

DOCUMENT OF INTERNATIONAL MONETARY FUND  
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**IMMEDIATE  
ATTENTION**

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CONFIDENTIAL

September 9, 1988

To: Members of the Executive Board

From: The Secretary

Subject: Report of the Executive Board to the Interim Committee of  
the Board of Governors on Overdue Financial Obligations  
to the Fund

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The attached report of the Executive Board to the Interim Committee of the Board of Governors on overdue financial obligations to the Fund takes into account the suggestions made by Executive Directors at EBM/88/140 (9/6/88). It is not proposed to bring the report to the agenda for discussion unless an Executive Director so requests by noon on Wednesday, September 14, 1988. In the absence of such a request, the report will be transmitted to the Members and Associates of the Interim Committee as ICMS/Doc/88/15.

Att: (1)

INTERNATIONAL MONETARY FUND

Report of the Executive Board to the  
Interim Committee of the Board of Governors  
on Overdue Financial Obligations to the Fund

September 9, 1988

1. Introduction

The communiqué of the Interim Committee issued after its meeting on April 14-15, 1988 stated that:

In its discussion of conditionality, the Committee reaffirmed the cooperative nature of the Fund and stressed the importance of preserving the revolving character of its resources. Members should continue to give the highest priority to fulfilling their financial and other obligations to the institution. Failure to honor these obligations had adverse effects on overdue members' financial standing and imposed an undue burden on other members. The Committee requested the Executive Board to review the question of the overdue financial obligations and to submit a report at the next meeting of the Committee on measures to reduce and eventually eliminate arrears.

In the 1970s, most of the members now facing protracted arrears to the Fund relied heavily on foreign assistance or other capital inflows to finance their sizable external imbalances. By the early 1980s, the economic and external payments positions of these countries had weakened markedly, reflecting both adverse external developments and inadequate economic policies. Serious debt servicing difficulties emerged and capital inflows, especially from private sources, declined sharply. These members found it increasingly difficult to meet their debt service obligations, including those to the Fund. It should be emphasized, however, that most members faced with adverse external circumstances have managed to stay current on their financial obligations to the Fund.

Overdue financial obligations to the Fund have increased from SDR 60 million at the end of 1983 to SDR 2.4 billion as of end-August 1988, of which SDR 1.9 billion was overdue for six months or more (see Attachment I, Table 1). Fund credit outstanding to the 13 members presently subject to complaints amounted to SDR 3.5 billion as of August 31, 1988 (Attachment I, Table 2), or 13 percent of total Fund credit outstanding. Eight of these members have been declared ineligible to use the general resources of the Fund.

The problem of protracted overdue obligations to the Fund, while remaining confined to a relatively few members, poses serious costs and risks not only for the individual members concerned but for the membership at large and for the Fund itself, affecting its financial integrity and the credibility of the economic programs supported by the Fund. It is vital for the financial position and future role of the Fund in the international monetary system as a cooperative monetary institution that the problem of arrears be solved early. A few Directors indicated that the willingness of their authorities to agree to increases in the Fund's resources could be impaired, while a large majority of the Board considers that a substantial increase in quotas to be decided before April 30, 1989 is well justified. Executive Directors have emphasized the Fund's central role in the international monetary system and its function in supporting policies without which the effectiveness of financial assistance provided by other creditors and donors would be seriously undermined. Resolution of the cases of arrears and restoration of access of the members concerned to Fund resources are therefore of broad international interest. Solutions in many of the present cases of protracted arrears will require special attention and exceptional efforts by the international community at large. The intent would be to pave the way for a restoration of orderly relations with all creditors and donors, renewed financial flows, and a resumption of sustained economic growth.

To meet the problem of overdue obligations, the Fund has implemented and adapted over time a series of policies and practices, summarized in Attachment II. It has also taken steps to strengthen its financial position, primarily by protecting income from the effects of overdue charges and building up its precautionary balances, financed by its debtor and creditor members through the "burden sharing" mechanism (Attachment I, Table 3). These protective actions have, however, imposed substantial direct costs on members, debtors and creditors alike, that meet their obligations to the institution. Moreover, while basically protecting the Fund's income position, they do not fully address the risks and effects on the Fund's liquidity and financial position arising from overdue repurchases.

