

FOR
AGENDA

MASTER FILES

ROOM C-120

01

SM/85/131

May 13, 1985

To: Members of the Executive Board

From: The Secretary

Subject: Financial Remedies in Connection with Overdue Financial
Obligations to the Fund - Legal Aspects

There is attached for consideration by the Executive Directors a paper on the legal aspects of the financial actions that the Fund can take in cases of overdue financial obligations to the Fund, which is scheduled for discussion on Wednesday, June 5, 1985.

Att: (1)

Other Distribution:
Department Heads

INTERNATIONAL MONETARY FUND

Financial Remedies in Connection With Overdue
Financial Obligations to the Fund -
Legal Aspects

Prepared by the Legal Department

(In consultation with the Treasurer's Department)

Approved by George P. Nicoletopoulos

May 10, 1985

I. Introduction

The failure by some members to discharge financial obligations to the Fund on time has drawn attention to the harmful consequences of such failures for the financial position of the Fund. The obligations that have not been met on time have included repurchase obligations and the payment of periodic charges on the Fund's holdings of currency in the General Department, the payment of net charges and assessments in the SDR Department, and the interest on, and repayment of, Trust Fund loans.

When these financial obligations are not discharged on time, the Fund may sustain financial losses. 1/ For instance, in the case of late payment of periodic charges in the General Department, which are payable in SDRs, the Fund suffers a loss which could be regarded as being equal to the interest on the amounts that it would have received if payment had been made when due. 2/ In addition to financial losses, overdue financial obligations may have nonfinancial consequences for the Fund and its members but these are not considered in this paper.

This memorandum inquires into the legal actions that the Fund could take to deal with the consequences of overdue payments in relation to the members that caused these consequences, and to prevent further harm from occurring.

The provisions of the Articles, Rules, and decisions of the Fund, as well as rules of international law relevant to the questions under consideration, are reviewed in Section II. Sections III, IV, and V describe the legal actions that are available to the Fund in respect

1/ Except in the case of late payment of net charges in the SDR Department, see Section IV below.

2/ The extent of the losses resulting from late payments is discussed in "Special Charges on Overdue Financial Obligations to the Fund" (EBS/85/121), prepared by the Treasurer's Department.

of the members that fail to make timely payments. A Summary and Conclusions are set forth in Section VI.

II. Relevant Articles, Rules and Decisions of the Fund and Other Principles of Law

A. Articles, Rules and Decisions

1. General Department

Actions by the Fund in connection with legal remedies relating to overdue financial obligations could be based on the following legal provisions.

(a) The Fund has the power, in accordance with Article V, Section 8(b) 1/, to levy periodic charges on the average daily balances of a member's currency that have been acquired under a policy subject to an exclusion under Article XXX(c) 1/ and, after excluding the amounts subject to exclusion under XXX(c), on such balances as exceed the amount of the member's quota. At present all of the Fund's holdings of currencies resulting from purchases (other than reserve tranche purchases) by a member are excluded by decisions of the Fund for the purpose of determining the member's reserve tranche position. 2/ Consequently, a member may have a substantial reserve tranche position, and may be receiving remuneration on a part of it, while the Fund holds a substantial amount of the member's currency that is subject to periodic charges.

(b) The requirement that the Fund levy charges on certain average daily balances of a member's currency, as set out in Article V, Section 8(b), is subject to the rule that "The rates of charge normally shall rise at intervals during the period in which balances are held". The rates of charge on the Fund's balances of members' currencies are not specified in the Articles, but are determined by decisions of the Executive Board. The rates currently in effect are set forth in Rule I-6. Rates of charge under Article V, Section 8(b) must be "uniform for all members" (Section 8(d)). 1/

(c) The requirement of uniformity does not apply to special rates of charge that the Fund might impose pursuant to Section 8(c) 1/ on balances that a member has failed to repurchase as required under Section 7 of Article V. Section 8(c) permits, after consultation with the member involved on the reduction of the Fund's holdings of its

1/ See Attachment I.

2/ Decisions Nos. 2836-(69/87), 5591-(77/163), and 6830-(81/65), Selected Decisions, Tenth Issue, pages 298-299.

currency, the imposition of "such charges as the Fund deems appropriate" on the balances that should have been repurchased.

