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Minutes of Executive Board Meeting 88/121

3:30 p.m., August 1, 1988

M. Camdessus, Chairman
R. D. Erb, Deputy Managing Director

Executive Directors	Alternate Executive Directors
	S. M. Hassan, Temporary
	C. Enoch
Dai Q.	
	D. C. Templeman, Temporary
	J. Prader
	R. Morales, Temporary
M. Finaish	M. B. Chatah, Temporary
	B. Goos
	Khong K. N., Temporary
A. Kafka	J. Hospedales
M. Massé	D. McCormack
Mawakani Samba	
	P. D. Péroz, Temporary
G. Ortiz	
J. Ovi	
H. Ploix	
G. A. Posthumus	G. P. J. Hogeweg
C. R. Rye	
	S. Rouai, Temporary
A. K. Sengupta	
K. Yamazaki	
S. Zecchini	

J. W. Lang, Jr., Acting Secretary
M. Primorac, Assistant

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2. Argentina - Report by Staff . . . . Page 21
3. Administrative Budget, FY 1989 - Increase in Personnel Ceiling . . . . Page 22

Also Present

European Department: M. A. Pinho. Exchange and Trade Relations Department: H. B. Junz, Deputy Director; P. D. Brenner, S. Kanesa-Thasan, J. P. Pujol, M. H. Rodlauer, B. C. Stuart. External Relations Department: H. P. Puentes. Fiscal Affairs Department: T. M. Ter-Minassian, Deputy Director. IMF Institute: O. B. Makalou. Legal Department: F. P. Gianviti, General Counsel; T. M. C. Asser, P. L. Francotte, A. O. Liuksila. Research Department: J. A. Frenkel, Economic Counsellor and Director; A. D. Crockett, Deputy Director; D. A. DeRosa, E. Hernández-Catá, R. Pownall, B. E. Rourke. Treasurer's Department: T. Leddy, Deputy Treasurer. Western Hemisphere Department: S. T. Beza, Director; D. N. Lachman. Personal Assistant to the Managing Director: H. G. O. Simpson. Advisors to Executive Directors: W. N. Engert, K.-H. Kleine, G. Pineau, A. Vasudevan, J. E. Zeas. Assistants to Executive Directors: N. Adachi, J. R. N. Almeida, R. Comotto, E. C. Demaestri, B. R. Fuleihan, S. Guribye, M. Hepp, C. Y. Legg, V. K. Malhotra, D. V. Nhien, C. Noriega, C. C. A. van den Berg, E. L. Walker, Yang J.

1. COMPENSATORY AND CONTINGENCY FINANCING FACILITY - PROPOSED DECISION

The Executive Directors resumed from the previous meeting (EBM/88/120, 8/1/88) their consideration of the proposed decision relating to the compensatory and contingency financing facility (EBS/88/146, 7/21/88). They also had before them the final version of the Chairman's summing up of the discussions on the compensatory and contingency financing facility concluded at EBM/88/105, 7/15/88 (EBM/88/105, Annex).

The General Counsel, in response to a question from an Executive Director on paragraph 17, said that the baseline would start when an arrangement became effective, and not when it was approved in principle.

Mr. Hogeweg asked what would happen if a contingency occurred between the time of approval in principle and the effective date of the arrangement.

The staff representative from the Legal Department remarked that the baseline need not coincide exactly with the period of the program. If a contingency occurred following approval in principle and before the effective date of the arrangement, the possibility of renegotiating the program should be retained.

Mr. Templeman said that a deadline should be set for the period of approval in principle, taking into account the risk that contingencies might develop in the intervening period.

Mr. Goos reiterated his request at the previous meeting that an addition be made to paragraph 17, reading: "...subject to the provisions of this decision that, should the member encounter payments difficulties produced by adverse external contingencies during the period of the arrangement...." It would seem asymmetrical to have such a reference in the introductory paragraphs of the other two sections and not in Section III.

Mr. Templeman remarked that he had sympathy for Mr. Goos's view.

Mr. Sengupta noted that while programs were subject to the balance of payments need criterion, a balance of payments problem could be corrected in the second year of a program, at which time an external contingency could develop. If the addition proposed by Mr. Goos were accepted, external contingencies that did not produce a balance of payments difficulty would not be eligible for contingency financing.

The Chairman noted that the Board was in favor of retaining the text as it stood, with the point of Mr. Goos being reflected in the minute.

Mr. Templeman recalled a suggestion in his chair's statement at EBM/88/120 that a reference be made in paragraph 18 to the general aim of seeking parallel contingency financing, with the clarification that there would not be a general requirement for such financing.

The General Counsel said that it had not been clear to the staff when it was drafting the decision whether the requirement of adequate financing would have to exist throughout the life of the arrangement or only from the time of activation on. Paragraph 24 of the proposed decision stated: "The Fund will decide to provide financing under this Section only if the program supported by the associated arrangement continues to be adequately financed...." That implied that sufficient parallel financing had to exist at the time of the decision approving the mechanism.