Executive Directors are of the view that there is an urgent need for new initiatives to solve the problem of arrears and to prevent its reemergence. This report proposes for the Committee's consideration and guidance a framework for a revitalized and strengthened approach to resolving the problem of arrears, consisting of three broad elements: preventive actions, intensified international collaboration, and remedial measures. The Executive Board also intends to maintain and, as appropriate and feasible, strengthen measures to safeguard the financial position of the Fund in light of the problem of overdue financial obligations to the Fund.

In presenting the general framework outlined below, Executive Directors have emphasized that the proposed approach should be viewed in light of the following general principles. First, given the pervasive effects of arrears on the Fund and its membership and the deep difficulties facing many members now having protracted arrears, a positive resolution of the problem must be collaborative in nature, involving not only the member concerned but also the Fund, its membership, and the international community in general. Second, Executive Directors have stressed the unique position of the Fund as an international cooperative institution, its role in the international monetary system, the revolving nature of its resources, and the consequent need for all members, creditors and debtors alike, in practice, to treat the Fund as a preferred creditor. Accordingly, all members should accord the highest priority to the settlement of financial obligations to the Fund. A few Executive Directors suggested that recourse to the provisions of the Articles of Agreement regarding rescheduling of repurchases and payment of charges in local currency would be in order in exceptional cases. The majority of Directors considered, however, that the Fund must avoid opening the way to rescheduling or payment of charges in local currency, which could impair its role in the international monetary system and its effectiveness in the debt strategy. Third, Executive Directors have also emphasized that this approach is to be regarded as a broad strategy and framework for action. The situations and positions of individual countries vary markedly. The strategy may not be applicable to all countries facing protracted arrears, and it is to be expected that the detailed elements of the approach to be taken with respect to each will need to be determined on a case-by-case basis. The Executive Board notes that a number of specific aspects will require further consideration in light of the Committee's guidance.

## 2. Preventive Actions

The Fund has given increasing attention to the effectiveness of the conditionality applied to the use of its resources and to strengthening the safeguards that give confidence that members will be in a position to settle their obligations to the Fund as they fall due. The Fund has also sought to secure adequate assurances that programs are fully financed from the outset and to assure an appropriate balance between resources provided by the Fund and other sources of financing. The use of medium-term scenarios has become more extensive and refined as part of the Fund's efforts to ensure medium-term viability, an adequate level of international reserves to cushion against exogenous shocks, and the capacity to repay the Fund according to schedule. Explicit assessments of capacity to repay the Fund have become a feature of staff papers on requests for use of Fund resources. The use of exceptional access levels and the front-loading of disbursements have been reduced.

Executive Directors will seek further to strengthen policies to prevent the emergence of new cases of arrears in the future. In adapting policies on Fund conditionality, increasing attention will continue to be given to the experience gained with the implementation of programs and to improvements in program design. The design of Fund-supported programs needs to take into account the economic conditions of the country concerned; in this regard, structural aspects of members' adjustment problems and the need for growth-oriented policies have received increased emphasis through the adoption of new policies and the adaptation of existing ones. Directors emphasized the need for the Fund to broaden its assessments of members' capacity to repay and, in this connection, to give close attention to the overall levels of indebtedness of these countries. Where appropriate, and consistent with the case-by-case approach of the debt strategy, the Fund will assist member countries in the arrangement of appropriate debt restructuring and/or debt reduction operations with a view to alleviate excess debt and thus provide better safeguards for the utilization of Fund resources.

Executive Directors stressed the importance of continued and strengthened efforts to prevent the emergence of new cases of overdue obligations to the Fund and to forestall the deterioration of potential or existing arrears problems before they surface or become very difficult to resolve. They have requested the management and staff to give particular attention to strengthening preventive aspects in developing and presenting proposals for the use of Fund resources, which may, on a case-by-case basis, include such reserve management practices as would help ensure that members have on hand sufficient SDRs or other readily available resources to meet forthcoming obligations to the Fund as they fall due. Such practices would be intended to improve the prospects for timely payment to the Fund and help safeguard against possible interruption of the member's program; they would not reduce the need for programs to have adequate underlying strength, design, and financing. Executive Directors emphasized the critical importance of members' implementation of their adjustment programs and noted that, in appropriate cases, prior actions could be required to provide needed assurances regarding implementation.