(d) The determination of rates of charge under both Section 8(b) and (c) requires a seventy percent majority of the total voting power (Section 8(d)). 1/ All charges must be paid in SDRs, but the Fund is authorized, in exceptional circumstances, to permit a member to pay charges in the currency of another member or in its own currency (Section 8(e)). 1/

(e) In accordance with Article V, Section 7(e), 1/ the Fund must adopt a repurchase period for its holdings of currency that were not acquired as the result of purchases but are subject to charges because they cause the Fund's holdings to be above quota for this purpose. A decision determining the period must be taken by a seventy percent majority of the total voting power, the same majority as that required for the adoption of a rate of charge.

(f) With respect to the procedures for the payment of charges, Rule I-2 of the Fund's Rules and Regulations specifies that periodic charges are to be paid (i) semiannually (each June 30 and December 31) on the average daily balances acquired as the result of purchases financed by supplementary financing or by borrowed resources under the Policy on Enlarged Access, and (ii) quarterly on all the other balances each July 31, October 31, January 31, and April 30 of the Fund's financial year. Rule I-2 further provides that the Fund is to notify each member by cable, as soon as possible after these dates, of the charges the member owes the Fund and that the charges so notified are to be paid on the third business day following the dispatch of the notification.

(g) The rates of charge on holdings resulting from purchases (other than reserve tranche purchases) are laid down in Rule I-6.(1) through (5). The rate of charge on balances subject to charges that were "acquired otherwise than as the result of a purchase" 2/ is the same rate that applies to holdings resulting from purchases of ordinary resources in the credit tranches, under the Extended Fund Facility, the Compensatory Financing Facility and the Buffer Stock Facility (Rule I-6.(7)).

(h) The Articles give members the absolute right to repurchase at any time the Fund's holdings of their currencies that are subject to charges. Reductions in the Fund's holdings of a member's currency resulting from repurchases or sales, or from

1/ See Attachment I.

2/ The exception in Rule I-6.(6) with respect to holdings resulting from the sale of gold to a member for its own currency is no longer relevant, as such holdings are no longer outstanding.

operational payments by the Fund, are applied in accordance with the rules of attribution set forth in Executive Board Decision No. 6831-(81/65), as amended. 1/ With certain exceptions, 2/ the decision follows the usual law and practice in most countries, which give the payor/debtor the freedom to choose which obligation he wishes to be discharged pro tanto by a payment. The usual practice is that only when the payor does not state how a payment is to be applied does the receiver/creditor have the discretion to choose the obligation to be discharged pro tanto. There is a limit to this discretion, however, for in some legal systems, if there is an outstanding obligation which if not discharged or reduced would result in a forfeiture, the payment must be applied by the creditor so as to prevent this result.

Special rules apply to repurchases relating to purchases under the Supplementary Financing Facility 3/ and the Policy on Enlarged Access 4/, which require that when such a repurchase is attributed to a purchase made with borrowed resources and is made in advance of the schedule of installments, it must be accompanied by a repurchase in respect of the part of the purchase financed with ordinary resources, if any part of that purchase financed with ordinary resources is still outstanding.

2. SDR Department

The following provisions govern the payment of net charges and assessments in the SDR Department.

(a) Each participant in the SDR Department is required to pay charges on the amount of its net cumulative allocation of SDRs, and is entitled to receive interest on the amount of SDRs it holds. In addition, a participant must pay charges on any negative balance that it may have, and on its unpaid charges. Both interest and charges are paid in SDRs (Article XX, Sections 2 and 5). 5/ The rate at

1/ Selected Decisions, Tenth Issue, page 108.

2/ The exceptions under Decision No. 6831-(81/65), as amended, are: (i) a member may attribute a reduction resulting from a sale of its currency or an operational payment by the Fund to a repurchase obligation relating to a purchase financed from borrowed resources only if the Fund is obligated or entitled to make an immediate repayment; and (ii) an attribution to create or increase a member's reserve tranche position cannot be made for a repurchase or if the member has outstanding purchases financed by borrowing under the GAB.

3/ Paragraph 7(d), Decision No. 5508-(77/127), Selected Decisions, Tenth Issue, pages 33, 37.

4/ Paragraph 10(b), Decision No. 6783-(81/40), Selected Decisions, Tenth Issue, pages 40, 44.

5/ See Attachment I.

which charges are levied must be the same for all participants, and must be equal to the rate of interest on the SDR (Article XX, Section 3). 1/

(b) The procedures regarding the payment of the charge are laid down in Rule T-1.(a) of the Fund's Rules and Regulations.