Mr. Templeman said that his suggestion had been that a general reference be made to parallel financing. The General Counsel had raised a second question as to the time period of the adequacy of financing. That adequacy had to exist at the beginning of the program. With respect to paragraph 24, he suggested that it read: "The Fund will decide to activate financing..." rather than "provide financing."

Paragraph 11 and paragraph 18 of the Chairman's summing up at EBM/88/105 both dealt with parallel financing, Mr. Templeman noted. He proposed reiteration of those two paragraphs by including in the decision a general paragraph--taken from paragraph 6 of the summing up--which could read: "Every effort would be made to obtain parallel contingent financing from other creditors and contingency mechanisms would not be activated unless the program continued to be adequately financed." Then from paragraph 11 of the summing up, the paragraph could continue with the sentence: "However, provided that adequate financing of the program is assured there would not be a formal requirement for advanced coverage of interest rates and other contingencies by mechanisms established with commercial banks."

The General Counsel pointed out that Mr. Templeman's second point was adequately dealt with in paragraph 24, which stated that there was, in principle, a requirement of financing "including, if necessary through the provision of financing from other sources."

Mr. Templeman said that parallel financing had been a matter of considerable debate in the Board. It was fundamental to the decision that while such financing should be sought, it should not be a precondition in every case. If paragraph 24 were depended on to cover the question of parallel financing, it should be worded in a way that made it clear it referred to the activation phase, when there would still be a need for adequate financing. In addition, he proposed that a paragraph be added before paragraph 24, stating that there was such an activation phase, when the Fund decided whether or not a contingency would be activated.

The General Counsel remarked that, as he saw it, although the reference to "every effort [being] made to obtain parallel financing" could be added to the decision, it was a statement of intention that had no legal effect and did not really belong in the decision.

Mr. Goos remarked that his proposed addition to paragraph 17 had been rejected despite the fact that it would do no harm; on that basis, the addition of Mr. Templeman should not be included either.

The Chairman noted that Mr. Goos's suggestion would have been repetitive, while the amendment of Mr. Templeman added a concept that had been clearly phrased in the summing up but did not appear clearly in the decision. While he felt that it would be sufficient to have the reference in the summing up, if it was the wish of the Executive Board, the addition could be made.

Mr. Sengupta said that he considered paragraph 24 as it stood to be sufficient.

The Chairman suggested that the staff prepare a wording that might receive unanimous support of the Board.

Mr. Templeman remarked that he had also made the point in his statement that, on the variables covered, the reference should not be to "one or more key external variables" but to "a few external variables." He did not anticipate any contingencies covering only one variable. In addition, the summing up stated that the variables must cover a significant portion of the current account; that should be added to paragraph 18.

Mr. Ortiz commented that the Mexican example had served as the basis for several paragraphs of the summing up, which suggested that the mechanism could, in certain circumstances, cover only one variable.

Mr. Templeman remarked that the Mexican case had never in fact resulted in the activation of contingency financing. If necessary, it could be stated that a few key external variables would be used as a general principle, and that "in all cases, the specific set of variables selected would need to cover a substantial proportion of the exogenous components of the country's current account." However, he considered it unlikely that only one variable would be covered.

The staff representative from the Legal Department said that the reference to a substantial proportion of the exogenous components of the member's current account could be added with no difficulty. However, the first point was more complex. The text of the summing up read: "As a general principle, contingency mechanisms would cover unanticipated changes in the exogenous components of a few key external variables." The phrase "as a general principle" was intended to cover the possibility of only one variable. For that reason, the draft decision read "one or more variables." He suggested that paragraph 18 begin: "As a general principle, such external contingency financing will only be provided in association with a Fund arrangement to a member facing unanticipated deviations from the baseline projections of a few key external variables that cover a substantial proportion of the exogenous components of the member's current account and that relate to the specified external contingencies during the period of the projections (hereinafter called the baseline period)...."

Mr. Templeman remarked that beginning the paragraph with the phrase "as a general principle" would give the impression that contingency financing for programs that were not associated with the Fund could be covered.

The staff representative from the Legal Department pointed out that similar language was used in paragraph 11 and in the first paragraph of the summing up.

Mr. Templeman said that it had not been agreed that financing of external contingencies would be permitted without such financing being attached to a Fund-supported program. The qualification ought to be inserted later on, with the sentence reading: "...to a member facing unanticipated deviations from the baseline of, as a general principle, a few key external variables."

Mr. Hogeweg pointed out that placing the qualification at that position implied that the variables would not always have to cover a substantial proportion of the current account; that was not advisable.

Mr. Sengupta remarked that if the reference to the variables covering a substantial proportion of a member's current account were added, the phrase "one or more key variables" could remain; Mr. Templeman's concerns would be accommodated.

The General Counsel noted that Mr. Sengupta's suggestion would allow for the elimination of the phrase "as a general principle," which was causing confusion as to which element of the sentence it qualified.

Mr. Templeman said that he preferred the language of the summing up.

The General Counsel remarked that it was difficult to use the language of the summing up since the decision brought together two different parts of the summing up into one sentence. By qualifying the first element, the second element would also be qualified, whereas with Mr. Sengupta's formulation that problem was solved. He suggested that the phrase read: "baseline projections of key external variables," allowing for the possibility of one or more variables.

