debt relief is being provided in the context of achieving the MDGs, the staff report should also include an assessment of the progress that the country is making towards reaching the MDGs, as well as the domestic and external constraints it is facing, and what additional resources are needed to achieve the MDGs.

We thank staff for the estimate of administrative costs. We find them reasonable and we are pleased to note that they can be broadly met within Fund's program and surveillance operations.

As regards the protracted arrears cases, specific modalities would have to be considered for them. The most pressing issue is to find a solution to their arrears, so that they can reach the completion point and benefit from the MDRI. We find both the limited grandfathering and the modified RAP approaches as described in the appendix as having lots of merit. However, as Mr. Ngumbullu and Mr. Mafararikwa note in their statement, the protracted arrears cases are also post-conflict countries. Therefore, it is important that innovative mechanisms be put in place to deal with these cases in an appropriate way. In this regard, we welcome the commitment of the G-8 to provide resources to deal with these countries' debt overhang.

On the delivery of debt relief, we strongly believe that it should be provided in full and at once, as soon as the country qualifies for such relief. This would also be consistent with the G-8 proposal. We also agree with the financing of the MDRI as described in Section B of SM/05/353 Supplement 2, and we support the amendment of existing decisions so that the MDRI can become effective before the end of the year. However, we have major concerns as regards staff's proposal on the transfer of the balance of SDR 0.47 billion to the PRGF Subsidy Account as outlined in the third bullet point of paragraph 15. Staff is proposing a transfer in steps of this amount. We think that the transfer should be made immediately and in full to ensure that there are adequate resources available to countries making use of the PRGF. Meeting the resource needs in case of shocks also call for a full and immediate transfer of this amount.

We look forward to the proposed draft decisions on the MDRI, as well as those related to the Exogenous Shocks Facility. As we have emphasized on numerous occasions, we see the PSI, the Exogenous Shocks Facility and the MDRI as a complete package aimed at helping low-income countries increase economic growth, reduce poverty, and meet the MDGs. At the same time, we would note that the G-8 requested reports on good governance, accountability and transparency in the beneficiary countries. Could staff indicate whether and when they will issue a paper on these topics and how these will be monitored? We think that such a paper should be issued preferably before the proposed decisions.

Finally, we would like to take this opportunity to thank countries that have indicated their intention to contribute resources to enable the MDRI and the ESF to become operational, and we appeal to countries that are in strong financial positions to support fully these initiatives.

Ms. Phang and Mr. Wesaratchakit submitted the following statement:

We thank staff for a set of informative papers and appreciate their efforts in coming up with the supplementary papers in a relatively short time. Nevertheless, we feel that Directors should have been given more time to thoroughly consider the implications of this important proposal. In light of the time constraints and tight schedules involved in coming up with a feasible and acceptable solution, we would like to reiterate our compliments expressed during the informal seminar in September that staff have made significant progress on the issues of uniformity of treatment and conditionality. However, we are of the view that some aspects of the financial arrangement still need to be clarified.

Uniformity of Treatment

We support staff's proposal to use a per capita income threshold of $380 as a cutoff point for countries that will benefit from the debt cancellation using the SDA resources. We agree with staff that this approach is consistent with the Fund's principle of uniformity of treatment stated in the Articles of Agreement.

We are of the view that the choice of US$380 or a higher per capita income cutoff is an appropriate eligibility threshold since US$380 only averages to about US$1 a day per capita. This is widely accepted by international developmental organizations as the poverty line threshold for extreme poverty, and thus, we would strongly oppose using an income cutoff anything below that as it would go against the true altruistic objective and spirit of the G-8 proposal to assist LICs achieve the MDGs. According to staff, the US$380 option will minimize the demand for additional contributions from donors, and thereby preserve the Fund's future financial capability to assist LICs while coming closest to the original framework of the G-8 proposal. We would also like to seek clarification from staff as to why the Board has to authorize the use of SDA resources for debt relief under the HIPC Initiative for all qualifying countries regardless of their per capita income level? From what we understand, SDA resources are only used to grant debt relief to countries below the US$380 per capita income level.

Conditionality

Although we would have preferred that debt relief is given in tranches (phased delivery approach) to safeguard and ensure that the freed-up resources will be utilized properly and productively in pursuit of achieving the MDGs, we are willing to go along with the proposal to grant full debt relief to eligible countries up-front so that they will be able to utilize the freed-up resources in a timely manner and the Fund's operations will be simpler. We are of the view that post-debt relief monitoring will be crucial in ensuring that the freed-up resources will be put to good use. As such, we urge staff to be rigorous in their post-debt relief monitoring and surveillance. We agree with staff that the post-completion-point HIPCs should be reassessed to ensure that their performance in three key completion point areas have not deteriorated, and that for countries whose performance has lapsed, remedial steps have to be taken. We would appreciate staff's comments on whether a time limit should also be set for countries to take remedial steps so as to provide incentives for early actions as well as to enable the Fund to complete its obligations without protracted delays. As for the non-HIPC cases, we welcome staff's recognition of their relatively sounder economic management policies and support the proposed use of similar conditions for the post-completion-point HIPCs.

Financial Arrangement

Under the proposed arrangement, staff estimate that additional resources of SDR 0.21 billion are needed to replenish the PRGF subsidy account so as to allow the full use of uncommitted interim PRGF loan resources. Whereas the main paper (SM/05/353, page 29, para 49) states clearly that these additional costs will come from the resource envelop of US$350-500 million pledged by the G-8, the supplementary paper (Supplement 1, page 4, para 6) merely indicates that new bilateral contributions are needed. We would appreciate staff's confirmation that the G-8 are committed to providing these additional resources.

We support the flexible approach in seeking consents from the 43 donors of the PRGF subsidy account. Those donors who agree with the amendment of the Trust are rightly given an option whether they consent to the use of their contribution to give debt relief to the higher-income HIPCs. Should eventual donors' consent to reallocate their contributions be less than the required resources, we would disagree with the use of the PRGF reserve account to replenish the subsidy account as this would curtail the future lending capacity of the self-sustained PRGF. We are of the view that the resource shortfall should come from additional external third-party sources/contributions.

With respect to the estimates of lending capacities of the interim and self-sustained PRGF, we take note that staff have assumed that the Board will continue to forgo the reimbursement of the PRGF administrative expenses to the GRA. While staff state in footnote 57 of the main paper that this non-reimbursement does not directly affect the rate of charge, it however has the effect of slowing down the accumulation of precautionary balances. This in reality can be considered as GRA borrowers indirectly financing some portion of the debt relief.

Finally, we agree with the early repayment of the full stock of eligible debt owed to the Fund by beneficiaries once they qualify for the relief as it would simplify Fund operations and incur lower costs. As for the pre-payment to PRGF Trust lenders, we support the principle of proportionality except when borrowing agreements are provided at below-market interest rates.

Mr. Oh and Mr. Murray submitted the following statement:

We thank the staff for the two supplementary papers aimed at moving the Board to a position where it can take formal decisions by the end of 2005 to implement the Multilateral Debt Relief Initiative (MDRI), as promised by the Managing Director at the recent IMFC meeting.

As set out at the Annual Meetings, this constituency fully supports the MDRI. We support the measures now recommended in the supplementary papers for implementation of the MDRI. Importantly, we support the approach of a per capita income threshold of US$380, to meet the Fund's uniformity of treatment guidelines. As set out in Table 1 of Supplement 1, this approach would minimize the need for additional donor contributions (at SDR 210 million), thereby maintaining the Fund's on-going concessional lending capacity. We note that these calculations do not include provision for extra resources for debt relief to the protracted arrears cases or to potential eligible countries under the HIPC extended sunset clause, in light of the G-8 Finance Ministers communiqué of June 16, 2005, and subsequent G-8 commitments on a fair burden-sharing basis.

We also support the qualifications criteria for post-completion point HIPCs and non-HIPCs as robust but also pragmatic. We agree that remedial actions should be required where there has been recent lapsed performance in the three criteria.

We also support the proposed modalities for post-debt relief monitoring. We agree that the design of appropriate fiscal and financing policies after debt relief should be a central element of policy discussions with beneficiary countries. It will be important for Fund-Bank staff to undertake robust debt sustainability analysis, and to undertake appropriate stress testing, and for Fund staff to explain DSA concerns to country authorities during Article IV and program discussions. The Board will need to monitor closely the evolution of the DSA framework and to review its ongoing appropriateness as scheduled in the first half of 2006.

We note the preliminary analysis and options for dealing with the protracted arrears cases as set out in Annex I to Supplement 1, and agree that these cases should be considered in due course.

While noting the arrangement for the MDRI and for interim PRGF commitments as set out in the supplementary papers, as well as the pending decision on establishing the Exogenous Shock Fund, we also look forward to the Board examining the longer term financing issues in relation to the PRGF in the not too distant future.

Mr. Ge and Ms. Wang submitted the following statement:

We thank staff for the supplement papers on the MDRI which have tried to address Directors' concerns and comments at our last Board meeting on this issue. We appreciate the efforts of management and staff to promote the implementation of the IMFC decision on the G8 debt proposal in a timely manner. Debt cancellation will provide significant additional resources for LICs' endeavors to reach the MDGs and reinforce their long-term debt sustainability.

We agree with the approach identified in SM/05/353 to meet uniformity of treatment requirements, under which SDA resources would provide MDRI debt relief to member countries below an agreed annual per capital income threshold and PRGF Subsidy Account resources attributable to third party contributors could be used to provide MDRI debt relief to those HIPCs with per capita incomes above the designated threshold. We think the selection of a per capita income threshold of US$380 is appropriate and would allow 37 countries—including two non-HIPC countries—to benefit from 100 percent debt relief. Under this approach, staff mentions that new bilateral contributions of SDR0.21 billion would be needed in bringing the total remaining PRGF subsidy resources to SDR1.40 billion to allow full use of uncommitted interim PRGF loan resources of SDR2.7 billion as well as all existing PRGF loans. Is this amount included in the G8 commitment of additional costs? When will the contributions start, at the beginning of the debt cancellation or later? Staff's comments are welcome.

