

0404

INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 87/171

10:00 a.m., December 15, 1987

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

Executive Directors

A. Abdallah  
Dai Q.

J. de Groote  
A. Donoso  
M. Finaish  
G. Grosche

T. P. Lankester  
M. Massé

Y. A. Nimatallah  
G. Ortiz  
J. Ovi

G. A. Posthumus  
C. R. Rye

A. K. Sengupta  
K. Yamazaki  
S. Zecchini

Alternate Executive Directors

M. K. Bush  
A. Rieffel, Temporary  
J. Prader

J. Reddy  
J. E. Zeas, Temporary  
C. Enoch

C. V. Santos  
I. A. Al-Assaf

D. Marcel

C.-Y. Lim  
O. Kabbaj

S. Yoshikuni

L. Van Houtven, Secretary and Counsellor  
S. L. Yeager, Assistant

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Also Present

IBRD: E. Grilli, Office of Senior Vice President - Operations. African Department: A. D. Ouattara, Counsellor and Director; E. A. Calamitsis, Deputy Director; J. Artus, S. N'guiamba. Asian Department: B. Banerjee. European Department: J. J. M. Kremers. Exchange and Trade Relations Department: L. A. Whittome, Counsellor and Director; J. T. Boorman, Deputy Director; S. J. Anjaria, M. W. Bell, S. B. Brown, B. Christensen, M. Nowak, R. L. Sheehy. External Relations Department: H. O. Hartmann, P. C. Hole. Fiscal Affairs Department: E.-A. Conrad. Legal Department: F. P. Gianviti, General Counsel; W. E. Holder, Deputy General Counsel; A. O. Liuksila, R. H. Munzberg. Middle Eastern Department: A. Tahari, M. Yaqub. Secretary's Department: C. Brachet, Deputy Secretary. Treasurer's Department: F. G. Laske, Treasurer; D. Williams, Deputy Treasurer; J. E. Blalock, K. Boese, J. C. Corr, G. M. Fitzpatrick, D. Gupta, D. V. Pritchett, G. Wittich. Western Hemisphere Department: S. T. Beza, Director. Personal Assistant to the Managing Director: H. G. O. Simpson. Advisors to Executive Directors: M. B. Chatah, A. Ouanes, P. D. Pérez, D. C. Templeman, N. Toe', A. Vasudevan. Assistant to Executive Directors: N. Adachi, R. Comotto, F. Di Mauro, S. K. Fayyad, V. J. Fernández, S. Guribye, M. A. Hammoudi, M. Hepp, G. K. Hodges, L. Hubloue, V. K. Malhotra, C. Noriega, W. K. Parmena, S. Rebecchini, C. C. A. van den Berg, E. L. Walker, R. Wenzel, I. Zaidi.

1. STRUCTURAL ADJUSTMENT FACILITY - ENHANCEMENT OF RESOURCES -  
PROPOSED FINANCIAL AND OPERATIONAL ARRANGEMENTS

The Executive Directors continued from a previous meeting (EBM/87/168, 12/11/87) their consideration of staff papers on operational arrangements governing the enhancement of the structural adjustment facility (EBS/87/245, 11/25/87; and Cor. 1, 12/3/87) and on legal documentation to give effect to the proposed enhancement (EBS/87/253, 12/2/87; Sup. 1, 12/9/87; and Rev. 1, 12/14/87). They also had before them staff papers discussed previously in Executive Board Informal Sessions 87/5 and 87/6 (11/13/87) and Informal Sessions 87/7 and 87/8 (11/20/87), on proposed financial arrangements (EBS/87/228, 10/29/87; and Sup. 1, 11/11/87), and on considerations relating to access and monitoring procedures under the enhanced facility (EBS/87/230, 11/9/87; and Cor. 1, 11/16/87).

The Deputy Director of the Exchange and Trade Relations Department made the following statement:

The staff considers that in view of the complexities of the modalities of the Subsidy Account, it might be useful to set out how the operations would actually take place.

In accordance with the Instrument, interest payments to creditors on outstanding borrowings are normally to be paid promptly after June 30 and December 31. These payments would be made from the interest paid by borrowers to the Trust's Loan Account and from resources held in the Subsidy Account. In the normal course, and in the absence of arrears, the payments in and out of the Loan Account would be expected to be offsetting and, together with the amounts disbursed from the Subsidy Account, to be sufficient to cover all interest payments due to creditors. In case of delays in interest payments to the Loan Account by borrowers, the Trust would meet obligations to creditors from the Reserve account which would be replenished as arrears are settled.

The Trustee would need to determine as early as possible in each half-year period the interest rate to be charged. The objective would be to reduce to the extent possible the rate of interest on Trust loans to 0.5 percent. If it appeared that the Subsidy Account did not contain sufficient resources to bring the rate down to 0.5 percent over the prospective life of the Trust, the Trustee shall seek additional resources. Failing that, the rate of interest would have to be raised to a rate that could be applied throughout the remaining life of the Trust on the basis of the projected availability of resources to the Subsidy Account.

It is not intended to increase the rate of interest retroactively at the end of each half-year period in part because this could require very short notice to borrowers. It is envisaged

that the adjustments would be made prospectively for succeeding interest periods and would apply to all outstanding Trust loans, though it is not precluded that a retroactive reduction in the rate of interest could be effected if the Subsidy Account contained sufficient resources.