### 3. Intensified International Collaboration

While the actions outlined above should help to prevent new cases of arrears from arising, the problems faced by members with sizable overdue obligations to the Fund are of a depth and nature which will require resolution and perseverance by all the parties involved. The Executive Board has considered a framework for organizing an intensified collaborative effort of the international community to resolve problems of protracted arrears to the Fund. This approach would be implemented on a case-by-case basis with adaptations appropriate to the individual circumstances, and would not be expected to

apply generally or simultaneously to all members having protracted arrears to the Fund. The principal determinants in each individual case would be the willingness of the member to embark on, and sustain, the required growth-oriented adjustment policies, and the preparedness of donors and creditors, including multilateral institutions, to provide supporting financing on appropriate terms. This approach would consist of three key, integrated elements, all clearly set forth at the outset.

The first element is the adoption and forceful implementation of a medium-term program of strong comprehensive economic reforms by the member with overdue obligations to the Fund. Frequently, the member's poor record of implementation of economic policies would seem to necessitate the establishment of a new track record in order to overcome doubts about the ability of the member to overcome its payments difficulties.

The member's economic program would represent a decisive break with the past, and be part of a medium-term strategy to achieve sustained growth and external viability. The member would develop the program in collaboration with the Fund and, as appropriate, the World Bank, and the program would be submitted to the Executive Board to obtain its endorsement that it meets the Fund's conditionality standards. In this phase, initial external financial assistance would be an important signal of the international community's willingness to support the appropriate foreign exchange requirements of the program. The program would not involve access to Fund resources while arrears remained outstanding. The member would be expected to meet financial obligations to the Fund as they fell due during the program, although this should not be interpreted as relieving it of responsibility for the settlement of all its overdue obligations to the Fund. In presenting programs, the Fund staff would provide an analysis of the factors that had led to the emergence of overdue obligations to the Fund and of the member's prospective debt-servicing capacity.

The second element of this approach, framed in the context of continuing implementation by the member of a strong adjustment effort, would center on the design of financing arrangements needed to mobilize resources for the clearance of overdue obligations to the Fund, and the organization of other financing needed to support the continuing adjustment effort. Such arrangements could include, if appropriate, bridge financing, debt rescheduling, and new money. In addition, where appropriate, an important complement to the member's adjustment program in the initial phase would be the establishment of an escrow account for the purpose of clearing the arrears with the Fund. Contributions to the escrow account should be provided by the debtor member through reserve accumulation, as well as by creditors and donors. The financing arrangements developed should in no way jeopardize any new resources that may be provided by the Fund.

The third element would comprise restoration of normal relations between the member and the Fund in the context of the Executive Board's approval of an arrangement involving use of Fund resources in support of the member's medium-term growth-oriented adjustment program. Many Executive Directors have stressed the need for an appropriate financing role for the Fund following clearance of the arrears. Some, for instance, have considered the possibility of some front-loading of the Fund's general resources, while others have referred to the possibility of some front-loading of ESAF resources. In particular, a number of Executive Directors expressed interest in the proposal of the U.K. Chancellor of the Exchequer that retroactive (or front-loaded) access under the ESAF be considered for low-income countries, once they have established a successful record of policy implementation under an economic program and have become current with the Fund. In some circumstances, where an economic program has yielded satisfactory performance and convincing assurances on the future stance of economic policies, some front-loading of the Fund's regular or ESAF resources may be justified. Directors will give further consideration to this matter in the near future. Use and phasing of any Fund resources would need to be determined on a case-by-case basis and to be consistent with the Fund's policies and practices, including the applicable access limits and the need for satisfactory assurances regarding the overall availability of financing and the member's capacity to repay. In this connection, Executive Directors have reaffirmed that ESAF resources are to be used in support of strong programs of structural reform, and only after the member has re-established a satisfactory track record with the Fund. ESAF resources are not to be used for the purpose of shifting the burden or risk of overdue obligations from the Fund's General Resources Account. This principle would need to be respected in devising financial arrangements for the clearance of arrears to the Fund and for support of the member's continuing adjustment efforts.

