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May 22, 1990

To: Members of the Executive Board

From: The Acting Secretary

Subject: Suspension of Voting and Related Rights - Proposed
Decision and Draft Report to the Board of Governors on
Proposed Third Amendment of the Articles of Agreement

The attached paper is scheduled for consideration by the Executive Directors tomorrow, Wednesday, May 23, 1990. A draft decision appears on pages 2 and 3.

Mr. Gianviti (ext. 8329) is available to answer technical or factual questions relating to this paper prior to the Board discussion.

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INTERNATIONAL MONETARY FUND

Suspension of Voting and Related Rights--
Proposed Decision and Draft Report to the Board of Governors
on Proposed Third Amendment of the Articles

Prepared by the Legal Department

Approved by François Gianviti

May 22, 1990

On May 21, 1990, the Executive Board considered a staff paper setting forth a revised draft text of an amendment of the Articles of Agreement to provide for a suspension of voting and related rights of members that do not fulfill their obligations under the Articles. ^{1/} Based upon those discussions, the staff has now prepared a draft report of the Executive Board to the Board of Governors on this subject. That draft report is attached hereto for the consideration of the Executive Board. A proposed decision adopting the report and addressing related matters appears below.

The draft report is similar in structure to the report on the Second Amendment of the Articles. It comprises four parts. By way of introduction, Part I notes the present provisions of Article XXVI, Section 2 on ineligibility and compulsory withdrawal, and the request of the Interim Committee that an amendment on suspension of voting and related rights be proposed. Part II is a commentary on the proposed amendment, addressing conditions for suspension, consequences of suspension, and termination of suspension. Part III explains the procedures to be followed in considering the proposed amendment. Part IV provides the text of a resolution recommended for adoption by the Board of Governors. Attached to that draft resolution is the text of the proposed amendment itself.

The draft amendment takes into account the views expressed during the Board meeting of May 21, 1990. In particular, (i) it follows the "Alternative 1" approach presented in the earlier staff paper, so that suspension would be a necessary step between ineligibility and compulsory withdrawal, and (ii) it provides that an Executive Director casting the number of votes allotted to several members would not, upon the suspension of one of those members, immediately cease to hold office but instead would continue to serve for an interim period of no more than 30 days to allow for an election to take place.

^{1/} "Suspension of Voting and Related Rights--Draft Amendment," (SM/90/89, 5/11/90).

Proposed Decision

The following draft decision is proposed for adoption by the Executive Board:

1. Pursuant to the request of the Interim Committee that an amendment of the Articles of Agreement be proposed providing for suspension of voting and related rights of members that do not fulfill their obligations under the Articles, the Executive Board:

- (a) adopts the "Report of the Executive Board to the Board of Governors on the Proposed Third Amendment of the Articles of Agreement of the International Monetary Fund";
- (b) proposes the introduction in the Articles of Agreement of the modifications included in the Proposed Third Amendment attached to the Resolution in Part IV of the Report; and
- (c) recommends the adoption by the Board of Governors of the Resolution in Part IV of the Report.

2. The Executive Board notes that the Secretary has been authorized and directed by the Chairman of the Board of Governors of the Fund to bring before the Board of Governors on his behalf by rapid means of communication the proposal of the Executive Board introducing modifications in the Articles of Agreement pursuant to the request of the Interim Committee. The Executive Board authorizes and directs the Secretary to send to each member of the Fund this proposal of the Executive Board together with the Report, with a request for a vote by each Governor on the Resolution in Part IV of the Report.

3. The Board of Governors is requested, pursuant to Section 13 of the By-Laws, to vote without meeting on the Resolution in Part IV of the Report. To be valid, votes must be received at the seat of the Fund on or before June 28, 1990. Votes received after that date will not be counted.

4. The effective date of the Resolution of the Board of Governors shall be the last day allowed for voting.

5. The Secretary is authorized to take such action as he shall deem necessary or appropriate to carry out the purposes of this decision.