There is a risk, especially in the first interest period if the rate is set at 0.5 percent and there is a delay in receipt of committed resources for the Subsidy Account, that the resources in the Subsidy Account may be inadequate to satisfy in full the interest payments to be made to creditors at the end of the interest payment period. In the event that such a situation should arise, it is intended to meet the payments temporarily from the Reserve and to take account of the need to replenish the Reserve through an adjustment of the rate of interest for the subsequent half year. The last point is considered important, because as mentioned in EBS/87/228, there is no intention that the Reserve would generally be available to supplement the resources of the Subsidy Account.

This use of the Reserve would be a further possible temporary use of the Reserve to meet interest payments to lenders in addition to two other possibilities already discussed in staff papers. These are first, to cover overdue interest payments by borrowers under the facility; and second, to make interest payments to lenders if the particular modalities of a loan to the Trust made it necessary for the Trustee to agree with a lender on interest payments at times other than promptly after June 30 and December 31, as explained in EBS/87/253, Supplement 1. Use of the Reserve in each case would be expected to be temporary and the resources would be channeled back to the Reserve as soon as practicable.

The Chairman made the following summing up of the discussion at Executive Board Meeting 87/168:

In the discussion of December 11, most Directors indicated their general agreement with the essential features that have been proposed for the enhanced structural adjustment facility. I would like to begin my summing up by expressing my gratitude to member governments for their generosity in responding, and in particular for responding so quickly, to this proposal to increase the flow of resources to our poorest member countries. The creation of the enhanced structural adjustment facility will enable the Fund to play an active role in promoting and supporting economic policy adjustment in these countries, thereby contributing to the achievement of higher growth and a resolution of the severe debt and other problems that many of these countries are facing. After summing up the December 11 discussion, we will have to go through the revised legal documentation that is

needed to give effect to the Instrument to Establish the Enhanced Structural Adjustment Facility Trust and related decisions. These have been circulated to you as EBS/87/253, Revision 1 (12/14/87). Final approval of these decisions should follow in the next few days, enabling the new facility to begin operations as soon as the details of the arrangements for loans and grants with individual contributors can be concluded.

Let me summarize the agreed position on a number of important points.

1. Establishment of the enhanced structural adjustment facility and review of the existing facility

Directors reviewed the existing structural adjustment facility and agreed that it should continue to operate as in the past. The existing facility will continue to be available to eligible members that already have arrangements under the facility as well as to those that have not yet requested use of the facility's resources.

Directors agreed that a new lending facility--the enhanced structural adjustment facility--should be established and that it will operate concurrently with the existing structural adjustment facility. The enhanced facility will be financed from two Fund-related sources--the Special Disbursement Account and the Enhanced Structural Adjustment Facility Trust--and will also include the possibility that other lenders might support enhanced structural adjustment arrangements through loans to qualifying members in association with loans under the enhanced facility. For a member qualifying for an arrangement under the enhanced facility, resources will be provided from the Special Disbursement Account to the extent that the member has not exhausted its potential access under the existing facility; resources made available in excess of these amounts will be provided from the Trust and from associated sources.

Until the cutoff date for commitment of resources, eligible members that have not yet made use of the resources of the structural adjustment facility will have the option to request a full three-year arrangement under either the existing facility or the enhanced facility. Members currently making use of the resources of the existing facility may request a new three-year arrangement under the enhanced facility or continue their current arrangement to its conclusion. If a member currently using the resources of the structural adjustment facility chooses to request a new three-year arrangement under the enhanced facility, that request should normally be made at the time of expiration of an annual arrangement under the existing facility. However, earlier replacement of an existing arrangement by a three-year arrangement under the enhanced facility could also be permitted in exceptional cases.

2. Terms and conditions of loans under the enhanced structural adjustment facility

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Commitments of resources under the enhanced facility will be made upon approval of a three-year arrangement. All commitments and disbursements will be subject to the availability of resources. Commitments may be made at any time until the cutoff date. Most Directors agreed, taking into account the limited period of time during which the resources would be made available by contributors, that the cutoff date should be November 30, 1989. At the same time, most Directors considered that the final date for disbursements should not now be extended beyond June 30, 1992, although it was recognized that maintenance of this date would imply that there would be little flexibility to accommodate delays under annual programs in arrangements that were agreed later in the commitment period. This matter will be kept under review as experience is gained with the facility.

Disbursements from the Special Disbursement Account in conjunction with enhanced structural adjustment arrangements will be provided under the financial terms applying to loans under the existing facility, as amended. To the extent possible, the financial terms applying to loans from the Enhanced Structural Adjustment Facility Trust will be the same as those under the existing facility. In particular, it was agreed that the maturities of loans will be five and a half to ten years. Most Directors also believed that it would be appropriate to set the initial interest rate charged on loans from the Trust at 0.5 percent per annum, even if the amount of firmly committed resources in the Subsidy Account was initially not fully sufficient for this purpose, but additional resources were confidently expected. These Directors indicated that if it appeared, because of inadequate contributions or future adverse developments in interest or exchange rates, that resources available or committed to the Subsidy Account were likely to be insufficient to maintain the rate of interest at 0.5 percent throughout the period of operation of the Trust, the Fund should seek the additional resources necessary to achieve this objective. This issue is to be kept under review, and the interest rate will be adjusted as necessary at the beginning of each six-month interest period whenever resources available to the Subsidy Account are judged insufficient to maintain a rate of 0.5 percent on loans under the enhanced facility.