The magnitude of financial resources and the degree of cooperation and coordination that will be required for this strategy to succeed is, in some cases, beyond the customary experience of the various parties involved, including, in many instances, agencies and institutions which have not in the past had occasion to work in close collaboration with the Fund. For these reasons, the Executive Board is of the view that, for the collaborative approach to succeed, it will be important in some cases for the Fund to take the initiative to promote the establishment of support groups of major donor and creditor countries for members with substantial arrears to the Fund that are prepared to cooperate in this strategy and willing to implement fundamental economic and financial reforms.

Although the form of such support groups might differ from case to case, they would generally include high-level governmental representatives, and would have a crucial coordinating role with respect to financing. A number of Executive Directors have indicated that their authorities would be prepared, under appropriate conditions and

safeguards, to participate in support groups that may be established for individual countries, without implying a commitment to provide financing in any particular amount or form. Further consideration will need to be given as appropriate in particular cases to the possible features of such groups, including, inter alia, their composition, timing of establishment, precise functions, and role of the chairing creditor.

The Fund itself would of course need to play a central role. The management and staff would have an active part in the process of collaboration and coordination, for instance, maintaining contacts with the support group, in particular as regards the process of matching a program's financing requirements with available resources and engaging in dialogue, as appropriate, with the support group on progress under the program. The Executive Board, which would remain solely responsible for any commitment of Fund resources, would be involved from the outset, in considering initial adjustment programs and subsequent Fund arrangements, assessing financing needs, reviewing developments under Fund-endorsed programs, and more broadly in evaluating the overall implementation of the collaborative approach.

#### 4. Remedial Measures

A number of Executive Directors expressed the view that the most effective deterrent against arrears to the Fund is the prospect for a member of increased financial isolation and prolonged economic deterioration. Nonetheless, most Executive Directors considered that, as part of a strategy offering collaborative solutions, the range of remedial measures to be taken or to be considered should be widened in order to demonstrate clearly the membership's determination to deal firmly with any member not prepared to cooperate actively in maintaining or normalizing its relations with the Fund. In considering certain of the actions outlined below, Executive Directors noted that, as a matter of equity, members failing to meet their obligations to the Fund could not expect to receive the same benefits of membership as those that have taken the actions necessary to fulfill their obligations.

In this connection, a number of Executive Directors considered that it would be important to distinguish between members that would seem to be in a position to meet their obligations to the Fund but are unwilling to do so, and those that are willing to pay but unable to do so. To this effect, they have suggested the establishment of objective criteria, and have considered that further analysis of such criteria or indicators could be of assistance to the Executive Board in assessing the relative performance of members in arrears to the Fund and could, indeed, complement more broadly the continuing effort to extend and strengthen the Fund's analyses of capacity to repay in connection with use of Fund resources. The Executive Board is, however, mindful that there are inherent difficulties in making such distinctions and that a

considerable element of judgment would be required, including judgment whether a member in arrears is collaborating in an effort to normalize relations with the Fund. The Executive Board will return to this matter in the near future.

The Executive Board has discussed and will give further consideration to the following possibilities for extending the range of remedial actions.

a. Most Executive Directors have agreed in principle that a member must first discharge its overdue obligations to the General Resources Account before it would be permitted to pay for an increase in its quota in connection with the Ninth General Review; and that, in the event the quota payment were not made within a prescribed period, the proposal for an increase in quota would lapse. In the view of these Directors, specific provisions to implement this approach should be incorporated into decisions to be taken in connection with the Ninth General Review of Quotas.

b. Most Executive Directors are agreed that, in the absence of clear willingness on the part of a member to cooperate with the Fund in the resolution of its problems, withdrawal of technical assistance should be considered on a case-by-case basis, paying due regard to the need to maintain a dialogue with these members. A number of Executive Directors noted that the Fund's technical assistance is a scarce resource in heavy demand and that the continued provision of such assistance in such cases, particularly where not directly related to settlement of obligations to the Fund, would inappropriately be at the expense of other members that meet their obligations to the Fund in full.

c. Most Executive Directors also agreed that the Fund's policies regarding the provision of information on individual members in arrears, in the context of the Annual Report and the Fund's financial statements, should be somewhat extended. Some Directors considered that increased use of press releases would be appropriate in some cases, in particular following reviews of ineligible members and where it is concluded that the member is not cooperating actively. Others felt that such increased publicity would not be appropriate.