The staff representative from the Legal Department said that the sentence would therefore read: "Such external contingency financing will only be provided in association with a Fund arrangement, to a member facing unanticipated deviations from the baseline projections of key external variables that cover a substantial proportion of the exogenous components of the member's current account and that relate to the specified external contingencies during the period of the projections (hereinafter called the "baseline period") if...."

In response to a request by Mr. Enoch for an elaboration of paragraph 19(a)(v), the staff representative from the Legal Department said that the paragraph could be clarified by adding, after the word "reduced," the phrase: "or other adjustments pursuant to paragraph 27 could be required." That phrase could also be added to paragraph 19(a)(iii), with the deletion of the words "or reductions in the amount of the associated arrangement."

Mr. Morales asked why the phrase "at the request of the member," which was the language of the summing up, had been omitted from paragraph 19(a)(iv).

The General Counsel said that the use of Fund resources could not take place without the request of a member.

The staff representative from the Legal Department said that the draft text followed the spirit of the summing up by referring to the need to ensure the continued viability of the member's program. Even if the member did not make a request to increase the proportion of deviation to be financed, if it was necessary to ensure the viability of the program, the Fund would probably make such a proposal.

Mr. Templeman suggested that paragraph 19(a)(iii), which made the first mention of the minimum threshold, have added after the word "threshold," the qualification: "which shall generally be 10 percent of the member's quota."

On paragraph 19(c), Mr. Templeman suggested that the length of the baseline period be specified as being "generally 12-18 months."

The Chairman noted that the Board accepted the proposals of Mr. Templeman.

Mr. Enoch suggested that the references in paragraph 20 to interest costs be qualified to read "net interest costs."

Mr. Templeman asked for an explanation of paragraphs 20(c)-(e) and paragraph 21.

Mr. Goos said that his authorities had also had difficulties understanding those paragraphs and suggested that a numerical example would be helpful.

The staff representative from the Research Department said that the language of the paragraphs in question attempted to avoid undesirable outcomes resulting from the 35 percent sublimit on interest rate deviations combined with the symmetric provisions of the mechanism, as well as from the 35 percent sublimit combined with the 4 percent deductible. A country could be faced with the activation of symmetric provisions even though in the absence of those limitations it would have faced a very large negative deviation. That was avoided by paragraph 20(c)(ii), which also tried to solve the problem that would arise if a country had a very large interest rate deviation by dealing with the deductible before application of the 35 percent limit. For example, if a country had an interest rate deviation of 94 percent, in the absence of the interest rate limitation it would have received 90 percent financing with 4 percent deductible. With the limit on interest rate contingencies, however, it could only receive 35 percent financing. It seemed undesirable to further reduce access to 31 percent by applying the deductible after imposition of the limit. Accordingly, paragraph 20(c)(ii) provided for the deductible, to be applied before the 35 percent limit was implemented.

Paragraph 20(e) attempted to avoid a situation in which a country might not qualify for contingency financing because its net sum of deviations was below the 10 percent threshold after application of the 35 percent limit, the staff representative from the Research Department said, even though in the absence of that sublimit the net sum of deviations would have been above the threshold.

Mr. Ortiz said that while his authorities had had difficulties with the 35 percent limit, he could reluctantly go along with paragraph 21(a) and would attempt to propose a change at the time of the facility's review.

Mr. Goos noted that the reference in paragraph 22 should be to paragraph 19(a)(i), and not (ii).

Paragraph 23 placed a restriction on contingency financing that would cause the Fund's holdings of the member's currency resulting from purchases under that section to exceed 40 percent of the member's quota, Mr. Goos observed. As he saw it, a similar limit should be added to Section II and Section IV.

The staff representative from the Legal Department said that the summing up had referred to such a limit only in the context of contingency financing, which was why it had been mentioned only in Section III.

The Chairman noted that Mr. Templeman had made the suggestion in his statement to add a paragraph after the present paragraph 23 that would parallel paragraph 2 of the summing up on the modalities for the activation of contingency financing.

The General Counsel observed that paragraph 24 currently dealt not with activation, but with the decision to adopt an external contingency mechanism. The amendment to delete the words "decide to" would change the text to read: "The Fund will provide financing," with the result that paragraph 24 would apply only at the time of activation. Mr. Templeman had proposed a reference to a decision by the Fund at the time of activation, and the term "provide financing" already referred to that stage.

Mr. Templeman said that paragraph 24 only talked about the adequacy of financing, whereas he considered that a Board decision was necessary as to whether or not there was a justification to provide contingency financing at all. The exception would be the case of classical export shortfalls. Accordingly, he suggested that a new paragraph state that generally a review would be held at which the Fund would decide whether or not to activate the external contingency mechanism.

The staff representative from the Legal Department acknowledged that no attempt had been made to parallel paragraph 2 of the summing up in the decision because that text did not lend itself to inclusion in the decision. In order for modalities to become operative, criteria were necessary to decide which procedures applied in each particular case. Nevertheless, the decision as drafted provided all the necessary flexibility for the Board to apply the rules and guidelines of the summing up.