The intended terms for the Trust's lending, with which you have agreed, determine the essential features of the borrowing arrangements that will have to be concluded by the Fund as Trustee for the Enhanced Structural Adjustment Facility Trust and the lenders to it. These have been set out in a prototype circulated to potential lenders and annexed to EBS/87/245. While there will need to be comparability in substance among

agreements, there will no doubt need to be alterations to the form and structure of this prototype to meet the particular legal and institutional requirements of individual lenders, and we will be flexible in meeting these requirements. There was further discussion of the security to be provided to the claims on the Trust. Directors accepted that the proposals that had been put forward to safeguard the resources lent to the Trust were adequate to provide the necessary assurance to potential creditors. Although noting the views of some Directors, I have repeated that the phrase "all such initiatives as might be necessary" had to be understood to include the possible use of gold.

I should also comment on a few specific financial issues raised in the papers. First, most Directors did not favor the inclusion of a provision on rescheduling because, inter alia, it was considered that this would create undue complications in light of the limited period for which resources were being committed by contributors and also because it was felt that such a provision could threaten the integrity of the Reserve that most contributors find to be an essential component of the facility. Second, most Directors did not find it appropriate to provide for temporary encashment of claims through use of the Reserve, given the relatively small amounts that will be available in the early years and the importance of the Reserve as security for claims. Third, it appeared generally acceptable to most Directors that the provision for temporary suspension of calls should apply to all lenders. I should note in this connection that we appreciate the position of several contributors who are providing support to the enhanced facility, despite a very difficult balance of payments situation of their own.

3. Framework for lending under the enhanced structural adjustment facility

Resources to be made available under the enhanced facility will be committed upon Board approval of a three-year arrangement and disbursements will be made semiannually in accordance with the provisions specified in annual arrangements. The preparation of policy framework papers will be an essential element of the enhanced facility, and the policy framework process will be strengthened to reflect the summing up of the June 1987 review of the structural adjustment facility (EBM/87/93, 6/19/87), as well as continuing discussions with eligible recipient countries, the World Bank, and the interested donors.

The list of members eligible to use the enhanced facility is the same as that currently applying to the existing facility. Directors have expressed their strong appreciation for the indication by China that in the present circumstances, it did not intend to make use of the resources of the enhanced facility

despite remaining fully eligible to do so. Directors also expressed their appreciation for the statement by India that, in the absence of a fundamental deterioration in its balance of payments position, it also did not expect to borrow from the facility. These indications are indeed most generous contributions to the enhancement of the facility. Directors stressed that China and India are among the countries with the lowest per capita income, and face formidable development challenges; they were of the strong view that these decisions should not be used as a justification for any reduction in concessional assistance to China and India. I agree fully and insist on this.

Directors were in broad agreement that the objectives of programs under the enhanced facility should be to promote, in a balanced manner, both balance of payments viability and growth through mobilization of domestic and external resources, improvements in resource allocation, and the removal of structural impediments. Such programs should involve a substantial effort to strengthen the external payments position in a sustainable manner, and in particular to assure substantial progress during the three-year program period toward an overall position and structure of the balance of payments that is consistent with orderly relations with creditors and a reduction in restrictions on trade and payments, while permitting the timely servicing of obligations to the Fund.

Directors agreed that monitoring of enhanced programs supported by arrangements under the enhanced facility will be conducted through benchmarks. Most Directors favored the establishment of quarterly quantitative benchmarks for the key financial variables, and the use of structural benchmarks to monitor implementation of the most important structural policy measures. Most Directors supported the establishment of some benchmarks, including, where appropriate, some structural benchmarks, as semiannual performance criteria in all cases. In addition, mid-year reviews will also be required in most cases. I have carefully noted the reservations expressed by a number of Directors regarding the treatment of benchmarks as performance criteria, and I assure you that performance criteria will be limited in number and will generally involve only a subset of the benchmarks. Similarly, prior actions will be required sparingly but when necessary to lay the basis for a long or difficult adjustment process, and particularly where arrangements involve a front-loading of disbursements. In the event of a substantial delay in completion of a midyear review or in agreeing on an annual program, the total amount of resources to be made available to a member could be reduced or rephased over the remaining period of the arrangement.

Most Directors agreed that access to the resources of the enhanced facility will be differentiated according to the strength of the member's adjustment program and its financing need. The structure of the member's external debt and its prospective debt service burden, along with the expected evolution of other macroeconomic aggregates, will be important elements in this assessment. Directors generally agreed that access under three-year enhanced structural adjustment arrangements will be subject to a maximum limit of 250 percent of quota. However, Directors stressed again that the access limits do not constitute entitlements, and they agreed that access should normally be below the maximum and that the guidelines for access should be applied so that the rate of access for all qualifying members would average about 150 percent of quota. It was also indicated that, in highly exceptional circumstances, the maximum could be exceeded, but it was not envisaged that access would exceed 350 percent of quota even in these cases. These access limits, along with the operation of both the enhanced facility and the existing facility, will be subject to review in light of experience and the utilization of the available resources.

Directors agreed that the amount of resources committed to an individual qualifying member under a three-year enhanced structural adjustment arrangement and the amounts for the second and third yearly arrangements will be reviewed at the time of consideration of each annual program. However, most Directors indicated that, subject to the availability of resources, the amounts committed to a member would not normally be reduced because of developments in its balance of payments. However, in the event that balance of payments developments were markedly more favorable than envisaged at the time of approval of the three-year arrangement, and particularly because of improvements in the external environment, it would be suggested that the member reduce voluntarily its use of enhanced resources, either by requesting lower access at the time of approval of an annual arrangement or by forgoing in whole or in part a midyear disbursement.