We emphasize that conditionality for debt relief under the MDRI should be consistent across members. Post-completion-point members to receive debt relief under the MDRI should prove a satisfactory record in macroeconomic performance and implementation of the poverty reduction strategies and public expenditure management systems. We agree that for members whose performance has lapsed in any of these areas, debt relief under the MDRI would be delivered only after the Board determines that appropriate remedial steps have been taken. The entry conditionality of non-HIPCs should be broadly similar to the criteria applied to post-completion-point HIPCs.

We emphasize that post-debt relief monitoring is critical to realize the full benefits of the relief. We agree that the design of appropriate and fiscal and financing policies after debt relief will be a central element of policy discussions with the beneficiary countries. Staff should provide policy advice and technical assistance to guide the use of the resources freed by the debt relief.

We think that specific modalities should be considered in due course for the treatment of protracted arrears cases and we welcome the preliminary options and considerations provided in Annex I on alternatives to address this issue so that these countries will not be excluded from the debt relief. We emphasize that any new approach should not imply an important departure from existing policies.

Regarding the delivery of debt relief, we agree with staff's recommendation that debt relief be delivered so as to allow the early repayment of the full stock of eligible obligations as the stock option will be more closely aligned with the intention of the initiatives and the expectations of beneficiaries, as well as reducing the administrative costs and risks for the Fund associated with the implementation of the MDRI. We also support the proposal that financial assistance provided under the HIPC Initiative at completion point be delivered in a similar manner.

We note that staff has not further addressed one important issue discussed in SM/05/353—the mitigation of the impact of the G-8 proposal on the GRA. Although the use of the SDA corpus to deliver debt relief would not have an immediate effect on the GRA balance sheet of its income position, it removes an option that was potentially available for permanently mitigating the impact of the off-market transactions. Also, as SDA resources are no longer available to pay for the reimbursement of the administrative expenses of the PRGF, this cost would fall on the Reserve Account, thus lowering the self-sustained lending capacity by a potentially significant amount. In this regard, we encourage staff to further research the effect of the MDRI on the overall financial integrity and financing capacity to LICs.

Mr. Schwartz and Ms. Valle submitted the following statement:

As we have stated in previous occasions, we support the debt cancellation proposal launched by the G-8, now called the Multilateral Debt Relief Initiative (MDRI). After we formally discussed this issue at the Executive Board last August, the staff has made further efforts to clarify the proposal's implications for the Fund, taking into account some caveats the Executive Directors expressed on that occasion. Furthermore, the IMFC reached an understanding on this issue in September.

Nevertheless, although we support the proposal and are ready to go along with the consensus that eventually arises, we would like to make the following observations, taking into account the more detailed assessment on different issues that the staff has made in this new set of papers.

Eligibility and Uniformity of Treatment

In previous occasions, staff made a very strong case that, on the grounds of uniformity of treatment, the proposal could not be addressed only to HIPC countries, just because of this condition. On reviewing this issue now, the staff concludes that "the provision of debt relief by the Fund to members with the lowest per capita incomes is consistent with the uniformity of treatment requirement". Yet, to adapt this criterion to the G8 proposal's "target" group, the staff identifies an approach that splits this group into two sub-groups, according to their per capita income, which, in turn, determines which source of financing can be used to grant the proposed debt relief. It is not yet clear to us, if there is an objective way to determine the advantage of one of the cutoff levels versus the other.

However, we agree that the per capita income criteria could be useful to achieve an outcome that is very close to the G-8 proposal, which we favor, and, thus, we are ready to support it.

Conditionality

At the outset, and as a general principle, we believe that debt cancellation should be linked to policy performance, which would ensure a better use of resources. Like staff, we also believe that conditionality for debt relief under the MDRI should be consistent across members. Therefore, we appreciate staff's efforts on concisely defining conditionality, depending on the group of countries considered: if non-HIPC countries are to qualify for the initiative, ad hoc HIPC-equivalent criteria are also needed to demonstrate good economic performance.

In this vein, we do agree that the qualification criteria for post-completion-point HIPCs (and for non HIPCs, if that is the case) should focus on the three areas highlighted by staff. Debt relief under the MDRI should not be granted for these countries until the Board confirms that the beneficiaries' performance in these areas has not deteriorated since they reached their completion point (for HIPCs), or since the latest review of the program (for non-HIPC). If the performance has lapsed in any of these areas, debt relief should not be granted until appropriate remedial actions are put in place. In this case, we believe that a scheduled approach to take these actions would be useful and would allow for a gradual debt relief under the MDRI, once each action (or phase) is concluded. We would welcome staff's comments on this option.

Further on the assessment of the three key areas, it is our opinion that, in order to make them more operational and objective, it would be necessary to specify the evaluation criteria in a more precise way, specially in those cases in which there is no Fund arrangement. For instance, in the case of the "satisfactory macroeconomic performance", defining benchmarks could be an option. We would appreciate further staff's comments.

Finally, for pre-completion-point HIPCs we agree that reaching the completion point would qualify them for debt relief under the HIPC Initiative and the MDRI.

Safeguarding PRGF Financing Capacity

The importance of not jeopardizing the IMF's financing capacity to LICs has been stressed in many occasions by this chair and others, but also by the G-8[1] and, lately, by the IMFC in its last Communiqué. In this set of papers, together with the presentation of an approach to meet the equality of treatment requirement, staff has made a welcomed effort to clearly present its financial implications.

The staff's paper (SM/05/353) concludes that, while, on current projections, the available subsidy resources after the debt relief (considering the option of US$380 cutoff per capita income) will not cover the remaining PRGF loan resources; the G-8 commitments ensure that the proposed debt relief would not undermine the Fund's financing capacity to LICs. Moreover, we understand that, if the chosen option is the US$270 cutoff per capita income, the Fund's capacity lo LICs would be even better-off, since new bilateral contributions will be needed. Could staff comment on this point?

Other Issues

On the legal considerations regarding the use of contributor resources in the PRGF Trust Subsidy Account, like staff, we are of the opinion that the protected provision excluded for amendment refers to the Fund's capacity to

[1] G-8 Finance Minister's Conclusions on June 11.

amending this provision unilaterally and not to the fact that it could never be amended.

The protracted arrears cases should be treated separately, as staff suggests. It is necessary to further study the available alternatives to deal with the arrears clearance and the debt relief, without damaging even-handedness across the membership.

Mr. Shaalan and Ms. Beidas submitted the following statement:

We welcome the revised paper on the Fund's role in the Multilateral Debt Relief Initiative (MDRI). The implications for the Fund and implementation modalities are well covered. Specifically, we would like to thank staff for the progress made to address the issue of uniformity of treatment, conditionality, safeguarding concessional lending to LICs and the Fund's future income position.

It must be noted that while the use of SDA resources will maintain the uniformity of treatment principle, use of the PRGF Subsidy Account will not. Instead, staff propose amending the PRGF Trust Fund's legal set up to allow using these resources for HIPCs above an agreed income threshold. It is clear that the application of uniformity of treatment while using in-house resources to fund such uniformity would be a double-edged sword. While being more inclusive and allowing as many LICs with credit outstanding to the Fund to benefit from the MDRI would drain the SDA account, thus posing financial risks—in the sense that the SDA balance would no longer be available to be transferred to the GRA. Limiting the extent of inclusiveness implies that those HIPCs with higher income levels would benefit (from non-IMF resources) at the expense of those poorer. Staff have identified income thresholds, which allow us to continue our PRGF operations with an acceptable level of financial risk and MDRI inclusiveness. We believe that the US$380 or US$400 strikes this balance. In view of the support garnered for the initiative, we find ourselves having to accept this solution—should the majority needed to make the requisite legal amendments be garnered.

The US$380 threshold compared to a lower threshold would imply no additional bilateral contributions beyond those currently available in the Subsidy Account, as well as more debt relief delivered overall, as shown in Supplement 1, since two non-HIPC countries would also benefit. Like Mr. Kiekens, we could not accept anything less than the US$380 threshold. With this threshold 21 HIPCs and two or three non-HIPCs will benefit from 100 percent Fund credit outstanding debt relief. However, should less than 100 percent debt relief be offered, the number of beneficiaries could be expanded. We continue to wonder why such a gradation has not be more strongly advocated by staff while remaining within the same envelope of SDA resource usage (i.e., SDR1.39 billion out of the total SDR 2.5 billion).

For countries above the US$380 threshold, bilateral resources in the PRGF Subsidy Account (SDR 1.4 billion) would be used to benefit 14 HIPCs—which are both post and pre-completion point countries. This would reduce the non-IMF part of the PRGF Subsidy Account from SDR 1.41 billion to SDR 0.29 billion, and would require more contributions from other accounts into the Subsidy Account, to bring it to a balance of SDR1.4 billion. Since the G-8 had originally agreed to pay for what is required, staff's new estimate is SDR210 million, which remains well below the initial pledge by the G-8. Indeed since, as mentioned by Mr. Misra and Mr. Srinivas, the two additional non-HIPCs would benefit on account of uniformity of treatment from the SDA, the G-8 would not be bearing these costs and implicitly the outstanding PRGF Subsidy Account balance is made even more affordable.

More resource may still be needed, particularly should the G-8 fulfill the commitment to resolve the three protracted arrear cases, which would then require increasing the level of future PRGF lending capacity and thus subsidies. It appears that staff has not yet factored this into the outstanding PRGF Subsidy Account resources.