d. A number of Executive Directors considered that, in certain cases, it would be appropriate for the Fund to inform other multi-lateral institutions and bilateral official creditors of a member's arrears to the Fund. Some of these Directors also supported adding to such notifications a request that the institutions take the situation into account in their own relations with the member concerned.

e. Executive Directors' views on the efficacy of imposing penalty charges on overdue repurchases continue to differ. Among those Directors favoring such charges, some were attracted by the possibility

of holding their application in abeyance if a member was judged to be collaborating actively with the Fund to reduce its arrears.

f. Executive Directors are generally agreed that compulsory withdrawal should be examined only in individual cases and only in the event that all other avenues had been exhausted. Some Directors have asked that possible forms of suspension of membership be examined further, although it appears that the possibilities in this area are quite limited in the absence of an amendment to the Articles of Agreement.

##### 5. Conclusion

The Executive Board believes that a comprehensive initiative to secure the reduction and eventual elimination of arrears to the Fund is urgently needed. Failure or too much delay in the resolution of this problem could well mean that the cost of using the Fund's resources would gradually become more expensive, remuneration to creditors would be eroded, and the Fund's usable resources would be reduced, thereby impairing the possibility for the Fund to discharge its responsibilities. This report has outlined a strategy to avoid such an outcome by addressing the problem of arrears through strengthened preventive actions, intensified international collaboration, and extended remedial measures.

In supporting the broad thrust and outlines of the approach proposed, Executive Directors have stressed that many specific aspects will need to be considered further and that implementation will need to be flexible and determined on a case-by-case basis. They have stressed also that success will require exceptional efforts both by the countries in arrears and by the international community in general. The need to organize and obtain substantial financing in support of members' efforts to fundamentally reform their economies and regularize their relations with the Fund will in many cases necessarily involve institutions such as aid agencies that have their own lending priorities. The Executive Board believes that by supporting this approach these institutions will contribute to restoring conditions in which their own operations in these countries can be most effective. Similarly, the suggested application of preventive and remedial actions will require firmness and determination on the part of the Fund's membership. For both reasons, the Executive Board emphasizes the need for a commitment from all Fund members to the approach to be adopted so as to ensure that all parties involved act together in support of a common interest, and requests the Interim Committee's guidance and endorsement.

Table 1. Overdue Financial Obligations to the Fund, 1983-88 <sup>1/</sup>  
 (SDR millions; End of period)

	Total		Of Which Outstanding for:			
	Amount	No. of Members	6 Months or More		3 Years or More	
			Amount	No. of Members	Amount	No. of Members
1983	60.3	14	29.7	3	22.5	1
1984	178.2	24	54.4	4	23.3	1
1985	621.2	25	265.5	9	24.0	1
1986	1,035.6	21	611.2	7	29.8	2
1987	1,752.4	26	1,332.8	8	116.1	4
August 1988	2,394.9	18	1,894.6	11	268.6	5

<sup>1/</sup> Includes repurchases, charges, and assessments in the General Resources Account, net SDR charges, repayments and interest on Trust Fund and SAF loans, and special charges.

Table 2. Fund Credit Outstanding and Overdue Obligations  
of Members Subject to Outstanding Complaints

As of August 31, 1988

(SDR millions)

Member	Fund Credit Outstanding <sup>1/</sup>		
	Total	Of Which Overdue	Overdue Obligations <sup>2/</sup>
Guyana	81.7	63.0	83.3
Haiti	40.9	5.3	6.6
Honduras	44.5	15.7	18.9
Kampuchea, Dem.	18.7	18.7	32.6
Liberia	230.4	164.7	226.4
Panama	243.9	63.1	80.6
Peru	595.4	360.9	477.6
Sierra Leone	80.8	39.3	47.8
Somalia	123.5	31.1	43.0
Sudan	672.7	512.4	677.8
Viet Nam	89.0	68.0	95.5
Zaire	608.3	52.7	66.1
Zambia	<u>698.8</u>	<u>410.6</u>	<u>532.0</u>
Total	<u>3,528.6</u>	<u>1,805.5</u>	<u>2,388.2</u>

<sup>1/</sup> Includes outstanding repurchases and SAF and Trust Fund loans.

<sup>2/</sup> Includes overdue principal plus charges and interest.