(c) The principle of separation of assets and property as between the General and the SDR Departments is given effect by the rule that assets or property held by the Fund in the General or the SDR Department may not be used to discharge or meet the liabilities, obligations, or losses of the Fund incurred in the conduct of the operations and transactions of the other Department. With respect to the expenses of conducting the business of the SDR Department, this rule suffers a temporary exception, because these expenses are paid in the first instance by the Fund from the General Department. From time to time, the Fund must levy assessments on all participants in order to reimburse the General Department (Article XVI, Section 2). The corollary of the Fund's obligation to levy assessments is the obligation of the participants to pay the levy in SDRs (Article XX, Section 4). 1/ Assessments have to be at the same rate for all participants on their net cumulative allocations. The procedures regarding the payment of assessments are laid down in Rule T-2 of the Fund's Rules and Regulations.

(d) A participant that lacks sufficient SDRs to pay the charges or assessment due by it is obligated and entitled to obtain them, for currency acceptable to the Fund, in a transaction with the Fund conducted through the General Resources Account. If sufficient SDRs cannot be obtained in this way, the participant is obligated and entitled to obtain them with a freely usable currency from a participant which the Fund must specify (Article XX, Section 5). 1/

(e) The Fund is required to pay interest due to holders of SDRs whether or not it receives sufficient amounts in charges to meet these payments. (Article XX, Section 1). 1/ If the amount of SDRs in a participant's account is insufficient to meet the charge due by it, the Fund creates an amount of SDRs equal to the amount of the shortfall. SDRs acquired by the participant subsequently are applied to the overdue charges and cancelled (Article XX, Section 5). 1/

(f) The Fund has no authority to create SDRs if the amount of SDRs in a participant's account is insufficient to pay the assessment levied on it, or to establish a negative balance for the participant against which SDRs subsequently acquired by the participant would be applied.

1/ See Attachment I.

3. Trust Fund

Recipients of loans from the Trust Fund are required to pay interest and to repay the loans in accordance with the terms and conditions of loans from the Trust, which are laid down in paragraph 4 of the Instrument to Establish the Trust Fund, adopted by Decision No. 5069-(76/72), May 5, 1976 (Selected Decisions, Tenth Issue, page 303). One of the terms is that interest shall be charged at the rate of one-half of one per cent per annum on the outstanding balance of a loan. Interest must be paid semi-annually. The Trust Instrument does not contain any other provision dealing with interest on loans. By a decision adopted in 1979 the Fund stipulated that interest on loans would be paid in U.S. dollars (Decision No. 6358-(79/188)TR, December 19, 1979 (Selected Decisions, Tenth Issue, page 317). Regarding the repayment of loans, the terms prescribe that each disbursement must be repaid in ten equal installments, beginning not later than the end of the first six months of the sixth year, to be completed at the end of the tenth year, after the date of disbursement. 1/

B. Other Principles

1. The Fund, as any other international organization, has those powers that, though not expressly stated in its charter, are necessary or appropriate for the performance of its functions as an international agency and incidental to the exercise of expressly granted powers. International law has recognized that among these implied powers is the power of the organization to recover damages caused by the failure of another party to fulfill its obligations to the organization.2/ An organization may rely on the same implied power to

1/ The final disbursement equal to about 0.4 percent of quota must be repaid not later than the end of the tenth year from the date of disbursement in one amount equal to the amount of that disbursement (Decision No. 6793(81/45), March 25, 1981, Selected Decisions, Tenth Issue, page 320).

2/ See, for example, Preparations for Injuries Suffered in the Service of the United Nations, 1949, ICJ Report p. 174 at p. 180:

"It cannot be doubted that the Organization has the capacity to bring an international claim against one of its Members which has caused injury to it by a breach of its international obligations towards it. The damage, specified in Question I(a) means exclusively damage caused to the interests of the Organization itself and to its administrative machine, to its property and assets and to the interests of which it is the guardian. It is clear that the Organization has the capacity to bring a claim for this damage. As the claim is based on the breach of an international obligation on the part of the Member held responsible by the Organization, the Member cannot contend that this obligation is covered by municipal law, and the Organization is justified in giving its claim the character of an international claim."

devise its own administrative rules that are designed to avoid or limit damages to the organization that might be caused by the failure of a member to fulfill an obligation to the organization.