In this context, we believe that a full resolution of the three protracted arrear cases must go hand in hand with the implementation of the MDRI. Staff have elaborated the full cost of protracted arrear cases at SDR 1.8 billion. On the modalities for the resolution of these three cases, we thank staff for initial deliberations on this and would need some time to reflect on these modalities. However, as an initial reaction, the second approach presented in Supplement 1 appears the most suitable—the modified rights approach accumulation program, since it would involve bilateral contribution amounting to SDR 1.8 billion without use of any bridge Fund loans, thus placing these three cases on an equal footing with other HIPCs. Staff suggest that this is a tested instrument, and therefore one could argue that it merits a special cases as did the HIPC Initiative at its inception.

We continue to favor a phased modality for debt relief delivery, contingent upon the fulfillment of the three conditionality areas proposed by staff; macroeconomic stability, PRSP and PEMs. This phasing could we waved if countries fully meet the above criteria ex ante. Thus is may end up only being applicable to countries which do not meet the staff assessment and need further monitoring. Phasing would act as an incentive for beneficiaries to meet the remedial actions proposed by staff while making progress in resolving their debt outstanding in a gradual manner. However, this approach would not be possible should full-stock relief, instead of flow relief, be agreed by the Board.

On the three areas identified by staff for HIPCs and non-HIPC, we can agree with the proposed staff assessment to be presented to the Board, preferably in the context of other documents presented to the Board to minimize administrative costs. However, we have trouble with the fact that assessments will also be eventually needed by the World Bank for its part of the MDRI. We believe there should be no duplication and that these assessments present similar findings. Indeed only the first component—the macroeconomic assessment is truly in the area of the Fund core competence. The two others are firmly within the World Bank's forte. Therefore we recommend that footnote 10 of Supplement 1 be amended to reflect this needed collaboration with the World Bank—i.e., through FAD for the PEM and PDR for the PRSP. We could even go further and express our preference for the World Bank ought to take the lead in these two sections of the assessment.

Clearly the above would imply different administrative costs for the Fund. We believe that staff have underestimated the on-going administrative cost, particularly those proposed in paragraph 15, 16 and 17. Remedial actions being reported in regular country reports, two or more new PEM assessment will be needed for non-HIPCs, the status of all members in the three identified areas will be reported on before the Spring Meetings, non-HIPCs being reported on within the HIPC Initiative status report may be unacceptable to non-HIPC members, are all not without additional costs.

In terms of conditionality for non-HIPCs, we would only suggest that the minimum of six months of a satisfactory macroeconomic track record be extended, while the implementation of the PRSP and quality of PEM be shortened. Twelve or eighteen months would appear to be a reasonable streamlined medium.

Finally on conditionality, we found the suggestion that the design of policies post debt relief would be a central element of the MDRI hard to believe, since post debt relief incentives to cooperate with the Fund would be weakened. Therefore, we support Mr. Kiekens' call for a letter of intent expressing consent to participate in such post MDRI policy discussions with staff.

Mr. Bischofberger, Mr. Duquesne, Ms. Lundsager, Mr. Kashiwagi, Mr. Lynch, Mr. Mozhin, Mr. Sadun, and Mr. Scholar submitted the following joint statement:

Following the agreement at the IMFC on the Multilateral Debt Relief Initiative, we are grateful to management and staff for all their work in bringing forward these papers so that the Board can complete its approval of the arrangements to deliver debt relief by the end of 2005.

Uniformity of Treatment

We welcome the approach set out in the staff paper to ensure that the IMF's resources will be used in a way which is consistent with the principle of uniformity of treatment; we support the proposed income threshold of US$380 GNI per capita; and we accept that it will be necessary for two additional countries—Tajikistan and Cambodia—to be considered for IMF debt relief. We stress, however, that the eligibility for debt cancellation under the MDRI for these additional countries will be exclusive to the IMF. IDA, other multilateral development banks, or the Paris Club will not be expected to provide such relief.

Conditionality

As the IMFC emphasized, countries benefiting from irrevocable debt relief should have demonstrated sound policies and high standards of governance.

In the case of pre-completion point countries we agree that reaching the completion point would qualify them for debt relief under HIPC Initiative and the MDRI. For post-completion point HIPCs, we accept the approach suggested by staff and agree that this should comprise satisfactory macroeconomic performance, satisfactory implementation of the PRS, and sustained improvements in the areas of public expenditure management systems, governance and transparency. Assessments should emphasize current performance rather than that since completion point. Also, all countries receiving relief must be current with their repayment obligations to the IFIs. Subject to satisfactory current performance in these areas, however, there should be a strong presumption of immediate eligibility for post-completion point countries. We also support the staff proposal that they should bring to the Board an assessment of the performance of all post-completion point countries in each of these three areas, and believe this should be done in a timely and efficient manner to enable the delivery of debt relief by the beginning of 2006.

We share staff's view that conditionality for debt relief under the MDRI should be consistent across members. For the two non-HIPCs, in order to ensure equality of treatment and the proper use of Fund resources, they should be required to demonstrate the same track record of sustained economic performance—including a satisfactory track record of strong policy actions meeting the upper credit tranche conditionality—as is required of the HIPCs, in order to receive debt relief. We do not feel that the framework proposed by staff is sufficiently robust to achieve this, and ask the staff to look again at this to ensure a consistent application of conditionality across the membership.

Financing

As set out in our previous statements, we are fully committed to ensuring that the financing capacity of the IMF is not reduced. The G-8 has agreed to provide SDR 100 million to the PRGF Subsidy Account. This amount, in addition to the remaining SDA resources (estimated at about SDR 0.47 billions) to be transferred to the Interim PRGF in a timely manner, will support continued lending during the interim PRGF period.

There is considerable uncertainty about whether and when the potential additional costs of including Tajikistan and Cambodia might arise, and how much the eventual costs could be. We will therefore consider dealing with these costs if and when they arise, consistent with our commitment to ensure that the financing capacity of the IMF is not reduced.

On the self-sustained PRGF we endorse the staff estimate for the likely level of future demand of SDR 1 billion per annum, including shocks.

We generally support the financial structure set out in the staff papers. As the paper highlights, implementation of the MDRI will require action by the Executive Board and by contributors to the Subsidy Account of the PRGF Trust. We look forward to early adoption by the Board of a number of decisions, and the necessary consents from donors, to enable the delivery of debt relief under the MDRI by the beginning of 2006. In this context we should move forward in parallel with decisions on the Exogenous Shocks Facility to enable management to seek the timely consent by all contributors to the amendments to the PRGF Trust required for the implementation of both the MDRI and the ESF.

We agree with the use of SDA resources described in paragraph 15 of the second supplement. However, we consider that the remaining balance, amounting to about SDR 0.47 billion, should be immediately transferred to the Subsidy Account that would subsidize both PRGF and ESF lending, as soon as the debt proposal is implemented. The "step-by-step transfer" suggested by staff in the second bullet point of paragraph 15 on page 8 of Supplement 2 is not appropriate in our view, unless there is a clear justification. We would appreciate staff comments.

Rate of Charge

As the Chairman stated in the IMFC discussion, there is no intention to change the current arrangements on the burden sharing for mitigating the effect of the 1999 gold transactions as a result of this proposal, and so equally there should be no impact on the rate of charge.

Other Issues

We agree with the proposed modalities for post-debt relief monitoring.

We agree on the need to consider in due course the treatment of protracted arrears cases and of countries that could become eligible under the sunset clause of the HIPC Initiative.

We support the staff recommendation that debt relief under MDRI should be delivered to allow the early repayment of the full stock of eligible obligations, with the understanding that there will also be a mutual agreement between the Fund and the individual lenders to the PRGF Trust on this issue.

We welcome plans to consider the implications of the MDRI when the low-income debt sustainability framework is reviewed in 2006 and attach great importance to ensuring that this exceptional debt relief leads to lasting debt sustainability.

Extending his remarks, Mr. Scholar made the following statement:

I read the set of grays over the weekend and saw that there were some questions in them directed to the G-8 Directors, in particular on financing commitments. I think that the statement that we put out late on Friday afternoon probably answers those questions, but for the sake of completeness, I would just like to quickly run through the various financing commitments that the G-8 governments have made to make sure that everyone is aware of the full commitment.

The overarching commitment is to ensure that the financing capacity of the IMF is not reduced. The statement of the Ministers in June made a commitment to provide resources on a fair burden-sharing basis for the interim PRGF, subject to further analysis by the institutions of the resource requirements. We received that further analysis in September from the staff, which showed that the amount required to ensure that the IMF's financing capacity is not reduced would be SDR 100 million. The G-8 Ministers, in their communiqué at the end of September just before the Annual Meetings, committed to cover that cost in full; hence, not just on a fair burden-sharing basis, but in full. That, in fact, goes beyond the original commitment.

On the protracted arrears cases, the proposal is that donors would commit to provide the resources necessary for debt cancellation at the completion point of the three protracted arrears cases—Sudan, Somalia, and Liberia. Here, we agree with the staff that there is a need for the Board to come back and consider that issue further in due course.

On the HIPC Initiative sunset cases, the commitment is that the G-8 will cover on a fair burden-sharing basis the cost of debt relief to countries that may enter the HIPC process based on their end-2004 debt burden.

Finally, we have the so-called uniformity cases. Here, the commitment is set out in the statement that we circulated on Friday. As discussed in our previous meeting in September, it seems to us that there is considerable uncertainty about whether and when the potential additional costs of including Tajikistan and Cambodia might arise and how much the eventual cost could be, so we propose that we consider dealing with these costs if and when they arise, and that is consistent with our overall commitment to ensuring that the financing capacity of the IMF is not reduced.

In sum, we have an overall commitment, and there are several elements to delivering that, which I have set out. In particular, on the interim PRGF, we have delivered on that commitment with a precise figure of SDR 100 million. So I hope that clarifies that issue.