Directors agreed that disbursements of loans under enhanced structural adjustment arrangements will be made semiannually, upon approval of an annual arrangement, and subsequently, on the basis of observance of performance criteria and, in most cases, completion of a midyear review. A range of views was expressed regarding the possibility of a limited front-loading of disbursements in some cases. Nonetheless, there seems to be a consensus that, subject to the availability of resources, the guideline should be that a uniform distribution of disbursements would be preferable and that any front-loading should not result in first-year disbursements exceeding 40 percent of the total amount to be made available under the three-year enhanced structural adjustment arrangement. However, I take it that there may be scope

for a higher first-year disbursement in some very exceptional cases. Existing policies regarding members with overdue obligations to the Fund will be retained; how best to deal with cases of large and protracted arrears is a question to which we will return soon, but in a different context.

#### 4. Relationship with other Fund facilities

Directors noted that members qualifying for loans under the enhanced structural adjustment facility would retain eligibility for access to the Fund's general resources. Access to those resources will have to be examined carefully on a case-by-case basis, taking into account a range of factors envisaged in the present guidelines, including past performance and use of Fund resources, terms for lending, the possible availability of financing from the enhanced facility and other sources, and the speed and time profile of the anticipated balance of payments adjustment.

Mr. Grosche recalled that some Directors had suggested that the provision that the Fund would "consider fully and in good faith all such initiatives as might be necessary to assure full payment to members" should mention the possibility of the sale of a portion of the Fund's gold, whereas a few Directors were opposed to the inclusion of any reference to gold in the decisions establishing the enhanced facility. Could the summing up indicate that it was understood that use of the Fund's gold was among the initiatives that could be undertaken? Such a reference would be helpful to a number of potential contributors who had problems with respect to the security of claims on the Trust.

Mr. Prader stated that he supported Mr. Grosche's suggestion.

Mr. Ortiz remarked that although he would prefer a specific reference to the possibility of gold sales in the decision, he could go along with Mr. Grosche's suggestion. A reference to the Board's understanding on that issue would satisfy his authorities' concern about the security of claims on the Trust.

The Chairman recalled that during the previous Board discussion of the enhanced facility, the staff representative from the Legal Department and he himself had made it clear that the sale of gold was among the possible initiatives that the Fund was committed to consider. That understanding would be reported in the record of the meeting.

Mr. Zecchini remarked that he associated himself with Mr. Grosche's comments. The issue would be clarified if a sentence reflecting the Chairman's understanding was incorporated in the summing up.

Mr. Nimatallah commented that in view of the agreements that had been reached between the Fund and some potential donors, and in particular, the

understanding that a pledge with respect to the Fund's gold should not be stressed, he preferred that no specific reference to the sale of gold should be made in the summing up.

The Chairman observed that the summing up and the minutes had the same legal import. However, in view of the preferences expressed by some Directors, he proposed to take up the question on a bilateral basis and to report the outcome of his discussions when the Board considered the revised decisions on December 18, 1987.

The Executive Directors then considered the draft legal documentation to give effect to the enhancement of the structural adjustment facility, which had been revised in the light of the Board discussion on December 11.

The staff representative from the Legal Department remarked that the suggestion to use the Reserve, on a temporary basis, to meet interest payments due to creditors in the event that the resources available in the Subsidy Account were insufficient to cover the required subsidy payments, was intended to provide some flexibility for the operations of the Subsidy Account. Such flexibility was needed if the interest rate on Trust loans was to be adjusted prospectively so as to assure the borrower a particular rate over a half-year period. If the interest rate calculated at the beginning of the half-year period was too low to cover the difference between the subsidy payment and the interest payment due to creditors, the interest rate on the Trust loan would be adjusted in the subsequent half-year period so that the Reserve would be replenished by the interest payment in the succeeding period.

Mr. Ortiz noted that with respect to the liquidity of claims and the access of a creditor to the Fund's general resources in the event of unfavorable developments in its reserve position under Article V, Section 3(b)(ii), it was indicated in EBS/87/253, Revision 1, that "if it were desired to exclude such purchases from the calculation of the reserve tranche, and to establish special repurchase periods, decisions to that effect would need to be adopted by an 85 percent majority." He would appreciate a clarification of that point by the staff.

The staff representative from the Legal Department remarked that if it was intended to establish special repurchase periods, for example, a period shorter than the usual three to five years, for purchases under Article V, Section 3(b), then a decision would be needed to that effect and would require an 85 percent majority of the voting power. Likewise, if it was desired to exclude such purchases from the calculation of the reserve tranche, a decision would have to be taken to establish the floating character of the purchase. The staff could prepare draft decisions for Board consideration in light of Directors' comments on those issues.

Mr. Ortiz remarked that he understood that the Fund would consider loans to the Trust to be adequate safeguards for such use by creditors of its general resources under Article V, Section 3(b). That point had not been explicitly mentioned in the revised documentation.

The staff representative from the Legal Department commented that the understanding that a claim on the Trust would be taken into account when considering the amount of requested access could be included in a later decision regarding access under Article V, Section 3, for the purpose of clarification, but a separate decision in that regard was not required.

Mr. Prader remarked that the special options described in the staff paper were particularly important for those members providing loans to the Trust out of their reserves. Moreover, his authorities were confident that the 85 percent majority required for such a decision would not pose exceptional difficulties.

Mr. Ovi agreed with Mr. Prader that implementing the options described by the staff should not pose any difficulties. He understood that a floating reserve was customary in Fund arrangements, so that failure to adopt a decision in that regard would be a deviation from traditional Fund policies. Moreover, for one of his central banks, access to the general resources in order to mobilize a claim was a precondition for its participation. If a creditor had to draw on its reserve tranche, it would not be mobilizing a claim, but rather using an existing asset.