Report of the Executive Board to the Board of Governors
on the Proposed Third Amendment of the
Articles of Agreement of the International Monetary Fund

Part I. Introduction

1. Article XXVI, Section 2(a) of the Fund's Articles of Agreement empowers the Fund to declare a member ineligible to use the general resources of the Fund if the member fails to fulfill any of its obligations under the Articles. Such a declaration may be made by a decision of the Executive Board carried by a majority of the votes cast. Article XXVI, Section 2(b) provides that if the member persists in its failure to fulfill any of its obligations under the Articles, it may be required to withdraw from membership by a decision of the Board of Governors carried by a majority of the Governors having eighty-five percent of the total voting power.

2. The Interim Committee of the Board of Governors included the following sentence in its communiqué of May 8, 1990:

"In order to deal with the rare cases where it is evident that a member with arrears to the Fund is persistently not cooperating with the Fund, the Committee invited the Executive Board to propose to the Board of Governors, by end May 1990, the text of an amendment of the Articles providing for suspension of voting and related rights of members that do not fulfill their obligations under the Articles."

3. The Executive Board is hereby proposing the text of such an amendment. The proposed amendment would add new provisions to the Articles, in Article XXVI, Section 2 and in a new Schedule L, under which a member's voting rights and certain related rights may be suspended by the Fund if the member, having been declared ineligible to use the general resources of the Fund, persists in its failure to fulfill any of its obligations under the Articles. The Commentary in Part II of this Report analyzes the proposed amendment and describes the main aspects of the new power that would be conferred upon the Fund. Part III describes the procedure for the adoption of the proposed amendment. Part IV proposes a Resolution for adoption by the Board of Governors. The text of the proposed amendment is attached to the proposed Resolution.

Part II. Commentary

This Commentary examines, first, the conditions for the imposition of suspension of voting and related rights of a member, then the consequences of suspension, and finally the conditions and effects of a termination of suspension.

A. Conditions of Suspension

1. The conditions applicable to a suspension of voting and related rights of a member are set out in a revised version of Article XXVI, Section 2. Suspension forms part of a required sequence: it can be imposed only after the expiration of a reasonable period of time following a declaration of ineligibility of the member to use the general resources of the Fund under Article XXVI, Section 2(a), and compulsory withdrawal of the member can be required by the Fund under Article XXVI, Section 2(c) only after the expiration of a further reasonable period of time following the decision of suspension of voting rights of the member.

2. Under Article XXVI, Section 2(d), the member must be informed in reasonable time of the complaint against it, and must be given an adequate opportunity for stating its case, before the Fund can decide to suspend its voting rights. The provision means that the complaint preceding a decision of suspension is distinct from the complaints that must be made before the member is declared ineligible to use the general resources of the Fund and before the member is required to withdraw.

3. Suspension requires a decision of the Executive Board by a seventy percent majority of the total voting power. It can be imposed in case of breach of any obligation under the Articles, except, in accordance with Article XXIII, Section 2(f), for the breach of an obligation with respect to special drawing rights.

B. Consequences of Suspension

1. Article XXVI, Section 2(b) provides that "the Fund may ... suspend the voting rights of the member" and that "[d]uring the period of the suspension, the provisions of Schedule L shall apply." Therefore, while the decision of the Fund is to suspend the voting rights of the member, the precise consequences of that decision are set out in Schedule L, and they include not only the suspension of voting rights of the member (paragraph 1 of Schedule L), but other consequences as well (paragraphs 2 to 4 of the same Schedule).

2. The consequences of suspension listed in Schedule L are automatic, temporary, indivisible, and exhaustive. They are automatic in the sense that they take effect without the need for any further action on the part of the Fund. They are temporary because their effects cease upon termination of the suspension (see Section C below). They are indivisible, since all the consequences set out in Schedule L apply as a unit; the Fund cannot decide that some of the consequences in the Schedule shall apply and some others shall not apply. Finally, they are exhaustive, because no consequence other than those listed in the Schedule can attach to the decision of suspension.