Mr. Rouai made the following statement:

We thank management and staff for their efforts in advancing the understandings reached during the last IMFC meeting on debt cancellation for LICs and their proposals on the design and financing of the Fund's part in the Multilateral Debt Relief Initiative (MDRI). In order to ensure an early implementation of this initiative, we accept at this stage the tentative and sketchy feature of some of its elements, particularly the cost arising from the inclusion of countries under the sunset clause of the HIPC Initiative, and the modalities for arrears clearance by Liberia, Somalia, and Sudan as well as the cost of debt cancellation and its financing for these countries. The staff is encouraged to revisit these issues as soon as possible and provide the Board with concrete modalities and financing options.

Turning to the issues for discussions, we have the following comments:

On uniformity of treatment, we support the per capita income threshold of \$380 as a cut-off for countries whose debt to the Fund will be financed from SDA resources. This threshold will add Tajikistan and Cambodia to the list of countries initially contemplated under the G-8 proposal. The G-8, however, considers that "eligibility for debt cancellation under the MDRI for these two countries will be exclusive to the IMF. Other multilateral development banks or the Paris Club will not be expected to provide such relief." The staff's response to this position and how to go with the initiative's multilateral character and designation is welcome. While the use of the \$380 threshold minimizes the need for additional resources, it will entail new bilateral subsidy contributions amounting to SDR 210 million to allow full use of uncommitted interim PRGF loan resources. While the indication of the G-8 that they will provide SDR 100 million to the PRGF subsidy account and by some Nordic countries that they will consider a contribution are welcome, the staff is encouraged to start consultation with bilateral donors to seek contribution to the PRGF subsidy account and the financing of the Exogenous Shocks Facility (ESF).

On conditionality for debt relief under the MDRI and post-debt relief monitoring, we support the modalities detailed in Section III of the staff report. Specifically, we agree that reaching the completion point would qualify countries for debt relief under the HIPC Initiative and the MDRI. For post-completion point countries, the three-pronged approach based on satisfactory assessment of macroeconomic policy, implementation of a PRS, and public expenditure management systems are recommended. For non-HIPCs, the staff rightly indicates that their debt ratio is comparable to that of post-completion point

HIPCs, and, therefore, these countries will qualify for the MDRI under same conditions as of post-completion point countries.

The staff's preliminary consideration of the issue of debt relief for the protracted arrears cases is welcome. Their two proposals on limited grandfathering, or modified RAP approach are noteworthy, and we join other Directors in helping staff to identify a solution that could garner Board's support.

At the outset, we have strong reservations about the modified RAP approach. The staff has already identified some shortcomings to this proposal, including the fact that the three protracted arrears countries will not be able to receive balance of payments support from the Fund before reaching the completion point. The staff is correct to indicate that this approach constitutes an important departure from existing policies, namely that HIPC assistance would be granted without a PRGF arrangement, which requires a modification of the HIPC Trust instrument. Since these countries would remain in arrears under this approach, a modified RAP could prevent them from regularizing their situation vis-à-vis multilateral and other creditors and could leave unchanged the negative perception of donors and investors about these countries. The staff may wish to consult with the World Bank and other MDBs as it is unclear how these institutions would deliver assistance to a country that is still in arrears. Moreover, in the particular case of Sudan, this approach does not seem to take into account the country's long and satisfactory track record of policy performance and its repayment record to the Fund.

The limited grandfathering approach recognizes the difficulties of applying the principle of cut-off date under the MDRI for the protracted arrears cases. This proposal is fair vis-à-vis other HIPCs servicing their debt to the Fund between their decision and completion points, and it contains incentives for the arrears cases to reach their completion points quickly. However, some legal problems with the concept of "notional repayment schedule" are to be observed, and staff may clarify whether such an approach would not imply the use of Article V, Section 7(g), to provide for a postponement of the discharge date of a repurchase obligation. The staff may also clarify if the concept of "notional repayment schedule" is consistent with paragraph 4(c) of the PRGF Trust which states that "The Trustee may not reschedule the repayment of loans from the Trust." For these considerations, we prefer a simple extension of the cut-off date, limited to the three protracted arrears cases, as suggested by Mr. Solheim and Mr. Hollensen.

To conclude, the MDRI has created considerable expectations in member countries, civil society, and the media. While the efforts made to reach a consensus on this initiative and to implement this policy are commendable, its success will rest only on the actual delivery of debt relief. To this end, we look forward to staff assessments of recent performance of post-completion point HIPCs and other MDRI-eligible non-HIPCs under Board's consideration.

Mr. Schaad made the following statement:

I thank the staff for its efforts in producing these informative supplemental documents. However, while I know that we have little time before the target implementation date of the initiative under discussion, I very much regret the very short time we were accorded to reflect on the new material.

At the Annual Meetings, the Chairman of the IMFC assured committee members that the process of implementing the debt relief initiative would be improved. I note that, as of now, this promise remains unfulfilled. The short circulation period did not allow us to adequately consult with the members of our constituency on an issue of great importance to them and of significant financial implication for all of us. This said, this chair supports the general approach proposed to ensure equality of treatment. We agree with the qualification criteria set forth by the staff, and consider the different categories of countries, namely pre- and post-completion point countries, and non-HIPCs, as being treated in a comparable way. We fully support the staff proposal on how to include non-HIPC countries in the initiative. It appears that the Board is converging toward a per capita income threshold of US$380, and this chair is prepared to support it.

I concur with Ms. Phang and Mr. Wesaratchakit that a threshold below what is generally considered to be the level of extreme poverty would be hard to reconcile with the spirit of this initiative.

With regard to conditionality, I support the three conditions set forth in the staff report. In addition, I would emphasize the importance of good governance and good cooperation with the Fund, as noted in our discussion in September and in today's issues for discussion. A candid assessment by the staff of a country's performance and effective remedial actions, if necessary, is very important in implementing the multilateral debt relief initiative. This will help assure that the ultimate goal of the initiative—progress toward the Millennium Development Goals—will be reached.

With regard to the delivery of the debt relief, I support the staff's recommendation to allow for the early repayment of the full stock of eligible obligations, as this reduces the administrative costs and risks for the Fund.

Concerning post-debt relief monitoring, I reiterate that coordinating with the World Bank is important and that the main focus of Fund staff should be on the fiscal framework. In particular, this chair considers expenditure monitoring to be crucial to maximize the chances of bringing the countries closer to the Millennium Development Goals (MDGs). In this regard, I missed a more detailed discussion of the envisaged content of the proposed MDRI status reports. Specifically, how will they monitor the effective use of resources freed up by debt relief? In my view, it is indispensable to define a set of criteria that ensures that the resources made available through debt relief indeed contribute to poverty reduction and to the MDGs. Moreover, the importance of preventing a rapid accumulation of new debt, particularly toward the IMF, cannot be emphasized enough. We look forward to the staff's proposal in this area in the forthcoming review of the Debt Sustainability Framework.

Generally, and as noted before, this chair would expect low-income countries' balance of payment financing needs to substantially decrease with the implementation of the MDRI. Accordingly, looking forward, the focus of Fund activities in low-income countries should shift from financing to surveillance and capacity building.

We would appreciate more information on the coordination with the World Bank and the African Development Bank in implementing the MDRI, especially with regard to the eligibility criteria and the start of implementation. Could the staff elaborate on that?

Turning to financing, I still consider that the financial analysis provided so far lacks the necessary rigor. As yet, this chair very much misses an overall view of the MDRI's financial implications. For instance, the two supplements do not include the cost of debt relief for potential HIPCs under the extended sunset clause and the protracted arrears cases. Although I recognize the uncertainty of these additional costs, it will be important to have at least an estimate and as clear a view as possible what they would entail in terms of necessary bilateral contributions.

The analysis also leaves out an overall assessment of how the MDRI impacts the PRGF's and ESF's financing needs. Such an overall assessment is now all the more important, as one single subsidy account is likely to be used for the PRGF and the ESF.

I remain unconvinced of the need to supplement the PRGF subsidy resources by the SDR 210 million determined by the staff. While I understand that this would be required to maintain the current capacity to provide financing under the interim PRGF, I would like to point out that this capacity is unlikely to be fully used. As mentioned in the June paper on PRGF financing, new commitments of PRGF resources amounted only to some SDR 500 million in 2004. As we can even expect the financing needs of PRGF-eligible countries to diminish following debt relief under this initiative, the remaining PRGF loan resources would normally substantially exceed the demand for new commitments until end-2006. I would welcome staff comments on this.

Finally, like others, I would expect the initiators of the MDRI to shortly bring forward firm financing commitments covering the bulk of the required bilateral contributions for all countries that will benefit under the initiative, including the non-HIPC countries that are entitled to take part in the initiative. I cannot talk about Cambodia, but as far as Tajikistan is concerned, I do not see the uncertainty that Mr. Bischofberger and the other G-8 chairs bring forward. For instance, Tajikistan is on a successful Fund-supported program. I would very much appreciate Fund staff's explanations on this.

Mr. Alazzaz made the following statement:

I thank the staff for an insightful set of papers that broadly addresses the issues raised during our last meeting. The papers also detail the proposed modalities and financing of the initiative. I am in general agreement with the staff proposals and will limit myself to few comments.

First, as I noted during our last meeting, the Legal Department seems to have found a way to help meet the letter of the law relating to the uniformity of treatment of Fund members. Accordingly, I can go along with the proposed approach, but continue to have doubts regarding its fairness. In this connection, a per capita income threshold of either US$380 or US$400 is preferable.

Second, I agree with the staff that qualification criteria for post-completion point HIPCs should comprise satisfactory macroeconomic performance, satisfactory implementation of their poverty reduction strategies, and a determination that public expenditure management systems had not deteriorated since the completion point. In this regard, I look forward to the staff's assessment of recent performance of all post-completion-point members. For those countries whose performance is not deemed satisfactory, the proposed modalities to address this issue appear reasonable.

Third, I share the staff's view that entry conditionality for non-HIPCs should be broadly similar to the criteria applied to post-completion-point HIPCs. Indeed, the modalities detailed in paragraphs 14 and 15 of the paper seem appropriate. I also agree with the proposed modalities for post-debt relief monitoring.