Table 3. Burden Shared Deferred Charges and Additions to Precautionary Balances,  
and Effect on Rates of Charge and of Remuneration

(SDR millions)

Period	Charges Deferred 1/	Burden Shared Additions to Precautionary Balances 2/	Total Burden Shared Amounts	Adjustment 3/ (basis points)	Adjusted Rate (percent)		Remuneration Coefficient 4/
					Charge	Remuner-	
FY 1987							
First half	73.2	14.0	87.2	46	6.28	5.44	90.1
Third quarter	65.6	7.0	72.6	77	6.59	5.01	85.0
Fourth quarter	43.0	7.0	50.0	57	6.38	5.31	90.5
Total/average for year	181.8	28.0	209.8	57	6.38	5.34	88.9
FY 1988							
First quarter	39.8	7.6	47.4	52	5.90	5.13	91.0
Second quarter	39.2	7.6	46.8	52	5.90	5.57	91.5
Third quarter	47.1	7.6	54.7	64	6.02	5.06	88.8
Fourth quarter	39.3	37.7	77.0	79	6.17	4.69	85.0
Total/average for year	165.4	60.4	225.9	62	6.00	5.12	89.2
FY 1989							
First quarter	61.3	15.7	77.0	92	6.42	5.03	85.0

1/ Charges deferred since May 1, 1986, when the policy of burden sharing was adopted. Charges deferred in prior periods amount to SDR 127 million.

2/ In FY 1987 the target amount of income was increased from 5 percent of reserves to 7.5 percent and the additional amount, generated under burden sharing, was placed to reserves. Income in excess of the target amount for that year amounting to SDR 26.5 million was placed to the Special Contingent Account. Burden shared income equivalent to 5 percent of reserves was placed to the Special Contingent Account in FY 1988, and a similar amount is to be placed to this account in FY 1989.

3/ Adjustments shown are for the rate of charge. Adjustments of the rate of remuneration have in some periods differed slightly when the total of remunerated positions was greater than the total of balances subject to charges.

4/ The rate of remuneration as a percent of the SDR interest rate.

Fund Policies Relating to Overdue Obligations

In 1984, when it became apparent that the problem of late payments to the Fund was beginning to involve more than short-term, intermittent cases of arrears, the Executive Board considered general aspects of the problem on the basis of a staff paper on "Overdue Payments to the Fund - Experience and Procedures." That discussion confirmed a number of emerging practices with respect to members in arrears and established a general framework of policies and procedures for the Fund's efforts to address the problem. This framework, which has evolved as a result of subsequent general policy discussions by the Board and its consideration of individual cases, consists of a number of elements, as outlined in the following paragraphs.

1. Use of Fund resources by members in arrears

At its initial policy discussion in 1984, the Executive Board confirmed the longstanding practice that a member may not make further use of Fund resources if it has an overdue financial obligation to the Fund. Access to Fund resources is not proposed to the Executive Board if a member has overdue payments to the Fund, and staff papers recommending use of Fund resources are withdrawn from the Board agenda if overdue obligations emerge following their issue. Negotiations involving potential use of the Fund's resources are not to take place while overdue obligations remain outstanding. The Board has emphasized that this does not mean that dialogue with a member in arrears should not continue but rather that the discussion with a member in arrears to the Fund should concentrate on the steps, including the adjustment policies, the member may need to take in order to settle its financial obligations to the Fund promptly. Such discussions, which have been held with all members with overdue obligations (except Democratic Kampuchea), may encompass the formulation of policies that would catalyze external support to assist in clearance of the arrears to the Fund prior to any commitment of Fund financial resources. Comparable approaches have subsequently been adopted with respect to use of resources of the Structural Adjustment Facility and the Enhanced Structural Adjustment Facility.

2. Executive Board procedures for consideration of individual cases

As regards the arrears of individual members, procedures have been developed for regular reporting to the Executive Board, for Executive Board consideration and decisions with respect to complaints regarding members, and for subsequent reviews and decisions relating to the

position of the member in the event it does not become current. The procedures have themselves been reviewed regularly with a view to their being strengthened, as judged appropriate by the Board in light of experience. As with other aspects of the Fund's policies on arrears, Executive Directors have stressed that application of the procedures needs to respect the principle of uniform treatment of members, while also emphasizing that this does not call for identical treatment without regard to the circumstances of individual cases. In general, if a member has failed to become current following issuance of a complaint by the Managing Director, the Executive Board has initially applied the formal provisions available under the Articles and Rules relating to "limitation" of the member's use of the Fund's general resources and subsequently, if the arrears become protracted, has decided on a declaration of the member's ineligibility to use those resources.