Mr. Nimatallah, commenting on the Decision on Review of the Structural Adjustment Facility and Establishment of the Enhanced Structural Adjustment Facility, remarked that while there were three sources of financing for the enhanced facility, provisions governing the use of resources were given for only two sources, namely, resources provided by the structural adjustment facility and resources provided by lenders to the enhanced facility. A provision governing the use of resources provided through associated lending should be added to paragraph 3.

The staff representative from the Legal Department explained that a reference to associated lending had not been included, pending the conclusion of discussions on arrangements between the Fund and the lender. If Executive Directors agreed, the words "and in accordance with arrangements to be agreed between the Fund and the lenders" could be added to the end of paragraph 3 of the draft Decision on the Review of the Structural Adjustment Facility and Establishment of the Enhanced Structural Adjustment Facility.

Mr. Reddy, referring to paragraph 2(a) of that Decision, commented that the phrase "normally in conjunction with loans under the structural adjustment facility" gave the impression that the enhanced facility was to be used together with the existing facility, which was not the Board's intention. Could that phrase be deleted?

The staff representative from the Legal Department remarked that if a member opted for an arrangement under the enhanced facility, the resources in support of that arrangement would be derived from the resources of the Special Disbursement Account and the Trust. "Normally," resources from both of those sources would be used in conjunction, unless countries had

exhausted their access limits under the Special Disbursement Account. In the latter event, a loan under the enhanced facility would be funded entirely by the Trust or by the Trust in conjunction with associated lending.

Mr. Zecchini, commenting on the Decision on Amendment of the Regulations for the Administration of the Structural Adjustment Facility, recalled that at the previous discussion on the enhanced facility, he had proposed that the deadline for the extension period should be specified. Subparagraph (4) should read "...the period of the three-year commitment may be extended up to mid-1992...."

The staff representative from the Legal Department remarked that a specific reference was unnecessary and might even be limiting. It was clear from the text of the Trust Instrument that no disbursement could be made after a certain period when all commitments were, in fact, fully exhausted. Thus, the phrase "subject to these Regulations" would govern both the Trust Fund and the Special Disbursement Account component of loans from the facility with respect to the final date of availability of resources. Moreover, there was a possibility that the commitment period would be extended in agreement with lenders. In that event, a fixed date--say, up to mid-1992--would be limiting. He therefore preferred to leave the provision as it was to allow flexibility if the commitment period was extended.

The Chairman observed that his summing up addressed Mr. Zecchini's concern by indicating that "...most Directors considered that the final date for disbursements should not now be extended beyond June 30, 1992, although it was recognized that maintenance of this date would imply that there would be little flexibility to accommodate delays under annual programs in arrangements that were agreed later in the commitment period. This matter will be kept under review as experience is gained with the facility."

Mr. Yamazaki remarked that he had received news from Tokyo that morning indicating that with the timely assistance of the Fund staff mission visiting Tokyo, his authorities had almost concluded their deliberations on lending to the Trust and could broadly support the proposed decisions as well as the borrowing arrangement. It had taken a long time to arrive at a feasible scheme for the capital contribution, since the proposed financial arrangements for the enhancement did not fit the institutional framework of the Japanese Government. The Managing Director's strong initiative had helped to overcome that difficulty so that his authorities could realize their intention of supporting the enhancement of the structural adjustment facility.

His authorities were still engaged in finalizing their work, Mr. Yamazaki continued. He therefore still had reservations on the proposed borrowing operations of the Trust, since the proposed decision

might not facilitate the conclusion of deliberations on Japan's contribution. He expected that a definitive commitment regarding Japan's contribution would be announced at the next Board discussion of the enhanced facility.

Mr. Zecchini, commenting on the Decision for the Establishment of the Enhanced Structural Adjustment Facility Trust, recalled that at the previous Board discussion on the enhanced facility he had suggested an addition to the second paragraph to convey the intention of the Fund to achieve an expeditious payment to lenders. He proposed that the sentence should be amended to read: "as might be necessary to assure full and expeditious payment to lenders."

The staff representative from the Legal Department said that he would think about the formulation and come back later to that issue.

Mr. Nimatallah noted that the decisions provided for the creation of a new facility and the establishment of a Trust. He understood that the Trust would be created by an external entity, for example, the lenders, who would then entrust the Fund to manage it according to a legal Instrument. He would appreciate an explanation of how the decisions under discussion were tied together. Who retained the Fund as Trustee, and who established the Trust? Also, what right did the Fund have to give a commitment to do certain things?

The staff representative from the Legal Department explained that the complex structure of the decisions was attributable to the various sources for funding the exercise, namely, the use of resources from the Special Disbursement Account under the original facility and the resources for funding the Trust. The decision to establish the Trust and the Instrument attached to it was required under Article V, Section 2(b), which permitted the Fund to administer resources provided by lenders and donors under an arrangement subsequent to that provision. The decision to be taken by the Board approved that arrangement. The structure of the decision and separation of the Instrument from the decision establishing the Trust followed the practice used for the 1976 Trust Fund.

As for the right of the Fund to take such a decision, the introductory section of the Instrument explained that "to help fulfill its purposes, the International Monetary Fund has adopted this Instrument establishing the Enhanced Structural Adjustment Facility...which shall be administered by the Fund as Trustee..." the staff representative noted. That sentence could be put into the decision itself to clarify the relationship between the decision and the Instrument, but it would not change the substance.