Fourth, it is very important to put in place appropriate modalities to allow the three protracted arrears cases to benefit from the MDRI while ensuring consistent treatment of members. The staff proposes two primarily options to deal with this issue. I look forward to a more detailed assessment of these options in a timely manner so as to reach a conclusion soon.

Finally, in view of the very important legal questions that have been recently raised, it would be useful in the future to vet in more detail the legal issues, especially in policy papers.

Mr. Loyo made the following statement:

This chair, like a number of others, has long recognized the intrinsic merits of debt relief but has had misgivings with respect to the financing of the

MDRI. In particular, such financing could impose a burden on the GRA and, as a result, on charges paid by borrowers of Fund resources. In the main body of SM/05/353, paragraph 59, the staff reminds us that the possible return of the corpus of the profits of the off-market gold transactions or of their income to the GRA was by no means a foregone conclusion and, in any case, was not expected to take place "well into the next decade." The staff estimated that it could not happen before 2020, when sufficient income would have been generated in the SDA to cover the needs of the HIPC Initiative. That possibility is foreclosed with the decision taken now to apply those resources to debt relief.

There remains, however, another avenue by which borrowers could be burdened in the meantime, and that is the modification of the burden-sharing arrangement in force to mitigate the impact on the GRA of the off-market gold transactions. In this respect, we welcome the joint reiteration by the G-8 Directors of the commitment announced by the Chairman of the IMFC in September. That announcement was made in direct response to queries on the part of the representative of our constituency, the Finance Minister of Brazil. The minister's decision to support moving ahead with MDRI was taken then on the strength of the Chairman's announcement. I imagine that the announced commitment with respect to the burden-sharing arrangement must have been crucial for similar positions taken by other committee members, as well.

I note also that Supplement 1 confirms the choices of per capita income cutoffs for the inclusion of non-HIPCs. A cutoff between US$380 and US$400 would not have changed the financial envelope of the initiative and would have had a negligible impact even in the composition of financing. As we can see, the two right-most columns of Table 1 of the supplement are identical after rounding. This is the comparison between the US$380 and US$400 cutoff, because extended sunset clause HIPCs are presumed to be counted as accessing the MDRI as HIPCs upon reaching completion point. We noted in the last meeting, however, that increasing the threshold to US$390 would have had a negligible impact on financing, even if potential extended sunset clause HIPCs were treated not as HIPCs upon reaching completion point but, instead, as non-HIPCs for both access and financing purposes, as it entailed the inclusion of just one country in that category with debt eligible for relief amounting to a mere SDR 3 million. Accordingly, we regret that, faced with options that are virtually identical in terms of financing requirements, the choice has not been for a more inclusive and flexible approach.

One reason that has been alluded to in response to my remarks in our last meeting was the possibility that inclusion of more non-HIPCs below a higher threshold could have a significant impact on the IDA side of the MDRI. We note, however, that the G-8 Directors proposed to eliminate this possibility entirely by limiting the eligibility of these countries to IMF debt relief only.

We are prepared to go along with the consensus on the access requirements proposed by staff. In particular, we note that it is proposed to treat non-HIPCs on the same footing as post-completion point HIPCs. This would not have made sense if the possibility was contemplated of granting debt relief to countries potentially qualifying for the HIPC Initiative within the extended sunset clause if their per capita income was below the threshold through the same procedures as for non-HIPCs, without necessarily going through the motions of the HIPC Initiative or waiting for the completion point to be reached.

With regard to the proposed post-debt relief monitoring, we have a number of serious reservations. First, we should carefully guard against the confusion this nomenclature can create with Post-Program Monitoring (PPM). The objective of PPM is not to ensure that countries take—in the view of the staff, management, or the Board—full advantage of the Fund resources they continue to use, but to ensure that their policies appropriately safeguard their ability to exit from Fund support and return those resources to the Fund. No comparable objective is present in the case of the MDRI, and for that reason, we suggest that a different terminology be used for any special component of the Fund dialogue with countries that have benefited from the MDRI.

Second, the Fund should refrain from laying too strong a claim to an expertise that it lacks and that falls outside its core mandate, namely, providing detailed guidance on the use of resources for developmental or poverty reduction purposes. Such detailed guidance was never the intention of any form of ongoing conditionality contemplated at the earlier stages of our discussion. Such ongoing conditionality was meant, instead, to ensure against serious slippages in macroeconomic stability or governance practices, and even that we ultimately rejected.

Third, given that consensus has already been reached on delivering debt relief upfront, the proposed post-relief monitoring should be shaped more as a vehicle for reviewing continuously the overall effectiveness of the MDRI, rather than the conformity of individual beneficiaries. We have carefully weighed the pros and cons of ongoing conditionality, which could be made viable by phased delivery of debt relief. Our conclusion, by consensus, was not to retain those options. It is our strong view, therefore, that we should not be tempted by artificial ways of mimicking the situation that would have prevailed had the Board decided to adopt mechanisms that would make ongoing conditionality effective. Here, I regret to say that I find myself in disagreement with my esteemed colleagues, Mr. Kiekens, Mr. Shaalan, and Ms. Beidas. I do not believe that it is a good idea to ask countries to sign LOIs expressing their commitment to post-relief consultations with the Fund. In my view, it would just reinforce the false impression that ongoing conditionality is in place, especially with the confusion that would arise with the eponymous LOIs in the context of Fund-supported programs. With a modification in nomenclature and focus, however, we would be willing to support some element of post-relief engagement and assessment.

The Director of the Policy Development and Review Department (Mr. Allen), in response to questions and comments from Directors, made the following statement:

> Let me start with a question raised by Mr. Shaalan and Mr. Misra about why we have not proposed graduated debt relief in order to expand the number of beneficiaries. We discussed this option in the very first paper on the subject, and our sense was that this did not seem to have the support of a majority of the Board, nor was it endorsed by the IMFC, which called for 100 percent debt relief for a defined group of countries as characterizing the initiative. That is the reason why we have not pursued that particular line here.
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> There were a number of points related to the entry conditionality proposed in the paper. For countries that are HIPC-eligible but that have not yet reached the completion point, there seems to be no disagreement that these countries will become eligible for debt relief under this initiative once they reach the completion point. Hence, the issue relates solely to how to cover the post-completion-point HIPCs and the non-HIPCs.
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> There are three criteria, and a number of Directors have asked for some clarity on how these criteria will be assessed in practice. We agree that implementation should be flexible, and we also note the point made by the G-8 Directors in particular that there should be a strong presumption of immediate eligibility for post-completion point countries.
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> The first criterion, which is satisfactory macroeconomic performance, should not necessarily require, in our view, a program relationship with the Fund for those members that do not currently have a Fund arrangement. We believe we can make this assessment without requiring a member to enter into a formal arrangement. For members that do have a Fund arrangement, we would check whether the program was on track and, if not, what would be necessary to bring the program back on to track, which would presumably be a sufficient condition for remedial action.
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> On the second criterion, which is the poverty reduction strategy, some Directors note that there may be cases where the country is, indeed, engaged in strong poverty reduction efforts under frameworks alternative to that of the PRSP. This, again, is an area where we will need to show some flexibility; hence, a valid PRSP will not necessarily be a requirement. If there is a PRSP in place, however, but which is not being satisfactorily implemented, that will be an issue that would be considered to determine eligibility.
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> The third criterion pertains to public expenditure management. We expect to cooperate very closely with the World Bank in this area. We will be assessing with Bank staff recent developments in public expenditure management systems in a country, with a focus on what has happened in this area since the member reached the completion point under the HIPC Initiative.

For non-HIPCs, the issue is how to make entry conditionality consistent across the membership, and there are a variety of ways in which one could approach this issue. We tried to come up with an approach that would give us the same level of assurance that the resources released under the MDRI would be well spent in these countries as those that were received under the HIPC Initiative. We need evidence of a satisfactory track record of sustained economic performance. What we are looking for is assurance that policies are in place and are likely to continue, which are needed to provide a prudent macroeconomic environment for the expenditure of the resources released by debt relief. We have proposed a minimum track record of six months of satisfactory implementation of a Fund-supported program, and if there is no Fund-supported program, we would make an assessment that the policies have met the standards of upper credit tranche conditionality for at least a similar period of time.

On the third criterion for non-HIPCs on public expenditure management, we face a slight difficulty in trying to make the requirement comparable with that for the HIPCs in that there is no completion point from which to track a deterioration or improvement in public expenditure management systems. What we plan to do is to focus on trends over the past three to five years to provide comfort that the expenditure management systems in place give us the assurance that any debt relief in this context would be spent well.

Moving to the subject of remedial actions, I can confirm that the intention is that when the remedial actions that a country would need to undertake to receive debt relief have been identified, those actions would need to be taken before the staff will recommend to the Board the release of debt relief for that country. This applies to both the post-completion-point HIPCs and the non-HIPCs.

Some Directors suggested that debt relief should be provided gradually, in line with the implementation of remedial actions. It is an interesting idea, but we are afraid that it would introduce an extra level of complexity into the implementation of the scheme, for example, determining what proportion of debt relief to give at the start of the process when it is judged that the required systems are not in place, and how to release debt relief subsequently. Hence, we felt that the soundest way to move forward was to specify the conditions for remedial actions, and once the remedial actions had been taken, to then provide full debt relief.

In this context, one Director asked whether the remedial actions would be taken in the context of a Fund arrangement or not. Again, the situation here can vary across countries. In some cases, a credible track record could require performance under a Fund-supported program, but this need not necessarily be a uniform requirement. We can also make the assessment in the context of an Article IV consultation, or possibly even on a stand-alone basis.

Finally, on remedial actions, there was a suggestion that time limits be set for taking such actions, so as to provide an incentive to the member to act quickly. Our view is that, given that a potential beneficiary of debt relief will have to continue to repay the Fund on its debts outstanding as of the cutoff point, the country would have a very strong incentive to take the remedial actions as quickly as possible, because the amount of debt relief would decline over time, especially given the relatively short Fund maturities. Hence, we felt that there was no need to introduce time limits for the remedial actions to be taken. It should be noted that we do not impose time limits under the HIPC Initiative.