The language of paragraph 17 and paragraph 18 incorporated the three-stage approach explained by the General Counsel at the previous meeting, the staff representative from the Legal Department said. Approval of the external contingency mechanism would be given at the time of the arrangement. Later on, when the contingency had taken place, the external contingency mechanism would be activated. The Board would then decide what procedures would be followed for providing financing.

Mr. Templeman remarked that it was not clear from paragraph 17 that two stages were implied. It would be preferable to make it clear that a second Board decision was necessary in most cases, by including a reference, in paragraph 24, back to paragraph 19.

Mr. Ortiz said that if Mr. Templeman's suggestion were acted upon, a reference would have to be made to the second paragraph of the summing up on exceptional cases. The language could become very complicated.

Mr. Goos said that it would be clearer that a decision by the Board was necessary if the phrase: "the Fund is satisfied that" was inserted in paragraph 18, after the word "if."

Mr. Templeman remarked that his suggestion could be accommodated by adding to the beginning of paragraph 24 a sentence reading: "Other than in exceptional cases, contingency mechanisms generally would be activated on the basis of a review by the Executive Board."

The staff representative from the Legal Department said that the language proposed by Mr. Templeman raised a number of questions. For example, a review by the Executive Board would have to be defined. Mr. Goos's suggestion to add a phrase to the end of the preamble of paragraph 18 would be logical, since that paragraph dealt with activation and the conditions of activation. Perhaps the suggestions of Mr. Goos and Mr. Templeman could be combined.

Mr. Enoch remarked that paragraph 24 appeared to be a general paragraph that applied to upper tranche compensatory financing as well as contingency financing, and therefore would be more appropriate in Section I.

The General Counsel said that it had not been clear to the staff whether the Board intended that the provision of paragraph 24 should also apply to compensatory financing. If so, it would indeed have to be moved to Section I.

The Chairman said that, as he recalled, the Board had intended to establish that principle only for contingency financing.

The General Counsel noted that paragraph 24 stated: "The Fund will decide to provide...." It was not clear to him whether the Board intended that the finding of adequate financing from other sources be made at the time of the initial decision or at the time of the activation of the contingency financing mechanism. If it referred to activation, a more appropriate wording would be: "The Fund will provide financing...." That could be combined with the requirement that parallel financing be actively pursued.

Mr. Templeman said that the distinction between paragraphs 24 and paragraphs 18 and 19 was that the former was ex ante while the latter were ex post. Paragraph 24 had to do with activation. It went without saying that a country had to have sufficient financing when the external contingency mechanism was first established. The term "activate" would be preferable since it would make it clear that one was dealing in an ex post fashion. The ex ante condition was as important, but needed less clarification because it was a general requirement.

Mr. Hogeweg remarked that paragraph 26, which dealt with symmetry, should specify which limits applied when it referred to repurchases. For example, would the 35 percent sublimit on interest rate contingency financing be applied to repurchases that were made as a result of overcompensation?

The staff representative from the Legal Department acknowledged the point of Mr. Hogeweg, while observing that thorough coverage of the interest rate case would require a long explanation. The term "in an amount equivalent to the overcompensation" was vague but captured the principle of adjustment. If there was an overcompensation, the mirror image of the formula used to calculate contingency financing would be used.

Mr. Ortiz said that he agreed with Mr. Templeman's statement that paragraph 27 did not accurately reflect the priorities for symmetrical actions--referred to in paragraph 8 of the Chairman's summing up--in the case of favorable developments when no previous contingency drawing had been made. That paragraph read: "When a favorable deviation relative to the baseline occurs, a substantial part of the favorable deviation would be used to build up reserves in cases where reserves were low."

The staff representative from the Legal Department said that the staff had considered that the term "as determined by the Fund" gave sufficient flexibility to the wording of paragraph 27(a). However, a sentence could be added to indicate the preference for buildup of reserves.

Mr. Goos asked whether the provision in paragraph 27 as formulated was actually an operational one. While the summing up stated that the favorable deviation "would be used to build up reserves," the decision merely stated that "the limits on, or objectives for, the member's reserves under the associated Fund arrangement shall be increased."

The General Counsel said that the reserve target could be formulated as an understanding, in which case the breach of that understanding would have no consequence on further use of the Fund's resources, or it could be formulated as a performance criterion, in which case noncompliance would trigger a suspension of the use of Fund resources unless a waiver were granted by the Fund.

Mr. Hospedales recalled that there had been four options for symmetrical action, the last of which was the possibility of expansion of investment. Was that captured in the language of paragraph 27(a)?

The staff representative from the Exchange and Trade Relations Department said that the point of paragraph 27(a) was that the favorable net sum of deviations would not have to be set aside in its entirety so that, in fact, part of the favorable shock could be used for such purposes as expanding investment.

Mr. Templeman said that he had not understood that to be part of the agreement as reflected in the summing up. The possibility to use favorable deviations for investment expansion seemed somewhat like a growth facility, a concept that had been rejected. While the threshold meant that not all the favorable deviation would go into reserves or be used for early repurchase, he did not recall the Board agreeing to an investment growth option as part of the symmetry provision.