Because it was proposed that the original facility and the Regulations for that facility should continue without change, the staff representative commented, a decision was needed to add a paragraph to those Regulations for those members that did avail themselves of the additional resources provided under the enhanced facility. Consequently, the Trust Instrument contained a crossreference in Section II, paragraph 1(b), to the addition

to the Regulations. The desire to have, as far as possible, the same rules for the two facilities in order to coordinate their administration had thus led to a somewhat complicated structure in the presentation of the decision.

In paragraph 2 of the proposed decision for the establishment of the Trust, the staff representative from the Legal Department explained, the Fund undertook the commitments made as the Fund, rather than as Trustee. Similarly, the establishment of the Trust required the adoption by the Fund of the Instrument attached to the decision. Subsequently, the Trust would be governed by the rules of the Instrument, and the Trust would be administered by the Fund as Trustee.

Mr. Rye asked whether the word "such" in the second paragraph of the decision establishing the facility had any particular significance.

The Chairman remarked that he understood it to include the full range of initiatives, "as might be necessary."

Mr. Grosche noted that according to Section I, paragraph 3 of the draft Instrument, the SDR was to be the unit of account for commitments, loans, and all other operations and transactions of the Trust. In that connection, his authorities were still considering a range of possible approaches for their capital contribution to the Trust, and they expected further clarifications in that regard during the forthcoming negotiations with the Fund staff. Pending those clarifications, they wished to retain some flexibility, particularly with respect to the denomination of loans extended to the Trust, including the issue of hedging and the costs of hedging operations if the unit of account was the SDR, as well as with reference to the interest rate applied to the capital contribution. He would certainly like to see the Instrument implemented as proposed, but he was not yet in a position to agree to the text.

More generally, there was no mention that loans to the Trust and the loans extended by the Trust had to be repaid, Mr. Grosche observed. Did he understand correctly that there was no need to include such a provision in the legal text?

The staff representative from the Legal Department remarked that additional legal documentation--namely, the individual borrowing agreements--would specify the repayment dates. Moreover, the Instrument provided that payments would be made from the loan account. However, the obligation to repay would derive from the borrowing agreements with individual lenders.

Mr. Zecchini, referring to the same paragraph, commented that a clarification was needed on the rationale underlying the second part of the sentence, which read: "...provided that commitments of resources to the Subsidy Account may be made in currency." Specifically, why was there an explicit reference to the Subsidy Account only; and what limitation was implied by that clause?

The staff representative from the Legal Department remarked that the clause had been added in the light of the previous Board discussion and legally meant that everything else was denominated in SDRs except for commitments that might be made to the Subsidy Account. It was still hoped that commitments would be made in SDRs, but some flexibility was being provided.

Mr. Zecchini said that he understood "provided" to mean "with the exception" of commitments of resources made in currency to the Subsidy Account. He wished to confirm that the word "provided" was to be interpreted in that sense.

The staff representative from the Legal Department confirmed Mr. Zecchini's understanding. The standard formulation to introduce an exception to a general principle in legislative drafting was the phrase "provided that." Therefore, the principle was that commitments were to be made in SDRs; the one exception was that commitments to the Subsidy Account might be made in currency.

Mr. Grosche suggested that Section II, paragraph 1(c) of the draft Instrument, should be amended to read: "the member is making an effort to strengthen substantially and in a sustainable manner its balance of payments position," so as to be consistent with the language used in the first paragraph in Section I on the purposes of the Trust.

Mr. Reddy noted that paragraph 1 of Section I set forth the purposes of strengthening the balance of payments and of fostering growth, whereas Section II, paragraph (c) identified only one of those purposes. The draft Instrument did not reflect how the purposes were to be translated into action and, as it was, seemed to place undue emphasis on one particular purpose. He would therefore like to see the inclusion of the growth objective in paragraph (c) as well. That same point also applied to paragraph 2(c) of Section II.

The Deputy Director of the Exchange and Trade Relations Department observed that Section I of the Instrument dealt with the general purposes of Trust loans, while Section II dealt with eligibility and conditions for assistance, including the assessment of repayment possibilities, which, in turn, involved the strengthening of the balance of payments. For that reason, the growth objective, which was explicitly stated as a general objective and principle in Section I, was stated in terms of the improvement in the balance of payments when referring to the conditions for assistance in Section II.

The Chairman remarked that Mr. Reddy's suggestion would add another condition for eligibility. Since the condition of fostering growth could imply additional efforts beyond those needed for substantial and sustained improvement in the balance of payments, it might cause difficulties for the recipient country. Also, once an objective was stated in a legal document, there was no need to repeat it. He was therefore satisfied with paragraph 1(c), as amended by Mr. Grosche, and paragraph 2(c) as it stood.

Mr. Reddy noted that in Section II, the access limit was not specified. Would a separate decision have to be taken in that regard?

The staff representative from the Legal Department responded that a separate decision on the amount of access would be needed. However, some indication of the initial maximum limit based on resources available had been given in the Chairman's summing up. The access limit would be reviewed annually or within the time frame outlined in the Instrument. To avoid the need to amend the Instrument every time access limits were reviewed, specific figures were not given in the draft Instrument.

Mr. Santos recalled that at the previous Board discussion on the enhanced facility, Mr. Mawakani had proposed an additional provision, namely, that access to the Fund's resources under other Fund policies would remain available to eligible countries in accordance with the terms of those policies. That wording was used in the Regulations for the Administration of the Structural Adjustment Facility. The Chairman's summing up at the outset of the present meeting had unambiguously reaffirmed that principle. Was there any substantive reason why that provision was not included in the draft Instrument?