On post-debt-relief monitoring, a number of Directors asked the staff to clarify what form such monitoring would take. We had envisaged discussions with the authorities on the use of the debt relief resources in the context of regular program review or surveillance. We did not feel that we need to establish a new set of monitoring requirements for this purpose. We could require the member to indicate in its letter requesting debt relief under the MDRI its intention to review with Fund staff the use of resources released by the initiative, but the staff would do that in the context of regular consultations.

Another area that Directors inquired about was the status of discussions on the initiative in the other institutions, that is, the IDA and the African Development Bank (AfDB). Further discussions are pending at the IDA Board after some clarification from the G-8 regarding the exact scope of debt relief and the cutoff date for eligible debt. Board discussion in the Bank on the subject is scheduled for late this month or early next month, with formal decisions being taken possibly in January or February, and implementation expected on July 1, 2006, in line with the Bank's fiscal year.

In the AfDB, a paper has already been prepared for Board consideration, although some costing and financing issues still need to be clarified. A formal meeting in the AfDB on the issue is tentatively scheduled for December, and the target date of implementation is, as in the Fund, January 1, 2006. In light of the questions that still arise on how the initiative will be implemented in other institutions, it is difficult, for the time being, to provide an assessment of the impact of the overall initiative—covering all three institutions—on members' balance of payments.

It is clear that the Board of each institution will take separate decisions on the implementation of the proposal. We will certainly work very closely with our colleagues in the Bank and in the AfDB on the implementation of the initiative, but it is clear that the decisions taken by the Fund Board will only implicate the Fund. This is true for both the eligibility criteria and the conditions that will be applied to countries that are eligible for relief.

Hence, although we are engaged in close discussion with our colleagues in the other institutions on how the initiative will be implemented by their respective institutions, the three institutions are moving at slightly different speeds. Given that we in the Fund have a very tight deadline to meet by the end of the year, there is very strong incentive on the part of Fund staff to cooperate very closely with Bank staff on these matters to reduce duplication in the processes.

Regarding the protracted arrears cases, we were asked at the time of the last Board discussion to consider how the initiative might apply to protracted arrears cases. We have presented some initial ideas in the annex to the main paper. Mr. Rouai also raised several important questions. We do not have all the answers at this point. The approach that we are inclined toward at the moment is for the Board to approve the debt relief initiative without covering the protracted arrears cases, and to consider subsequently how we would handle those cases. Obviously, the three protracted arrears cases are nowhere near the completion point under the HIPC Initiative, which would be the trigger for MDRI relief. Hence, the issue does not have to be resolved with the same urgency as the other issues of the MDRI.

One final point: we are working on a paper on the 20 eligible countries—the 18 post-completion point HIPCs and the two additional cases. We intend to bring that paper for Board consideration before Christmas. If the Board approves the eligibility list, and the consents on the amendments to the PRGF Trust are received, we will be able to deliver the relief on the first of January, 2006.

Mr. Shaalan remarked that graduated aid would still result in 100 percent aid over time, which would still be consistent with the consensus that had been reached at the IMFC. On quantitatively calibrating aid release to corrective policy action taken by the potential beneficiary country, the process should not necessarily be complex, as it was standard procedure with regular Fund-supported programs.

Mr. Rouai wondered if the staff had discussed with the World Bank the extension of the MDRI to the two additional countries, Tajikistan and Cambodia.

The Director of the Policy Development and Review Department (Mr. Allen) said that there were two issues on graduation of aid. The first was whether to provide graduated relief to countries above some threshold, in other words, less than 100 percent relief to a group of countries, so as to expand the number of beneficiaries. The staff had proposed that possibility earlier, but had concluded that the IMFC was interested in a limited group of countries, as well as in providing 100 percent debt relief to that limited group of countries, and not in an additional group to which less than 100 percent debt relief would be applied.

The other possible application of graduated debt relief was in connection with the remedial actions that a potential beneficiary might need to undertake in order to qualify for debt relief, the Director continued. Under the HIPC Initiative, it was possible to provide a certain amount of phased relief in terms of interim HIPC assistance between the decision and completion points. However, the staff viewed the MDRI as being more similar to the HIPC completion point. The staff would simply be trying to reestablish that required conditions had been maintained. As in the HIPC completion point, the staff would essentially be certifying that certain required conditions had been met, and therefore debt relief could be released at that point with some confidence that it would be used well. The remedial actions had been designed to provide similar confidence that those conditions had been restored and that debt relief under the initiative could therefore be committed definitively. There did not seem to be benefit in linking partial debt relief under the MDRI to the individual remedial actions being taken.

Mr. Shaalan stated that his chair's initial proposal had been to provide less than 100 percent debt relief to countries with per capita incomes above the chosen threshold, in order to satisfy the requirement of uniformity of treatment, given the limited resources available.

The Director of the Policy Development and Review Department (Mr. Allen) said that the staff had kept the Bank informed of the MDRI proposals in the Fund. The staffs of both institutions considered that the Fund Board's decisions would have no implications on the Bank's operations or legal structure.

The Director of the Finance Department (Mr. Kuhn), in response to questions and comments from Directors, made the following statement:

> First, on the issue of financing capacity, I welcome the clarifications from Mr. Scholar, which state quite clearly what resources the G-8 has committed to provide. The overall financing capacity of the Fund for concessional lending was set out in this paper as the ability of the Subsidy Account of the PRGF Trust to fully subsidize the remaining SDR 2.7 billion in uncommitted loan resources while leaving the Reserve Account of the PRGF untouched. Under those conditions, an additional SDR 100 million would be needed after the application of the MDRI, plus about SDR 110 million in subsidy resources estimated for the non-HIPC cases, Tajikistan and Cambodia.
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> I can also confirm that the current financing envelope does not take account of the protracted arrears cases nor of the HIPC Initiative sunset cases.
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> In terms of the overall capacity of SDR 2.7 billion in PRGF loan resources that can be used, there was never a limit as to how long the resources can last. A longer life for the interim PRGF simply postpones the implementation of the self-sustaining PRGF. If I understand Mr. Scholar correctly, additional subsidy contributions will be forthcoming to ensure that the SDR 2.7 billion can, in fact, be fully subsidized.
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> On Mr. Kremers' question regarding the interest rates that were assumed in order to calculate the required subsidy resources, we used an interest rate path that is in line with the WEO assumptions, that is, for interest rates to go up to 5 percent by 2010.
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> On whether we have ever restituted any resources from the Subsidy Account of the PRGF Trust to their donors, this has never happened in the past.

> This brings me to the point that it might be quite challenging to obtain the consent of all 43 contributors within a very tight deadline. We will be asking Executive Directors to assist us in getting these consents.
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> Finally, regarding the issue of early repayment of lenders to the PRGF Trust, we take the point that has been raised by a number of Directors that the staff should consult very closely with our lenders on the exact modalities of that repayment.

Mr. Prader said that his chair had inquired about the interest rate that the staff was using to calculate the subsidy resources needed for continued PRGF operations. Regarding the G-8 commitments, he noted that it was a collective commitment, and that the G-8 was evasive on some crucial issues, for instance, on the SDR 110 million needed if debt relief would be extended to Tajikistan and Cambodia. Saying that the G-8 would "consider dealing with these costs if and when they arise" amounted to no commitment. Collective commitments did not amount to anything unless the individual commitments from the countries involved were known. The Fund had plenty of experience with donors' pledging sessions, and the commitment that the G-8 had made would not be considered satisfactory at a donors' meeting. It was not certain that the G-8 governments would live up to their commitment, given that the original promise of SDR 350-500 million had now been whittled down to SDR 100 million.

Mr. Scholar replied that the G-8 Finance Ministers had published a communiqué in September committing to make a contribution of $150 million. That seemed to be a sufficiently clear and binding commitment. That commitment would be honored. With regard to the original $350-500 million commitment that the G-8 had made in June, the G-8 had committed to a figure that at that point had been a working assumption, given that the staff then still needed to make a full assessment of the costs. The staff had explained how the assessment had been conducted, which had shown that the required amount would be SDR 100 million, equivalent to $150 million. That was the commitment that had been formalized and confirmed by the G-8 Ministers. As a matter of fact, having initially promised to meet the financing requirement on a fair burden-sharing basis, the G-8 had decided to go all the way and meet the full financing requirement that had been estimated by the staff.

Mr. Solheim stated that he shared the same concerns that had been raised by Mr. Prader. Mr. Scholar's clarification of the overall G-8 commitments was welcome, but it would be more useful, as Mr. Prader had emphasized, if it could be made more specific with regard to each country's expected contribution. Countries in his constituency had been contributing quite significantly to the PRGF Trust , and some of them were considering further contributions, but would await firmer commitments by the G-8 countries. The staff's presentation had not indicated that there were firmer commitments from the group.

Mr. Schaad wondered if he had understood the staff correctly that, by December, the uncertainty with regard to debt relief under the MDRI for the two additional, non-HIPC cases would be resolved.

Mr. Scholar said that it was important to differentiate between two types of contributions to the PRGF. On the one hand, there was the SDR 100 million that was currently being discussed, which was the cost that would need to be met as a result of the debt relief initiative and which was the amount that had been committed by the G-8. No further commitments were being sought from any other donor in respect of that amount, as the G-8 would meet it in full.

With respect to Mr. Solheim's statement regarding the importance of ensuring that the PRGF Trust be sufficiently equipped with resources to meet projected future demands, Mr. Scholar noted that the G-8 governments very much supported that, and had previously endorsed the staff estimate of a projected demand for PRGF loans of around SDR 1 billion including under the new Exogenous Shocks Facility (ESF). In fact, when the Board had discussed the ESF in the previous week, two chairs had indicated a willingness to contribute immediately, and those announcements would be made shortly. He understood Mr. Solheim's statement as referring to that process of gathering extra contributions, for which indications of specific amounts from particular donors would be needed and would certainly be forthcoming. That, however, was not the same discussion as the one regarding the consequences of the MDRI for the PRGF Subsidy Account.