The staff representative from the Exchange and Trade Relations Department observed that the first sentence of the section on symmetry in the summing up stated that "a substantial part of the favorable deviation would be used to build up reserves."

Mr. Hospedales suggested that his point be emphasized by adding to paragraph 27(a), after the words "or both," the following: "by part of the favorable applicable net sum of deviation, as determined by the Fund, so that the sum of the parts shall not exceed an amount that would have been financed...."

The staff representative from the Exchange and Trade Relations Department remarked that paragraph 27(a) implied that just as the Fund would not provide 100 percent financing for an unfavorable deviation, so it did not expect a member to set aside 100 percent of a favorable deviation.

Mr. Templeman said that the notion of a substantial proportion of the favorable deviation being used for repurchases or to increase reserves should be included in the decision.

The staff representative from the Exchange and Trade Relations Department said that since the Fund would finance a substantial part of the unfavorable deviation, Mr. Templeman's concern was dealt with by the wording: "generally shall be equivalent to the amount that would have been financed under this Section if the applicable net sum of deviations would have been unfavorable."

Mr. Templeman observed that the Fund ordinarily would finance 70 percent of a contingency, which was not a substantial proportion.

The Chairman noted that paragraph 27 could state that "a substantial part of any favorable deviation would be set aside."

Mr. Hospedales said that his comments on paragraph 27(a) also applied to paragraph 27(b).

Mr. Templeman noted that he had suggested in his statement that the words "provided that" in the last clause of paragraph 27(b) be replaced with the word "or." That would put the options of increasing reserves, reducing the amount of the associated Fund arrangement, or making an early repurchase on equal levels.

The staff representative from the Legal Department said that the words "provided that" had in fact been used to distinguish between two levels. The reduction in the use of the Fund resources and an increase in reserves were decided by the Fund, while a decision to make an early repurchase was made by the member.

On Mr. Templeman's suggestion regarding paragraph 28, the staff representative from the Legal Department said that the staff would eliminate the commas after the words "financial assistance" and "decision."

The Chairman noted that there were no comments on paragraphs 29, 30, and 31.

The staff representative from the Legal Department remarked that changes corresponding to those made to Section II would be made in Section IV.

Mr. Hogeweg asked whether there was any conflict between paragraph 14 and paragraph 32. Paragraph 14 stated that no more than six months of the data on merchandise exports could be estimated, while in paragraph 32 on the cereal decision, it was stated that the calculation of the shortfall in exports should be for the same 12-month period as for the data on cereals. However, the cereal data were estimated on a 12-month period ending not later than 12 months after the latest month for which the Fund had sufficient data on the member's cereal import costs.

The staff representative from the Research Department said that there was no inconsistency between paragraph 14 and paragraph 32 with respect to the period for the estimation of exports and of cereal import costs. The text of the two paragraphs reflected differing Fund policy toward, on the one hand, shortfalls in export receipts, and on the other, increases in import prices. Both were dealt with under the umbrella of the early purchase provision.

In the case of exports, the staff representative continued, the early purchase provision had been in effect since 1975, when the Executive Board took a decision that would permit members to base an export shortfall on up to six months of estimated export data rather than waiting for the actual export data to become available. That had been done to speed up members' access to compensatory financing.

When the cereal decision was introduced in 1981, the Executive Board also examined the case for an early purchase provision in that case, the staff representative explained. However, the Board felt that members facing increases in cereal import costs, particularly those associated with crop failures, were likely to require even more timely provision of additional financing than was the case for exports. Accordingly, the estimation period for such cases was increased to one year. The intent of paragraph 32 was that the member could use up to 12 months of estimated data for increases in cereal import costs, while paragraph 14 stated that only up to 6 months of estimated data could be used for export shortfalls.

In the case of workers' remittances and tourist receipts, the staff representative from the Research Department remarked, similar provisions had led to the decision that an estimation of up to 12 months would also be allowed, because many countries had particular data difficulties. If the 12-month provision were not in effect, that would slow down the receipt of compensation for shortfalls in those categories.

Mr. Hogeweg noted that the last sentence of paragraph 32 stated that: "the calculation of a member's shortfall or excess in exports and its excess or shortfall in the cost of its cereal imports shall be made for the same 12-month period." Since only six months could be estimated with respect to the export shortfall, would that be a bottleneck for cereal import financing?

The staff representative from the Research Department stated that the 12-month period related to the period of shortfall or excess. A shortfall ending December 1988, for example, could include 12 months of estimated cereal import costs and up to 6 months of estimated export receipts. If a country had actual data on exports through June 1988, it could base its shortfall calculation on exports estimated from July to December. If the country did not have import data for cereal import costs beyond the end of 1987, it could estimate up to 12 months of those data. Therefore, the export constraint of six months would not limit the purchase in that case. However, if export data were not available beyond, say, March 1988, exports could not be estimated beyond September, which would then have to be the end of the shortfall year. In such a case, it might be that the combined shortfall and cereal excess for that shortfall year would be smaller than that which could materialize for a shortfall year ending later than September. In that sense, the size of the shortfall/excess would be constrained as Mr. Hogeweg had thought.