3. A decision to suspend the voting rights of a member results in the suspension of the right of the member to participate in the adoption of a proposed amendment of the Articles is suspended (paragraph 1(a) of Schedule L). Therefore, the member will not be asked whether it accepts a proposed amendment and will not be counted among the members that have accepted it, and the number of votes allotted to the member will not be included in the voting power of the members accepting the proposed amendment, for purposes of the last sentence of Article XXVIII(a). In addition, the member is excluded from the total number of members, and the number of votes allotted to the member are excluded from the total voting power, for purposes of the same sentence (paragraphs 1(a) and 2 of Schedule L, respectively). As a result of these provisions, the suspended member is to be disregarded for purposes of ascertaining whether a proposed amendment has been accepted by the required majorities. Such an amendment will nevertheless enter into effect for the suspended member, as for all other members, in accordance with Article XXVIII(c). The suspension of the voting rights of the member does not affect, however, the right of the member to participate in the adoption of, and otherwise be counted for purposes of, proposed amendments that require the acceptance of all members under Article XXVIII(b) or proposed amendments that pertain exclusively to the SDR Department. The member shall be treated like non-suspended members for the purposes of the adoption of such amendments (although, as a result of the suspension, pursuant to paragraph 3 of Schedule L, there will not be any Governor, Executive Director, or Councillor for the member to participate in the process of recommendation and approval of the amendment. The right to participate in the adoption of a proposed amendment must be distinguished from the right to propose an amendment; the suspension of voting rights of the member does not preclude the member from proposing an amendment in accordance with the first sentence of Article XXVIII(a).

4. The other voting right of the member (understood in a broad sense) that is suspended (paragraph 1(b) of Schedule L) is the right to select or participate in the selection of officials of the Fund who are entitled to cast the number of votes allotted to members, namely a Governor and an Alternate Governor, as well as an Executive Director (Councillors and Alternate Councillors are also named in case the Council is established). The suspension affects the right of the member to select such an official either on its own or with other members of a group, and either by way of appointment or by way of election. Alternates to Executive Directors are not included because they are appointed by the Executive Directors and not by the members (Article XII, Section 3(e)), and Associates in the Council are omitted because they are not entitled to cast votes (Schedule D, paragraph 1).

5. The first sentence of paragraph 2 of Schedule L provides that the number of votes allotted to a suspended member shall not be cast in any organ of the Fund (i.e., the Board of Governors, the Council if it is established, and the Executive Board). This provision complements the provisions of paragraph 3 of Schedule L, under which the Governor, the

Alternate Governor and the Executive Director (as well as the Councillor and the Alternate Councillor, if the Council is established) for the member cease to hold office, whereupon they are unable to cast the number of votes allotted to the suspended member. While paragraph 3 of Schedule L sets out the rule that these officials cease to hold office immediately upon effectiveness of the decision of suspension, it allows, in specified circumstances, an Executive Director (and a Councillor to remain in office for a short period of time (see paragraph 7 below). Pursuant to paragraph 2 of Schedule L, the Executive Director (and the Councillor) for the suspended member shall not cast the votes of the suspended member during that period of time.

6. The second sentence of paragraph 2 has the effect of excluding the number of votes allotted to the member from the calculation of the total voting power, not only for purposes of the acceptance of proposed amendments of the Articles (see paragraph 3 above), but also for purposes of the adoption of decisions by organs of the Fund. It is not necessary to exclude the Governor, Councillor, and Executive Director for the suspended member from the calculation of quorums under the Articles, since these officials cease to hold office, and therefore cease to be regarded as Governor, Councillor, and Executive Director for any purpose under the Articles, including the calculation of quorums, pursuant to paragraph 3 of Schedule L.

7. Under paragraph 3 of Schedule L, all the officials selected by the member who are entitled to cast the number of votes allotted to the member cease to hold office (the Alternate to the Executive Director for the member is not referred to in the provision, because he is not appointed by the member, but by the Executive Director who can replace him at any time). This means that these officials cease to be officials of the Fund for all purposes under the Articles.