Mr. Prader reiterated his query on whether the G-8 Directors could indicate their chairs' individual commitments. He also wondered what difference the G-8 perceived between Tajikistan and the pre-decision-point HIPCs such that there was uncertainty in the G-8's commitment regarding debt relief for Tajikistan under the MDRI.

Mr. Scholar explained that in the case of the HIPCs, the Board's thinking had more or less converged on the way in which debt relief under the MDRI would be provided, including the nature of the conditionality, whereas in the case of the two non-HIPCs, the so-called uniformity cases, no such convergence in the Board's thinking had yet been achieved.

With regard to individual commitments by the G-8 countries, the Fund's Finance Department was keen to ensure that those commitments were delivered, Mr. Scholar continued, but he was not sure how those discussions were taken forward between the Finance Department and the individual governments. He did not have a list of the individual commitments by the G-8 governments, but he could assure the Board that the G-8 Finance Ministers would meet their stated commitment in connection with the MDRI.

Mr. Dumont said that he understood that even after the commitment of SDR 100 million, SDR 110 million would still be needed to fully finance the MDRI. However, during the Board discussion on the ESF, the G-8 chair had been fairly categorical that there was enough resources in the Subsidy Account of the PRGF Trust to let the ESF be implemented immediately. Was there, or was there not, enough resources?

Mr. Scholar replied that there was no inconsistency. Even before the SDR 100 million, plus potentially up to SDR 110 million, was added back to the Subsidy Account of the PRGF Trust, there was enough subsidy resources in that account to subsidize a little over SDR 2 billion in PRGF lending. Hence, the potential gap that would arise would be toward the end of the SDR 2.7 billion of loan capital. PRGF lending commitments were currently running at around

SDR 400 million per year. Such commitments might well increase, but there would be sufficient resources to implement the ESF immediately.

Mr. Prader noted that the fungibility of resources in the self-sustained PRGF was also an issue that needed to be addressed. Also, as Mr. Kremers had pointed out, the question of the nonreimbursement of the GRA of the cost of PRGF administration—around SDR 80-90 million per year—had not yet been resolved, as well as the issue of the mitigation scheme for the 1999-2000 off-market gold transaction. The costs added up, and his chair was not reassured by the G-8's commitment. The largest borrower in his constituency would pay dearly for the initiative. The Fund's borrowing members would vote with their feet if the Fund would make them pay the cost of the MDRI.

Mr. Scholar reiterated that the G-8 would provide the SDR 100 million, and that there would be no effect, as a result of the MDRI, on the rate of charge.

The Director of the Finance Department (Mr. Kuhn) said that the assumed rate of interest was in line with the WEO assumptions, which would increase from the current level of slightly over 2.5 percent over the next four years to 5 percent in 2010 and then stay constant.

The General Counsel (Mr. Hagan), in response to questions and comments from Directors, made the following statement:

> Mr. Silva-Ruete wondered whether non-HIPCs were actually experiencing a BOP need, which is necessary in order for them to be eligible to receive assistance under Article V, Section 12. As is indicated in paragraph 23 of Supplement 1, the Executive Board determined some time ago that all PRGF-eligible members have, a priori, a protracted balance of payments problem by virtue of their income levels; hence, they would qualify under Article V, Section 12.
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> In a related question, Ms. Phang asked why HIPC Initiative relief is provided to all qualifying countries regardless of per capita income, while under the MDRI there would be a per-capita-income test. In fact, in order to qualify under the HIPC Initiative, a country has to be PRGF-eligible, which eligibility is based on an income threshold—the IDA operational cutoff. It is a different income threshold than the one proposed for the MDRI, but there is an income threshold constraint nonetheless.
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> There were questions raised by Mr. Misra and Mr. Kiekens on the amendments that would allow for a transfer of subsidy resources from the PRGF and to what extent such restitutions have been done in the past. As Mr. Kuhn has indicated, this would be the first time that restitution would be made, but for the numerous reasons identified in the paper, we are of the strong view that the Fund, with the consent of all contributors, has the legal authority to effect such a transfer.

> Regarding the majority that would be required for this transfer, we have consistently taken the position that an 85 percent majority is required when SDA resources held in the PRGF Trust are to be used for a purpose that is different from the purpose at the time of the original transfer to the Trust. In this case, however, the SDA resources would continue to be used exclusively for subsidy purposes, and therefore an 85 percent majority is not required. However, to the extent to which, in the context of these overall amendments, SDA resources would not only be available for subsidies for PRGF arrangements but also for shocks, that would constitute a new purpose, and an 85 percent majority would be required.
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> Mr. Kremers asked whether there could be legal complications regarding the earmarking of resources for the HIPC Initiative sunset cases. This should be very clear in the decision: to the extent that a sunset case has a per capita income under $380, it will be eligible for MDRI relief through the use of SDA resources.
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> Finally, Mr. Rouai asked whether or not there could be legal complications in the implementation of the modified grandfathering proposal set forth in Annex 1 with respect to protracted arrears cases. As Mr. Allen has indicated, we will take another look at this again, but I wanted to assure Directors that the problem regarding extending the repurchase obligations through Article V, Section 7(G) or modifying the trust for rescheduling would not apply, because these would be notional or hypothetical repayments. The Board would not actually be taking a decision to reschedule.

Mr. Scholar said that the principle set out in the paper was that conditionality for debt relief under the MDRI should be consistent across members. In that context, it was puzzling that the conditionality proposed for the two so-called uniformity cases was significantly lighter than that applied to HIPCs, which raised some uniformity questions of its own. As the staff paper indicated, for example, for non-HIPCs, no comprehensive assessment of public expenditure management systems had ever been undertaken, and while it was true that, as Mr. Schaad had noted, a country might have been under a program and was performing successfully under that program, that was not a substitute for the necessary assurances. Conditionality under the HIPC Initiative was tougher than that which would normally be included in a Fund-supported program. Hence, given the need for consistency, the appropriate conditionality were those that would apply to pre-completion-point countries rather than to post-completion-point HIPCs.

The conditionality that had been proposed by the staff for the uniformity cases was, in fact, lighter than that which the post-completion-point countries would face, Mr. Scholar continued. First, on macroeconomic performance, paragraph 23 of the main paper said that a country would meet the macroeconomic performance criterion if it had completed a review within the previous four months. However, paragraph 14 of the supplement said that a non-HIPC would meet the same criterion if it had completed the review in the previous six months. That might not constitute a huge difference, but it was nevertheless more generous to the non-HIPCs than to the HIPCs. Similarly, paragraph 23 of the main paper said that a HIPC would need to have been implementing a PRSP for at least one year, but paragraph 15 of the supplement stated that a non-HIPC would only need to have done so for six months. It was arguable that the standard applied for public expenditure management was tougher in the case of HIPCs than the non-HIPCs.

It was not clear how the different approaches could be reconciled with the principle of consistency of treatment, Mr. Scholar considered. Non-HIPCs should be required to demonstrate the same track record of sustained economic performance, including a satisfactory track record of strong policy actions meeting the standard of upper credit tranche conditionality, and the same track record as was required of HIPCs. The staff should take another look at the issue.

Mr. Schaad said that he was greatly concerned with Mr. Scholar's explanation. Equality of treatment meant treating similar cases equally. The non-HIPCs did not have the same debt levels as the HIPCs since, as the staff had argued, those countries had been more prudent. Hence, it was not appropriate to require the non-HIPCs to satisfy exactly the same conditions as the HIPCs. His minister had agreed with the proposal at the IMFC because he had received the impression that the requirement of equality of treatment would be met. It now appeared as if the G-8 countries were stepping back from their pledge.

Mr. Scholar said that the G-8 had made exactly the same point during the Board discussion in September, and hence had been fully consistent throughout. Moreover, he had not said that the uniformity cases should be subject to exactly the same conditionality as HIPCs; he had said—carefully—that the conditionality could be calibrated in various ways. Nonetheless, what needed to be assured was for the freed-up resources to be used for the purpose for which they had been intended. The approach that had been proposed by the staff did not give sufficient assurances in that regard. There were at least two respects in which the proposed standards were looser than even those for post-completion-point HIPCs. Hence, the staff should look further at the matter, in order to reach a proposal that could command consensus across the Board.

The Director of the Policy Development and Review Department (Mr. Allen) said that the essence of the delivery of HIPC Initiative debt relief at the completion point was that of meeting a set of conditions that gave the Fund confidence that the relief, when disbursed, would be used well. The staff was trying to design conditionality that would give similar assurances with regard to the non-HIPCs. The staff would propose to make the requirement with regard to implementing the PRSP, and the time elapsed since the last review, uniform between both HIPCs and non-HIPCs. There would be required satisfactory implementation of the PRSP at least over the past six months or the equivalent, and a review of a Fund arrangement completed over the previous six months would apply in both cases.

Finally, the staff was preparing a paper for Board discussion before the end of the year—which would cover the 18 post-completion-point HIPCs and the two additional cases, Cambodia and Tajikistan—to assess whether they met the policy criteria for relief under the initiative, and if not, what remedial actions would be needed for them to qualify, the Director stated. A Board decision on the conclusions of that paper would be expected before the end of the year.

Mr. Scholar reiterated that he was not persuaded that the post-completion-point standard was the correct standard to apply to the uniformity cases. However, that should not hold up work on the other aspects of the MDRI, in order to meet the deadline. There was time to look at the issues further to reach a consensus.