2. The doctrine of implied powers served as the basis for the first program of investment of the Fund's gold. The doctrine was explained in the paper entitled, "Investment of Gold in U.S. Securities" 1/ as follows:

"Such implied powers have been recognized where they were:

- (i) incidental to the exercise of expressly granted powers;
- (ii) necessary or appropriate for the performance of the functions of the international agency; and
- (iii) not in conflict, directly or indirectly, with the provisions of the treaty establishing the agency."

There is no reason to suppose that the Fund was intended to be an exception to the generally recognized practice in that it was to have no implied powers. On the contrary, there is positive evidence in Article XII, Section 2(g) of the recognition by the drafters that the Fund would have such implied powers as were necessary or appropriate to conduct the business of the Fund:

'Article XII, Section 2(g) - The Board of Governors, and the Executive Directors to the extent authorized, may adopt such rules and regulations as may be necessary or appropriate to conduct the business of the Fund'."

That paper, examining the question of whether the power to invest was incidental to the exercise of an express power and whether it was necessary or appropriate for the Fund's functions, continued:

"The Fund has assets which have been transferred to its ownership for certain specified purposes of international importance. Its assets must be wisely administered and protected so

1/ Committee on Investment of Fund Assets, Document No. 1, May 3, 1951. This document was also the basis for the further consideration of the subject in 1955, which led to Decision No. 488-(56/5), adopted January 25, 1956, that authorized the sale of a portion of the Fund's gold for the purpose of the investment of the proceeds to raise income towards meeting an existing deficit. See SM/55/30 and Correction, May 10, 1955. Additional material on the doctrine of implied powers in international law may be found in Attachment II to this Memorandum.

that they can be fully available for the purposes for which the Fund was established. Safeguarding these assets against an impairment of them which would reduce their availability must thus be regarded as incidental to the purposes of the Fund and necessary or appropriate for the achievement of them. To conclude otherwise would be tantamount to holding that the Fund has no power to husband its resources in accordance with the dictates of prudent management."

4. The Fund thus has the power, as provided in Article XII, Section 2(g), and by necessary implication, to make the incidental arrangements which it considers necessary or appropriate to avert financial losses that might arise from the failure of members to fulfill their financial obligations in accordance with the Articles and the Rules, provided there is no conflict between the arrangements proposed and any provision of the Articles. The principle of implied powers cannot be used, however, as the legal basis for actions that serve purposes other than the recovery of financial damages.

III. Methods to Deal With Financial Consequences of Overdue Payments in the General Department

As mentioned in the Introduction above, certain financial consequences follow for the Fund when payments for repurchases or charges in the General Department are not made on time. The legal aspects of certain actions by which these financial consequences could be prevented or reversed are examined in subsections A and B below.

A. Overdue Repurchases of Holdings and Overdue Charges on Holdings the Repurchase of Which is Overdue

1. When a member is not meeting an obligation to repurchase balances of the Fund's holdings of its currency, 1/ the Fund has the authority under Article V, Section 8(c), after consultation with that member on the reduction of the Fund's holdings of its currency, to impose "such charges as the Fund deems appropriate" on the holdings of that member's currency that should have been repurchased. The Articles do not specify any criteria for the determination of an appropriate rate. As mentioned above, the rate or rates of charge decided upon under Section 8(c) do not have to meet the requirement of uniformity for all members. The Fund could determine the rate in light of the circumstances of the particular member and its relations with the Fund. Thus, a rate found to be appropriate by the Fund in the circumstances could be higher than the ordinary rate, but the Fund would not, as a legal matter, be precluded from deciding that a lower

1/ I.e., when a repurchase obligation is not discharged in accordance with the applicable provisions and decisions of the Fund.

rate would be appropriate in the circumstances. In determining a rate the Fund would be guided by the specific purpose of Section 8(c), which is to create conditions in which the overdue repurchase is more likely to take place, and by its purposes set forth in Article I.

2. Instead of acting with respect to an individual member, it would also be possible for the Fund to prescribe, by a generally applicable decision, special rates of charge that would apply to the balances of any member's currency that should have, but had not been, repurchased. A decision of the Executive Board setting the rate in an individual case would then not be necessary. The application of an increased rate to the Fund's holdings of an individual member's currency that should have been repurchased would be based on Section 8(c) and require prior consultation with the member on the reduction of the holdings the repurchase of which is overdue. It would be possible to institute procedures that would allow consultation to take place in a timely manner so that the increased rate of charge could be applied as of the date on which the obligation became overdue.