Mr. Goos suggested that the phrase "for which the Fund has sufficient data" be clarified to read "sufficient statistical data." That made a clearer distinction between estimated and actual data.

The staff representative from the Research Department said that such clarification was possible.

The staff representative from the Legal Department observed that that change would also have to be made in other places in the text.

The Chairman noted that there were no comments on paragraphs 33, 34, 35, and 36.

The staff representative from the Legal Department, in response to a question from an Executive Director, indicated that paragraph 37 described the combined limit for the export shortfall and cereal import components. A similar paragraph appeared in the original cereal decision. It could not be incorporated in paragraph 8 of the compensatory and contingency financing facility decision because it was possible, under the cereal decision, for a purchase to consist of two components--export shortfalls and cereal import costs. Paragraph 37(a) covered the classical case in which a combined limit of 105 percent of the member's quota applied. Paragraph 37(b) referred to ordinary cases in which the access limits outlined in paragraph 8 applied.

Mr. Templeman suggested that the staff provide an explanatory paper on the implications of paragraph 37.

The Chairman observed that there were no comments on paragraph 38, but recalled that Mr. Templeman had suggested a clarification on paragraph 39(b) in his statement.

The staff representative from the Legal Department said that the provision in paragraph 39(b) appeared in the old cereal decision. It need not be included in the other sections for the following reason. Generally, the expression of access limits in terms of the Fund's holdings of a member's currency made it unnecessary to specify that a member's access would be restored if there was a repurchase or a reduction in the

Fund's holdings owing to other reasons. For example, if the Fund had held 40 percent of quota in the member's currency and a repurchase of 10 percent brought the holdings to 30 percent, the member would be able to purchase up to 40 percent once again. However, in the case of the cereal decision, as dealt with in Section IV, one purchase could cover more than one component. In that case, it might not be clear as to which component of a country's access to Fund resources would be restored when the Fund's holdings of its currency were reduced. Paragraph 39(b) attempted to rectify that.

The Chairman noted that there were no comments on paragraph 40.

The staff representative from the Legal Department said that paragraph 41 made reference to a review not later than May 13, 1989 because the cereal decision remained in effect until that date. He understood that Mr. Templeman had made a proposal to extend the review of the cereal decision to have it coincide with the review date for the entire facility, which would result in the date in paragraph 41 being changed.

Mr. Templeman said that the review of the cereal facility could not easily take place before a review of the entire facility since the two were very integrated. He felt that the Fund's emergency assistance and contingency financing already covered any increase in cereal import costs, and considered the cereal decision to be no longer necessary. However, that decision should be made in the context of the review of the entire compensatory and contingency financing facility.

The General Counsel indicated that if the decision were adopted at the current meeting, the current date would be inserted in the blank in paragraph 42. Alternatively, the Board could take the decision on a lapse of time basis, in which case the later date would be inserted.

The Chairman suggested that the decision be taken on a lapse of time basis with Friday, August 15, being the deadline.

The General Counsel said that the staff had prepared a new paragraph to be inserted between paragraph 44 and paragraph 45 to make it possible for members having arrangements enforced at the time of the decision's approval to benefit from the new external contingency mechanism. The paragraph read: "Notwithstanding the provisions of paragraph 17, the Fund will be prepared to decide, when completing a review of a Fund arrangement approved before [the date of this decision], that external contingency financing will be provided under this decision for the remaining period of the arrangement, if this period is at least one year. The provisions of Section III shall apply _mutatis_ _mutandis_ to this decision."

Mr. Chatah suggested that the cutoff date for such consideration be postponed to three months after the date of the decision to take into account cases in which negotiations were complete but an arrangement had not yet been approved.

Mr. Templeman said that the qualification that the remaining period of the arrangement be at least one year should actually refer to a baseline period of 12 months. The qualification as it stood implied that a program could be interrupted in the middle of a baseline period, requiring a new policy package and balance of payments estimate.

Mr. Ortiz said that he agreed with Mr. Templeman, in that an arrangement could have only nine months remaining but if the projection could go forward for one year, the country should be able to benefit from contingency financing. Accordingly, the one-year period constraint should refer to the baseline period and not to the length of the arrangement.

The staff representative from the Legal Department pointed out that it was possible to have a multiyear arrangement that would have several baseline periods remaining. The staff had felt that arrangements eligible for transitional treatment should have at least one year remaining from the date on which contingency financing was agreed to. Theoretically, the baseline period could stretch further into the future than the arrangement, but that was very unlikely.

Mr. Templeman said that if a country opted at the middle of an 18-month program to apply for contingency financing, it would have to recalculate the baseline.

The staff representative from the Legal Department remarked that the phrase in the new paragraph "if this period is at least one year" could be changed to: "if such period is at least one year."

Mr. Templeman remarked that paragraph 44 seemed to provide a transitional arrangement for compensatory and cereal financing as well as contingency financing, which had not been the intent of his chair.