(a) The principle is that these officials cease to hold office immediately upon effectiveness of the decision of suspension. This principle applies to the Governor and the Alternate Governor appointed by the member. It also applies to the Executive Director appointed by the member, if the member may appoint an Executive Director under Article XII, Section 3(b) or (c), except, as discussed below, in the case of an appointed Executive Director who is entitled to cast the votes of members other than those that appointed him, pursuant to an agreement under Article XII, Section (i)(ii). Finally, the principle that the official ceases to hold office immediately upon the effectiveness of the decision of suspension applies also to an Executive Director elected by one member that has later been suspended, or by several members, all of which have later been suspended (the principle also applies to a Councillor and Alternate Councillor in similar circumstances).

(b) The principle that the officials chosen by the member shall cease to hold office immediately receives an exception in the case of an Executive Director who is entitled to cast the number of votes of other, non-suspended

members, in order to allow the number of votes allotted to these members to continue to be cast (the same exception applies to a Councillor and an Alternate Councillor who were appointed by a group of members that include non-suspended members). This may apply either when the Executive Director was elected by more than one member, or when the Executive Director was appointed by a member and it was agreed that this Executive Director would cast the number of votes allotted to other members in accordance with Article XII, Section 3(i)(ii). Then, the Executive Director in office when the decision of suspension became effective is entitled to remain in office until another Executive Director is elected to replace him. This new Executive Director, who may be the same person, will be elected by the non-suspended members by a majority of the votes cast. Once elected, he will be entitled to cast the number of votes allotted to all such non-suspended members and will serve for the remainder of the term of the Executive Director who ceased to hold office as a result of the suspension. No such election will take place, however, if a regular election of Executive Directors under Article XII, Section 3(d) occurs beforehand. The Executive Director in office when the decision of suspension became effective shall cease to hold office not later than 30 days after the date of effectiveness of the decision of suspension, even if another Executive Director has not yet been elected by that time. It is expected that a period of 30 days will provide sufficient time for the other members of the constituency to hold an election.

8. The amendment does not contemplate that, if a member having one of the five largest quotas were suspended, the member with the sixth largest quota would be called upon to appoint an Executive Director so as to maintain at five the minimum number of Executive Directors appointed on account of the size of quotas. Instead, the number of Executive Directors appointed by members would be reduced during the period of the suspension.

9. Paragraph 4 of Schedule L confers an entitlement on suspended members to send representatives to meetings of the Board of Governors and the Executive Board (and the Council if it is established) whenever these organs consider requests made by the member or matters that particularly affect the member. The provision does not create an entitlement for suspended members to send representatives to meetings of committees of these organs of the Fund when such matters are under consideration, because non-suspended members do not have such an entitlement under the Articles. In the cases where suspended members do not have an entitlement to send representatives to meetings of these organs or of their committees, the provision does not prohibit, however, such representatives from being invited to such meetings in accordance with the applicable rules of procedure.

C. Termination of Suspension

Conditions for Termination

1. The termination of suspension requires a decision of the Executive Board carried by the same majority required for the imposition of suspension, namely, seventy percent of the total voting power.

2. The amendment leaves it to the Fund to decide when to terminate suspension. In particular, the Fund is not compelled to terminate the suspension upon resumption by the suspended member of compliance with all of its obligations under the Articles, nor is it prohibited from terminating the suspension prior to the resumption by the member of compliance with all such obligations, if this were considered appropriate. The Fund has similar flexibility under the Articles with respect to termination of a member's ineligibility to use the general resources of the Fund.

Effects of Termination

3. Termination of suspension revives the voting and related rights of the member that had been suspended. Thus, the member may immediately participate in the adoption of a proposed amendment of the Articles. For instance, if a proposed amendment had been submitted to members for their acceptance under Article XXVIII(a), and the Fund had not yet certified to members that the required majorities had been obtained by the time the member's suspension was terminated, the member shall be asked whether it accepts the proposed amendment and both the member and the number of votes allotted to it shall be counted for purposes of calculating whether the majorities of three-fifths of the members and of eighty-five percent of the total voting power have been obtained.