### 3. Preventive measures

The Fund's policies on the use of its resources are intended to provide the necessary assurances and safeguards as regards the timely settlement of financial obligations to the Fund by the member using Fund resources. In this regard, the sound design and full implementation of Fund-supported adjustment programs are obviously paramount. With the emergence of serious arrears, the Executive Board has asked that, in papers proposing use of Fund resources, the staff not only report on the member's past performance in meeting obligations but also present an explicit assessment of the members's capacity to meet its financial obligations to the Fund in the context of the program being proposed. While the form and content of these assessments differ according to the particular circumstances of the case, the analysis normally centers on the member's overall adjustment effort and the prospects for medium-term balance of payments viability. If it appears that there will be a financing gap for any period during which a member would have repurchase obligations to the Fund, this fact is highlighted and an explanation provided of how the gap could be closed. The assessment would suggest whether the gap was expected to be closed by exceptional finance, in which case possible sources and amounts would be indicated, or alternatively, whether an intensification of the adjustment effort would be required. The Fund has also on recent occasion sought informal assurances from major creditors that sufficient resources for servicing a member's obligations to the Fund would continue to be made available over the repurchase period.

Apart from the fundamental question of the design and implementation of Fund-supported programs, a number of specific steps have been taken in an effort to avoid the emergence or reemergence of arrears. These include the regular provision of advance information on forthcoming obligations to all members, in addition to the specific operational communications dispatched in connection with an individual maturing obligation; close monitoring of members' forthcoming payments

and payments performance; efforts to avoid a bunching of obligations; and immediate and continuing follow-up in the event of a late payment. Depending on the specific difficulties that have been faced by a member, the staff gives particular attention to such measures as safeguards intended to prevent foreign exchange expenditures from exceeding those provided for in the foreign exchange budget, steps to ensure regular transfer of the local currency counterpart of debt service obligations (including debt to the Fund) to the Central Bank, and reporting on the execution of the foreign exchange budget in the regular reviews under a program. In a number of recent cases, the staff has encouraged and assisted the authorities to make arrangements for the advance acquisition of SDRs so as to build up their SDR holdings to meet forthcoming obligations to the Fund. This technique has proven useful in assisting several members that had experienced repeated, short-term difficulties in servicing their debt to the Fund to remain current in recent years.

As appropriate, the staff also makes an active effort to assist members to manage their external debt servicing obligations through the provision of technical assistance and through the ongoing work of the Fund's resident representatives in the countries where they are assigned.

4. Corrective actions

The bulk of the overdue obligations presently outstanding to the Fund is accounted for by a relatively small number of members. In most of these cases, balance of payments difficulties have been protracted, and in a number the arrears to the Fund emerged during the course of a Fund-supported program. In such instances, the emergence of the arrears to the Fund has generally been preceded or accompanied by serious departures from the program, which rendered the member unable to make further purchases, and in varying degrees by a reduction or withdrawal of financial support from other sources.

In addition to continuing efforts of a preventive nature and in light of the heavy concentration of arrears on a relatively few protracted cases, the Executive Board has increasingly emphasized the urgent need for corrective actions to achieve settlement in these difficult cases. In each instance, the staff and management have sought to assist the member in formulating needed corrective policies and, as appropriate, in obtaining financial support from other sources that could facilitate clearance of arrears to the Fund and open the way for a resumption of access to the Fund's resources.

5. Steps to safeguard the Fund's financial position

Despite the Fund's efforts to prevent the emergence of overdue obligations and to eliminate as rapidly as possible arrears that do occur, the amount and duration of arrears have increased and it has

become necessary to adopt a series of measures designed to protect the Fund's financial position. These include steps to strengthen directly the Fund's income--for example, the decision not to accrue charges from members with obligations overdue for more than six months; increases in the net income target; the compensation to the Fund for deferred income through adjustments to the rate of charge and the rate of remuneration; and the adoption of a system of special charges to recover the direct financial costs to the Fund of overdue obligations. The Fund has also acted to safeguard its financial position more generally through increases in precautionary balances as reflected in higher reserves and the establishment of the Special Contingent Account.