The staff representative from the Legal Department said that the purpose of paragraph 44 was to permit a member that had outstanding export shortfall purchases in excess of 65 percent of quota to make up to 40 percent contingency purchases. However, in the classical case, in which an export shortfall was the only reason for a balance of payments difficulty, purchases up to 83 percent would be permitted. As a result, it was necessary to make an exemption for the transitional period to the combined limits of 105 and 122 percent set out in paragraph 8. For example, if a member had already made export shortfall purchases worth 70 percent of quota under the old compensatory financing decision, it would be prevented by the 65 percent access limit from making another export shortfall purchase outside the classical situation. However, if the purchase being applied for was based on the classical case, the member would be allowed access of up to 83 percent.

Mr. Templeman said that the 83 percent classical case had been preserved in the access limits set out earlier in the decision. The two concepts had to be separated, since paragraph 44 did not clearly set out the proposal of his chair.

The staff representative from the Legal Department presented another example. If a member made 83 percent of quota purchases for export shortfalls and was granted 40 percent of quota contingency purchases, its total would be 123 percent, which was over the 122 percent limit set out in paragraph 8. Accordingly, paragraph 44 had to provide for an exemption.

Mr. Templeman repeated that the two concepts should be spelled out in different paragraphs.

The staff representative from the Legal Department said that it was difficult to improve on the text of the provision by spreading it over two paragraphs; in any event, division of the two concepts into two provisions would result in doubling of much of the complex language.

The Chairman suggested that paragraph 44 also be explained in the technical staff paper.

Mr. Templeman said that he saw no reference in paragraph 44 to the type of balance of payments problems that were being faced. He wanted it to be made clear that the only time the 105 percent limit could be exceeded was in the classical case.

Mr. Goos said that the reference to "in excess of...122 percent limit" was only made because of the 1 percent excess that a country might attain if it qualified for 83 percent compensatory financing purchases. Was it really worthwhile, for 1 percentage point, to stipulate that that limit could be exceeded? Was it not simply easier to allow countries in the classical situation to have only 39 percent transitional contingent financing.

The Chairman proposed retaining the paragraph as it stood.

Mr. Goos remarked that paragraph 44 seemed to have an additional ambiguity in the last sentence, which read: "The transitional access limit shall apply until the Fund's holdings of the member's currency resulting from purchases on account of export shortfalls are reduced to 65 percent of the member's quota or the Fund's holdings of the member's currency resulting from both purchases on account of export shortfalls and purchases on account of external contingencies are reduced to 105 percent of the member's quota, whichever shall come first." Could there not be a situation where the member had reached the transitional access limits and made repurchases that failed to reduce it below either of those limits, in which case it could have access to the higher transitional limit? That possibility should be excluded, since it allowed a member the opportunity to operate between the normal limits and the transitional limits indefinitely.

The staff representative from the Legal Department said that while such a case was indeed possible, it was not left only to the discretion of the member to make such purchases; the proper circumstances were necessary to justify them. However, if the Directors so decided, the staff would change the text of paragraph 44 to indicate that once a net reduction in the level of purchases took place, no further purchases would be allowed until the total holdings of the Fund were brought below the limits. That could have serious consequences since if a country had already made, say, a purchase of only 1 percent of quota, at the time of its following repurchase, it would lose its entitlement to the transitional provision. In fact, however, further purchases under the compensatory financing element were predicated on the classical case applying, in which there were no other balance of payments difficulties except the export shortfall; therefore, there was little likelihood of compensatory financing purchases in excess of 65 percent up to the 83 percent occurring in conjunction with contingent purchases. A possibility would be to provide a cutoff date of, say, six months after which the transitional provisions would not apply.

Mr. Chatah suggested that the reference to 65 percent of the member's quota could be specified as being purchases that occurred before the decision was in effect; in other words, once the original 65 percent of quota declined, the transitional arrangement would no longer apply even if a member's total holdings were above 65 percent.

The General Counsel said that, in that case, the second sentence of paragraph 44 would read: "The transitional access limit shall be equal to the sum of such holdings of the Fund (expressed in terms of the member's quota) on the date of this decision and 40 percent of the member's quota." That would place a freeze on the Fund's holdings of the member's currency while the 40 percent contingency financing remained available.

Mr. Rouai pointed out that since paragraph 42 extended by three months the current compensatory financing facility decision, the General Counsel's proposal should refer to November 1, and not to the date of the decision.

The staff representative from the Legal Department said that the summing up seemed to define the cutoff date as the date of the decision itself.

Mr. Templeman said that the intention of the cutoff date was to freeze the situation for the transitional period. He saw no reason to extend the cutoff date by three months.

The Chairman said that while the new paragraph to be placed between paragraph 43 and paragraph 44 allowed countries that had entered into a compensatory financing arrangement by November 1 to qualify under the compensatory financing facility decision, the cutoff date in paragraph 44 was not necessarily related.

Mr. Rouai observed that the two purchases were governed by the same compensatory financing facility decision.

The staff representative from the Legal Department said that there was a risk of double counting if the period during which the original decision, with higher access limits, was extended together with an extension of the cutoff date for transitional arrangements.