4. The member is also able to appoint a Governor and an Alternate Governor, as well as a Councillor and an Executive Director if it is a member that appoints such officials, immediately upon termination of the suspension. In contrast, members that may not appoint an Executive Director would have to wait until the next general election of Executive Directors under Article XII, Section 3(d) to elect or participate in the election of an Executive Director. The only exception would be if the suspension were terminated before another Executive Director is elected in accordance with paragraph 3(c) of Schedule L; in that case, the election required by Schedule L would take place notwithstanding the termination of the suspension, and the member could participate in that election. If, in contrast, the suspension were terminated after the election of another Executive Director pursuant to Schedule L and the office of that other Executive Director subsequently became vacant (for instance because that other Executive Director resigned), the formerly suspended member could not participate in any special election that would take place to fill the vacancy in accordance with Article XII, Section 3(f), since it would not have participated in the election of the Executive Director to be replaced.

The same analysis would apply with respect to the appointment of a Councillor appointed by a group of members: the member whose suspension had been terminated could participate in the appointment of a Councillor under Schedule D at the time of the next general election of Executive Directors, but could not participate in any special appointment of a Councillor prior to the next general election, except if the suspension were terminated before the appointment of a new Councillor under paragraph 3(b) by the non-suspended members of its group.

5. The number of votes allotted to the formerly suspended member could again be cast in organs of the Fund as soon as the member had appointed, elected or participated in the appointment or election of a Governor, Alternate Governor, Councillor, Alternate Councillor, or Executive Director.

Part III. Procedure

1. The procedure for the adoption of modifications in the Articles of Agreement is set forth in Article XXVIII. Under those provisions, a proposed amendment is to be communicated to the Chairman of the Board of Governors for consideration by the Board of Governors. If the proposed amendment is approved by the Board of Governors, the Fund is to ask all members whether they accept it. When three-fifths of the members, having eighty-five percent of the total voting power, have accepted the proposed amendment, the Fund is to certify that fact by a formal communication to all members. Under Article XXVIII(c), an amendment enters into force for every member, regardless of whether or not it has accepted the amendment, three months after the date of that communication unless a shorter period is specified. In the case of the amendment now being proposed, the Executive Board recommends that it should enter into force on the date of the formal communication.

2. Part IV of this Report contains the text of a Resolution, to which is attached the text of the proposed amendment discussed above. The Chairman of the Board of Governors has requested that on his behalf the Secretary of the Fund bring the Resolution and proposed amendment before the Board of Governors for its approval. It is pursuant to this request that the Secretary is transmitting this Report to the Board of Governors.

3. In the judgment of the Executive Board, and particularly in view of the desirability of an early completion of the amendment process, 1/ the action requested of the Board of Governors should not be postponed until the next regular meeting of the Board and does not warrant the calling of a

1/ In its May 8 communiqué, the Interim Committee noted its "consensus that, as part of the overall quota increase package, no increase in quota shall become effective before the effective date of such an amendment, and that every effort should be made by members to ensure that both the quota increase and the amendment shall be effective before end 1991."

special meeting of the Board. For this reason, the Executive Board, pursuant to Section 13 of the By-Laws, requests Governors to vote without meeting. To be valid, votes must be received at the seat of the Fund on or before June 28, 1990. The Resolution will be adopted if replies are received from a majority of the Governors exercising two-thirds of the total voting power and if a majority of the votes is cast in favor of the Resolution. The Resolution must be voted on as a whole.

Part IV. Resolution

WHEREAS the Interim Committee of the Board of Governors has invited the Executive Board to propose an amendment of the Articles of Agreement of the International Monetary Fund providing for suspension of voting and related rights of members that do not fulfill their obligations under the Articles; and

WHEREAS the Executive Board has proposed such an amendment and prepared a Report on the same; and

WHEREAS the Chairman of the Board of Governors has requested the Secretary of the Fund to bring the proposal of the Executive Board before the Board of Governors; and

WHEREAS the Report of the Executive Board setting forth its proposal has been submitted to the Board of Governors by the Secretary of the Fund; and

WHEREAS the Executive Board has requested the Board of Governors to vote on the following Resolution without meeting, pursuant to Section 13 of the By-Laws of the Fund;

NOW, THEREFORE, the Board of Governors, noting the said Report of the Executive Board, hereby RESOLVES that:

1. The proposals for modifications (Proposed Third Amendment) that are attached to this Resolution and are to be incorporated in the Articles of Agreement of the International Monetary Fund are approved.
2. The Secretary of the Fund is directed to ask, by letter or telegram, all members of the Fund whether they accept, in accordance with the provisions of Article XXVIII of the Articles, the Proposed Third Amendment.
3. The circular letter or telegram to be sent to all members in accordance with 2 above shall specify that the Proposed Third Amendment shall enter into force for all members as of the date on which the Fund certifies, by formal communication

addressed to all members, that three-fifths of the members, having eighty-five percent of the total voting power, have accepted the modifications.

Proposed Third Amendment
of the Articles of Agreement
of the International Monetary Fund

The Governments on whose behalf the present Agreement is signed agree as follows:

1. The text of Article XXVI, Section 2 is hereby amended to read as follows:

"(a) If a member fails to fulfill any of its obligations under this Agreement, the Fund may declare the member ineligible to use the general resources of the Fund. Nothing in this Section shall be deemed to limit the provisions of Article V, Section 5 or Article VI, Section 1.

(b) If, after the expiration of a reasonable period following a declaration of ineligibility under (a) above, the member persists in its failure to fulfill any of its obligations under this Agreement, the Fund may, by a seventy percent majority of the total voting power, suspend the voting rights of the member. During the period of the suspension, the provisions of Schedule L shall apply. The Fund may, by a seventy percent majority of the total voting power, terminate the suspension at any time.

(c) If, after the expiration of a reasonable period following a decision of suspension under (b) above, the member persists in its failure to fulfill any of its obligations under this Agreement, that member may be required to withdraw from membership in the Fund by a decision of the Board of Governors carried by a majority of the Governors having eighty-five percent of the total voting power.

(d) Regulations shall be adopted to ensure that before action is taken against any member under (a), (b), or (c) above, the member shall be informed in reasonable time of the complaint against it and given an adequate opportunity for stating its case, both orally and in writing."

2. A new Schedule L is added to the Articles, to read as follows:

"Schedule L

Suspension of Voting Rights

In the case of a suspension of voting rights of a member under Article XXVI, Section 2(b), the following provisions shall apply:

1. The member shall not:
 - (a) participate in the adoption of a proposed amendment of this Agreement, or be counted in the total number of members for that purpose, except in the case of an amendment requiring acceptance by all members under Article XXVIII(b) or pertaining exclusively to the Special Drawing Rights Department;
 - (b) appoint a Governor or Alternate Governor, appoint or participate in the appointment of a Councillor or Alternate Councillor, or appoint, elect, or participate in the election of an Executive Director.
2. The number of votes allotted to the member shall not be cast in any organ of the Fund. They shall not be included in the calculation of the total voting power, except for purposes of the acceptance of a proposed amendment pertaining exclusively to the Special Drawing Rights Department.
3.
 - (a) The Governor and Alternate Governor appointed by the member shall cease to hold office.
 - (b) The Councillor and Alternate Councillor appointed by the member, or in whose appointment the member has participated, shall cease to hold office, provided that if such Councillor was entitled to cast the number of votes allotted to other members whose voting rights have not been suspended:
 - (i) another Councillor and Alternate Councillor shall be appointed by such other members under Schedule D; and
 - (ii) pending such appointment, the Councillor and Alternate Councillor shall continue to hold office, but for a maximum of 30 days from the date of suspension.
 - (c) The Executive Director appointed or elected by the member, or in whose election the member has participated, shall cease to hold office, provided that if such Executive Director was entitled to cast the number of votes allotted to other members whose voting rights have not been suspended:
 - (i) another Executive Director shall be elected for the remainder of the term by such other members; a majority of the votes cast shall be required for election; and
 - (ii) pending such election, the Executive Director shall continue to hold office, but for a maximum of 30 days from the date of suspension.

4. The member shall be entitled to send a representative to attend any meeting of the Board of Governors, the Council, or the Executive Board, but not any meeting of their committees, when a request made by, or a matter particularly affecting, the member is under consideration."