The Chairman made the following summing up:

Executive Directors welcomed the opportunity to continue their discussion of the debt relief proposal initially advanced by the G-8 and considered by the Board in August and by the IMFC in September. They reaffirmed their support for further debt relief by the Fund under what they agreed to call the Multilateral Debt Relief Initiative (MDRI). Directors welcomed again the G-8 commitment to provide the resources to ensure that the Fund's financial capacity is not undermined by the MDRI and to cover, on a fair burden sharing basis, the cost of debt relief for countries that may become eligible for the HIPC Initiative under the extended sunset clause. Directors also welcomed again the G-8 commitment that donors would provide the extra resources necessary for debt cancellation at completion point for the three protracted arrears cases (Liberia, Somalia, and Sudan).

Directors concurred with staff's approach of ensuring uniformity of treatment by providing debt relief to members on the basis of a per capita income eligibility criterion, and welcomed the additional elaboration on the various legal issues raised by the approach. They endorsed the choice of a US$380 per capita income cutoff, which meets uniformity of treatment requirements by providing Special Disbursement Account (SDA) resources to the Fund's poorest members. At the same time, it balances the use of resources in the SDA and of third-party contributor resources in a manner that minimizes the need for additional resources, thereby maintaining the Fund's future concessional lending capacity. Directors agreed that SDA resources would be used to provide debt relief under the MDRI to member countries (including non-HIPCs) with incomes at or below the income cutoff. Third-party contributor resources held in the Subsidy Account of the PRGF Trust could be used, upon request of contributors and subject to the consent of all of them, to provide MDRI debt relief to HIPCs that have per capita incomes above that threshold.

Directors reaffirmed that the cutoff date on eligible debt under the MDRI should be end-2004 for all qualifying members, but the effective delivery date for debt relief would be decided on a case-by-case basis. Assuming the requisite Board decisions are effective by that time, the 18 HIPCs that have reached completion point and the two non-HIPCs eligible under the initiative could benefit from MDRI relief at the beginning of 2006, subject to the Board's confirmation of their qualification for such relief. The other HIPCs that have not yet reached their completion points would become eligible for MDRI relief upon reaching the completion point. Directors emphasized that the commencement of debt relief operations at the beginning of 2006 would hinge critically on obtaining timely consents from all contributors to the Subsidy Account of the PRGF Trust.

Most Directors agreed that the MDRI should be implemented so as to allow early repayment of the full stock of eligible debt owed to the Fund once the countries qualify for such relief. This approach would closely align with the intention of the initiators of the MDRI and the expectations of qualifying countries. Under this approach, the MDRI would be implemented over a relatively brief period. This would minimize accounting and investment issues, and therefore administrative costs and risks, for the Fund. Directors agreed that, to be consistent with this approach, financial assistance provided under the HIPC Initiative at completion point should be delivered in a similar manner. Some Directors considered that phased debt relief for post-HIPCs or non-HIPCs would better ensure that freed-up resources are used productively in pursuit of the Millennium Development Goals.

Directors stressed that conditions to qualify for debt relief under the MDRI should be consistent for pre- and post-completion-point HIPCs, as well as for non-HIPCs. In this regard, most Directors agreed that, to benefit from MDRI debt relief, post-completion point HIPCs' performance in three key areas should not have deteriorated substantially since the time the completion point was reached. These areas are: (i) macroeconomic performance; (ii) implementation of a poverty reduction strategy or a similar framework; and (iii) public expenditure management systems. For non-HIPCs eligible for MDRI debt relief from the Fund, satisfactory performance in the same three areas should be a requirement. Views were divided between those who felt that non-HIPCs are closer in circumstances to post-completion-point than to pre-completion-point HIPCs, and that entry conditionality should be designed accordingly; and those who felt that the proposed qualification requirements do not go far enough to ensure consistency of treatment with HIPCs. The latter group of Directors called for non-HIPCs to be required to demonstrate the same track record of strong policy actions meeting the standard of upper credit tranche conditionality as is required of HIPCs to receive debt relief, and asked the staff to look again at the issue of conditionality for non-HIPCs. Directors agreed that for HIPCs, a minimum six-month track record of satisfactory macroeconomic performance and implementation of poverty reduction policies would be needed to qualify for debt relief. For countries with a Fund arrangement in place, the assessment would be based on the outcome of the latest review under the program, assuming that it was completed less than six months earlier. As is the case in the HIPC Initiative, the qualification criteria should be used flexibly, taking into account a country's specific circumstances. In addition to the above criteria, Directors re-affirmed that all countries receiving debt relief must be current with their repayment obligations to international financial institutions.

Directors requested that, by end-2005, staff prepare, in collaboration with the World Bank, an assessment of the 18 post-completion point HIPCs, as well as eligible non-HIPCs, and propose for Board consideration a list of members that would qualify immediately for MDRI debt relief. Corrective actions should be proposed for post-completion point HIPCs whose performance has deteriorated substantially in any of the three areas, and for non-HIPCs whose performance is unsatisfactory. Qualification for MDRI relief would be reassessed once these remedial measures have been implemented.

Directors considered staff's proposed options for addressing the three protracted arrears cases (Liberia, Somalia, and Sudan) in the context of the MDRI. Given the complexity of the issue, Directors asked staff to give further thought to potential financing and policy implications for these cases, and looked forward to a follow-up paper on these issues.

Directors called on the Fund and the World Bank to cooperate and coordinate in the implementation of the MDRI, particularly in the areas of assessing qualification for MDRI relief and monitoring and reporting on MDG-related spending after provision of debt relief.

Most Directors agreed with the modalities proposed for post-debt relief monitoring, while acknowledging the challenges, given the fungibility of resources. They requested that progress reports on the implementation of the MDRI (including status reports on all members benefiting from MDRI) be presented to the Board before the 2006 Spring and Annual Meetings. They agreed that subsequent MDRI status reports would be included in regular joint Bank-Fund HIPC Initiative status reports.

Directors discussed the implications of the MDRI for the Fund's finances, including the overall cost, sources of financing, the impact on the Fund's interim PRGF operations, and the modalities of the Fund's future concessional lending. Some Directors requested a timely discussion of the overall longer-term concessional financing issues in the context of the MDRI and Exogenous Shocks Facility (ESF) decisions. Directors noted that the overall cost of the MDRI, excluding potential sunset clause and protracted arrears cases, would be about SDR 3.4 billion, to be financed by resources in the HIPC Umbrella Account, the Special Disbursement Account, and bilateral contributor resources in the Subsidy Account of the PRGF Trust. Additional bilateral contributions would be expected to cover the costs associated with HIPC and MDRI debt relief for the sunset clause and protracted arrears cases. Directors also noted that there is no intention to change, as a result of the MDRI, the current burden-sharing arrangements for mitigating the effect of the 1999-2000 off-market gold transactions and, hence, that there should be no impact on the rate of charge.

Directors acknowledged that for bilateral contributors to reallocate their contributions from the Subsidy Account of the PRGF Trust for MDRI debt relief to those HIPCs that have per capita incomes above the threshold of US$380, an amendment to the Subsidy Account provisions of the PRGF Trust would be needed. To become effective, this amendment would require the consent of all bilateral contributors. In this context, Directors agreed that a separate administered account or trust could be established into which the bilateral contributions from the Subsidy Account of the PRGF Trust could be transferred, and that additional modalities could be considered for receiving new contributions needed to cover costs associated with debt relief to potential sunset-clause and protracted-arrears countries. Directors urged bilateral contributors to the Subsidy Account of the PRGF Trust to consent to the needed amendment to the PRGF Trust expeditiously upon the Fund adopting the relevant decisions. This would enable the Fund to provide debt relief to member countries that meet all criteria for debt relief under the Initiative by the start of 2006.

Directors concurred that the implementation of the MDRI will require the amendment of existing decisions and the adoption of new decisions governing the use of SDA resources. Specifically, the Board will need to authorize the use of a portion of the corpus of the 1999-2000 off-market gold transactions (and not only the investment income, as is currently the case) to provide debt relief under the HIPC Initiative for all qualifying countries (that is, regardless of income levels). In addition, the Board would need to authorize the use of SDA resources to provide: (i) MDRI relief for PRGF-eligible members with per capita incomes at or below US$380; and (ii) further subsidization of the interim PRGF through the transfer of additional resources from the SDA. Many Directors were of the view that the transfers referred to in (ii) should be effected immediately upon the effectiveness of the relevant MDRI decisions. Many Directors also considered that these resources should also be made available to subsidize lending under the new Exogenous Shocks Facility.

Directors agreed that outstanding borrowing by the PRGF Trust could be repaid early to lenders in proportion to the total loan resources, thereby reducing the Fund's administrative costs and risks associated with continuing to carry and manage these obligations. Directors also urged staff to seek compensating arrangements with those bilateral contributors that are providing implicit subsidy resources through loans at below-market interest rates, since these subsidies are crucial for the continued operation of the interim PRGF.

Directors noted that the MDRI would preserve the resources in the Reserve Account of the PRGF Trust, but bilateral contributors' reallocation of their resources for MDRI relief to HIPCs above the threshold would reduce the available subsidy resources for existing and future interim PRGF loans. They took note of the staff's estimate that additional subsidy contributions of about SDR 210 million in end-2005 NPV terms would be needed to allow the full use of the available loan resources under the interim PRGF (though there remains some uncertainty over the potential additional costs of including the two non-HIPC countries). In this context, Directors welcomed the G-8's commitment to provide an additional subsidy contribution of SDR 100 million, and to consider dealing with the potential additional costs of including Tajikistan and Cambodia, if and when they arise, consistent with their commitment to ensure that the financing capacity of the Fund is not reduced.

Directors considered the modalities of the Fund's concessional operations involving the use of the Reserve Account of the PRGF Trust over the medium term. Most Directors were of the view that the proposed approach to maintain the current framework beyond the interim period would seem appropriate and should be pursued. Directors generally saw flexibility in addressing uneven demand for the Fund's concessional lending as the main advantage of this approach.

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Secretary