The staff representative from the Legal Department explained that provisions on access to other Fund resources could not be included in the Instrument, which regulated access to resources under the Trust only. Access to the Fund's other resources was regulated by policy decisions and by considerations that guided Fund policy on access, which were confirmed in the Chairman's summing up.

Mr. Grosche, commenting on paragraph 4 of Section II, remarked that his authorities considered that the Fund should indeed aim at an interest rate on Trust loans of 0.5 percent, but that the extent to which interest payments were actually subsidized could be decided only on the basis of the financing available to the Subsidy Account. In that regard, he welcomed the staff's statement at the outset of the meeting. Nonetheless, it would be advisable not to refer to a specific interest rate in a legal document. Rather, a general reference would be sufficient, leaving the decision on the interest rate to the Board to be taken in the manner indicated in the Chairman's summing up. He therefore suggested that paragraph 4(a) should read: "The interest rate on the outstanding balance of a Trust loan shall be charged at a rate to be determined by the Trustee." Also, the reference to a rate of 0.5 percent should be omitted in Section IV, paragraph 5.

The Chairman remarked that he understood the prudent consideration underlying Mr. Grosche's suggestion not to have a binding legal text. Management's goal was an interest rate of 0.5 percent on loans from the Trust, and when launching the initiative and negotiating with the membership, he had strongly argued that for those countries eligible to use the enhanced facility, the conditions applying to the structural adjustment facility were relevant. The changes suggested by Mr. Grosche might give the impression that something fundamental to the understanding reached

with many countries had changed. He therefore preferred the text as it was, subject to the careful consideration he had offered in his summing up. That created a moral obligation to strive in the coming months to attain the means to assure a 0.5 percent rate of interest. If sufficient funding for the Subsidy Account was not forthcoming, then decisions would have to be taken expeditiously to increase the interest rate somewhat to match available resources. In any event, the constraint of the exercise--to provide resources on the same terms and conditions as under the existing facility--had to be accepted.

Mr. Grosche responded that he also would not like to deviate from the objective of attaining a 0.5 percent interest rate and everything possible should be done to reach it. Nevertheless, the Fund had always carefully drafted its legal texts, and what was stated in the Instrument should be achievable. At present it could not be said that the targeted rate of 0.5 percent was achievable. He was therefore reluctant to include a specific figure in the legal text. Moreover, while he recognized the implicit moral obligation, he doubted that such an obligation should be included in a decision of the Fund. As with access limits, a separate decision on the interest rate could be taken once the availability of the resources was assured.

The staff representative from the Legal Department remarked that the text was qualified, in that paragraph 4(a) included the proviso that the rate of 0.5 percent was subject to the calculations to be made in accordance with Section IV, paragraph 5. The considerations given in Section IV, paragraph 5, were, inter alia, the availability and the prospective availability of resources. The Chairman's summing up also referred to that proviso, namely, in stating, "that the interest rate will be adjusted as necessary at the beginning of each six-month interest period whenever resources available to the Subsidy Account are judged insufficient to maintain a rate of 0.5 percent...." A decision needed to be taken on the initial interest rate, based on the resources available or confidently expected. If there was a shortfall, the Instrument provided that the rate would be adjusted in the succeeding interest rate period. The reference to a specific figure of 0.5 percent set the objective to be achieved. It also established a floor for subsidization. For the structure of the subsidy exercise, a reference point was needed and that point was 0.5 percent. Moreover, the Instrument also indicated some of the parameters for establishing the interest rate, which depended on a statement of the target rate.

Mr. Zecchini remarked that as Mr. Grosche had correctly noted, the amount of resources available to subsidize loans from the Trust was uncertain. It was likewise uncertain what amount of resources was available for Trust loans. Therefore, the financial arrangements for the enhanced facility were at a stage of uncertainty on all grounds.

As a matter of record, his authorities considered the 0.5 percent interest rate charged to borrowing countries to be a fundamental aspect of the enhanced facility, Mr. Zecchini commented. Without that level of

subsidization one could hardly speak of an enhancement of the structural adjustment facility. In his view, for a number of justifiable reasons, the Board was gradually moving away from the conditions and terms applicable to an enhanced facility. Earlier, when he had questioned the establishment of a completely separate account for the facility, the staff had explained that there were some legal arguments in favor of a separate arrangement. Having adopted the present route, his authorities' position with respect to the interest charged to borrowers was that the objective of 0.5 percent was an irrevocable condition.

Mr. Reddy remarked that from the point of view of potential borrowers, the maximum access available under the facility as well as the cost of use of those resources was crucial information that should be set forth in the Instrument.

Mr. Grosche noted that paragraph 4(b) of Section II mentioned the repayment of Trust loans and interest in "other currency." He would prefer that both disbursements and repayments should be made in "freely usable currencies as decided by the Trustee."

The staff representative from the Legal Department remarked that the proposed amendment presented no difficulty.

Mr. Zecchini, commenting on Section IV of the draft Instrument, recalled that at the previous discussion on the enhanced facility, he had proposed a deletion in paragraph 4 of the phrase "in such order as it may determine." He saw no need to specify what kind of flexibility the Trustee may deem appropriate or adequate. In paragraph 5(a) he had suggested the elimination of the words "to the extent possible." The sentence should read, "...in the light of (i) the objective of reducing the rate of interest charged on Trust loans to 0.5 percent...."

The staff representative from the Legal Department commented that "in such order as it may determine" could be deleted, as long as it was understood that flexibility was needed in drawing on the resources of the Subsidy Account. He would, therefore, prefer to state explicitly that the Fund would need that flexibility. Similarly, "to the extent possible" had been retained in paragraph 5(a) to indicate that there would be flexibility.