The General Counsel said that paragraph 44 as it stood reflected a point that had been discussed and agreed upon by the Executive Board and was part of the transitional provisions under the decision. The Board could give further consideration to that matter and come back to it on the basis of an actual case, at which time it could decide whether or not it was necessary to amend the transitional provisions.

The Chairman noted that there were no comments on paragraph 45 and paragraph 46.

Mr. Rouai asked whether Decision No. 5703-(78/39), which dealt with repurchase obligations, would have to be amended to include the compensatory and contingency financing facility.

The General Counsel said that the general principle under the Articles of Agreement was that repurchase took place within three to five years of the date of the purchase. There was no need to have a specific provision on repurchases unless the Board planned to depart from that rule. While the decision on repurchases made reference to specific facilities, that list was only illustrative. Moreover, he agreed with Mr. Rouai that an amendment of Decision No. 5703-(78/39) would help in avoiding further misunderstandings.

The Chairman noted that a decision had to be made with respect to the date for the review in paragraph 46. It had been agreed to have the review in one year's time, which would result in a review date of August 1, 1989. However, since July was a heavily burdened month, he suggested a review deadline of November 1, which would allow the review to take place during October.

Mr. Yamazaki said that he could go along with the Chairman's proposal.

Mr. Hogeweg said that he would prefer that the review be completed before the Annual Meetings.

Mr. Templeman said that he preferred the solution of the Chairman, which provided sufficient time for the review to be conducted.

Mr. Goos reiterated his concern about the form of the decision. It was awkward that, after having agreed to a difficult case, paragraph 46 allowed for all aspects of the new facility to be changed by a simple majority vote. When the review took place, it would only be fair if the Board was aware of the substantial problems many Directors had had in supporting many features of the decision. Perhaps it could be agreed that certain elements would not be changed without the consent of those

Directors who had had particular difficulties with specific aspects. With respect to the date of the review, he saw the attractiveness of it taking place before the Annual Meetings, but on the other hand considered that sufficient time should remain for the review. He would have to reserve his position on that.

Mr. Enoch proposed that the review deadline be set at December 1, since staff papers had to be circulated four weeks in advance and the staff, with a November 1 deadline, would have to write the related papers at the time of the Annual Meetings.

Mrs. Ploix said that since October was the month with least Board work, she considered November 1 to be a preferable deadline.

The Chairman remarked that a December 1 deadline did not preclude completion of the review earlier in November. Accordingly, the date of December 1 could be inserted into paragraph 46.

Mr. Goos made the following statement:

> Despite their major reservations against the new facility my authorities support the proposed decision in a spirit of compromise.
>
> In supporting the proposed decision my authorities expect that, at the occasion of next year's general review, the package--which undoubtedly represents a very delicate balance of conflicting interests--will not be reopened and altered in some crucial aspects unless such changes are approved by the same majority of the votes (85 percent) that is required to adopt the proposed decision.
>
> One specific minimum safeguard is of utmost importance to my authorities, namely, that contingency financing of interest costs remains subject to a cumulative sublimit of 35 percent of quota. If at the occasion of the general review of the compensatory and contingency financing facility that important minimum safeguard were to be amended by a simple majority of 50 percent of the votes, we would very likely not be in a position to go along with such a move, because the establishment of a cumulative sublimit of 35 percent of quota played a crucial role in our willingness to support the overall compromise.

Mr. Templeman requested that the staff's explanatory paper be provided to Directors in sufficient time before the lapse of time deadline.

After a brief discussion, Directors agreed on August 22 as the lapse of time deadline. 1/

Mr. Sengupta suggested that the summing up form part of the decision, as was the case for the enhanced structural adjustment facility decisions, to which the summing up had been attached as an official explanation.

The Chairman said that the summing up reflected the political agreement of the Board and while it was an important explanatory element of the decision, it did not have the same legal value.

The General Counsel agreed that the summings up were an essential instrument of interpretation and implementation of Executive Board decisions. However, they could not be appendices or attachments to a Board decision; there was never a reference in a decision to a summing up as an appendix. The summing up reflected the Managing Director's understanding of the consensus reached in the Executive Board.

The Executive Directors then concluded their discussion of the proposed decision on the compensatory and contingency financing facility.

2. ARGENTINA - REPORT BY STAFF

The Director of the Western Hemisphere Department reported on consultations with Argentina.

1/ See EBS/88/146, Supplement 1. Decision No. 8955-(88/126), adopted August 23, 1988.

DECISION TAKEN SINCE PREVIOUS BOARD MEETING

The following decision was adopted by the Executive Board without meeting in the period between EBM/88/120 (8/1/88) and EBM/88/121 (8/1/88).

3. ADMINISTRATIVE BUDGET, FY 1989 - INCREASE IN PERSONNEL CEILING

The Executive Board approves the proposal to raise the personnel ceiling, as set forth in EBAP/88/187 (7/27/88).

Adopted August 1, 1988

APPROVED: April 7, 1989

JOSEPH W. LANG, JR.
Acting Secretary