The staff representative from the Treasurer's Department remarked that the concept of flexibility was indeed most important.

Mr. Zecchini remarked that he did not think that the flexibility of the Trust's operation would be put at risk by the suggested deletion.

The staff representative from the Treasurer's Department agreed that the proposed deletion in paragraph 4 was acceptable. However, for the record, the intention was to treat the funds in the Subsidy Account as totally fungible, because, for example, certain resources that had been invested might have to be disinvested.

The staff representative from the Legal Department considered that the proposal to delete the words "to the extent possible" in paragraph 5(a) was acceptable. The phrase qualified the stated objective, whereas the remainder of the paragraph set out the other parameters that would enter into the calculation of the subsidy, namely, the resources available and the interest rate charged by lenders. The mechanism in place and the adjustment of the interest rate would have to be made if those conditions were not met indicated that the rate of 0.5 percent was really an objective.

The Chairman noted that Directors accepted the proposed amendment to paragraph 5(a), but that Mr. Grosche had expressed reservations with respect to the deletion.

Mr. Zecchini, commenting on paragraph 5(c) of Section IV, remarked that consistent with his previous statement on the specification of a rate of interest and financial arrangements for the Trust, he had reservations on the entire subparagraph at the present time.

The Chairman took note of Mr. Zecchini's reservations.

Mr. Reddy, referring to paragraph 5(b) of Section IV, suggested that the phrase, "beginning with the operations" should be deleted at the beginning of the second sentence because the preceding phrase, "at any time" was sufficient to set the time period.

The staff representative from the Legal Department observed that it was important to indicate that the mechanism being described related to the adoption of the interest rate at the start of the Trust's operations. If the phrase "including the beginning of the operations" was deleted, it might have to be emphasized somewhere else. He understood that it was important, particularly for Mr. Grosche, that the beginning of operations should be emphasized with respect to the mention of the 0.5 percent interest rate.

The Chairman remarked that he accepted Mr. Reddy's point that the expression "at any time" included the beginning of operations. He suggested that the phrase should be deleted and that the staff representative's explanation should be set forth in the record of the discussion.

Mr. Marcel suggested that paragraph 1 of Section V should incorporate the possibility of including additional reserves, if necessary, among the resources to be held in the Reserve Account.

The staff representative from the Legal Department commented that at the present stage, the staff did not foresee any additional reserves becoming available and therefore had not included any reference to them in the draft Instrument. The guiding principle behind that approach was that only those resources committed to the Reserve Account should be mentioned. The Instrument should not include in the list of resources of the Reserve Account additional resources that would only become available if a separate decision on their allocation to the Reserve Account were taken.

Mr. Zecchini, commenting on Section VI, recalled that at the previous discussion on the enhanced facility, he had remarked that the nonnegotiability of claims was not consistent with his authorities' views. They would like to have an explicit reference to the principle of the transferability of claims among members, apart from participation in the "electing lender" scheme. He requested that the staff incorporate that request in the draft text for consideration by the Board at the next discussion of the enhancement.

Mr. Grosche, commenting on paragraph 2(b) of Section VII, wished to confirm that the provision that "the property and assets held in the other accounts of the Fund shall not be used to discharge liabilities or to meet losses arising out of the administration of the Trust" did not conflict with the provisions in paragraph 2 of the decision establishing the enhanced facility.

The staff representative from the Legal Department confirmed that Mr. Grosche's understanding was correct.

Returning to Mr. Zecchini's request regarding paragraph 2 of the decision establishing the facility, the staff representative from the Legal Department suggested that the inclusion of the word "expeditious" probably would be the best response. The sentence would read: "...to consider fully and in good faith all such initiatives as might be necessary to ensure full and expeditious payment to lenders."

The Chairman remarked that in the coming week, management and staff would try to clarify a few remaining points in the legal documentation. On December 18, it was hoped that the Board would formally adopt the decisions to give effect to the enhancement of the structural adjustment facility. At that time he would also report on the status of contributions to the enhancement. Until the financing objectives were attained, he urged Executive Directors not to reduce their efforts in their respective capitals to achieve as positive an announced commitment as was possible. He then invited the staff representative from the Legal Department to comment on the further decisions that would have to be taken by the Board.

The staff representative from the Legal Department explained that further decisions would need to be taken on the initial interest rate, on the initial access limits and, if desired, on liquidity issues with respect to access to Fund resources under Article V, Section 3(b). There was, however, some flexibility with respect to the timing of those decisions, and they could be taken after the establishment of the facility.

Mr. Zecchini commented that he did not know whether the legal instruments could be formally accepted on December 18. He understood that once there was a consensus among Board members on the text, the Chairman would brief Executive Directors on the financial arrangements. The decisions could be taken once there was a clear picture of the financial arrangements.

Mr. Grosche remarked that he supported Mr. Zecchini's views.

The Chairman suggested that Executive Directors leave the question of the timing of the adoption of the decisions to give effect to the enhancement open until their December 18 discussion.

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/87/170 (12/14/87) and EBM/87/171 (12/15/87).

2. APPROVAL OF MINUTES

The minutes of Executive Board Meetings 87/78 through 87/80 are approved. (EBD/87/316, 12/8/87)

Adopted December 14, 1987

3. EXECUTIVE BOARD TRAVEL

Travel by an Advisor to Executive Director as set forth in EBAP/87/271 (12/11/87) is approved.

APPROVED: July 25, 1988

JOSEPH W. LANG, JR.  
Acting Secretary