3. In determining the rates of charge to be levied on holdings that should have been repurchased, whether in individual cases or by a generally applicable decision, the Fund would be able to take into account the effect of the failure of a member to pay charges or discharge repurchase obligations on the Fund's financial position. The rate could be set at a level that would compensate for the costs resulting from the non-payment. The loss resulting from charges being overdue on a balance after the due date for its repurchase, as well as the costs resulting from charges being overdue prior to that default, would be considerations that the Fund would be able to take into account in deciding an appropriate rate of charge.

Seventy percent of the total voting power would be required for the adoption of a decision setting the rate either in respect of an individual member or generally.

B. Overdue Charges in the Absence of Overdue Repurchases

When the member that fails to pay charges on time is not also overdue in respect of a repurchase obligation, it is not possible for the Fund to employ the methods discussed in A above. Three other techniques are examined below: to increase the rate of charge on the Fund's holdings of currency on which charges are overdue; to permit the member to pay the overdue charges in its own currency, which would then be subject to charges; and to require the member to indemnify the Fund for the loss resulting from its failure to pay the charges on time.

1. Increase in the Rate of Charge on Fund Holdings of
Currency in Respect of Which Charges are Overdue

a. Before discussing this approach, it is useful at the outset to mention that the Articles do not authorize the Fund to levy periodic charges otherwise than on holdings of currency. Consequently, the Fund cannot impose charges on overdue charges.

b. The actions described in Section A above could not be taken by the Fund in the case of a member that had overdue charges but was current in its repurchase obligations. There is, however, another technique that could be used, even in cases that would not involve overdue repurchases. This technique would be to amend the current schedules of periodic charges to provide for the application of a higher rate on the holdings in respect of which charges were overdue. The higher charges could be set at a rate that would enable the Fund to offset the costs incurred because of the overdue charges. Other factors could be taken into account as well, provided they are relevant to the purposes of the Fund and its proper functioning under the Articles.

c. An amended schedule providing for this approach would be adopted under Article V, Section 8(b). Any rates of charge established under that provision must be uniform for all members. The requirement of uniformity has been understood by the Fund to permit the establishment of different rates of charge, provided that the differentiation was related to differences in use of the Fund's resources, and that the distinctions were reasonable, were not arbitrary or capricious, and were consistent with the purposes of the Fund. ^{1/} Use of the Fund's resources by a member which is not making timely payments of charges is a form of use that could reasonably be considered to constitute a basis for the establishment of a different rate of charge. It would not be inconsistent with the requirement of uniformity, therefore, to levy a higher rate of charge on the balances in respect of which charges are overdue. The higher rate would have to be uniform for all members, applying to all balances in the same category.

d. Higher charges could apply only while the relevant balances of currency remained outstanding. Under Article V, Section 7(a) ^{2/}, members have the unqualified right to repurchase at any time

^{1/} See SM/74/47 entitled "Uniformity in Relation to Charges", February 21, 1974).

^{2/} See Attachment I.

the Fund's balances of their currency subject to charges. It is possible even if not likely as a practical matter, that a member would repurchase the balances with respect to which charges were overdue and that would be subject, therefore, to the higher charge, and not pay the amount of the overdue charges. In that case, this technique would not enable the Fund to recover the loss resulting from the overdue charges.

e. Because of this possibility, it should be explored whether the Fund could adopt a rule of attribution that would ensure that the overdue charges would be paid before the holdings which were subject to charges could be repurchased. Would it be possible, for instance, to introduce a requirement that payments presented in discharge of a repurchase obligation, or in discharge of charges that were due but not overdue, be applied pro tanto to the overdue charges, leaving the other obligations outstanding? It seems that such a requirement would raise certain legal and practical difficulties. It would seem to be inconsistent with the unlimited right of members to repurchase the Fund's holdings of their currency on which charges are levied. There would be a further legal difficulty stemming from the fact that this attribution technique would cause members intending to discharge a particular obligation to default on that obligation and, if the repurchase of the balances in question were overdue, to prolong the violation of that obligation. In addition, while members are free to use SDRs in repurchase without limitation, currencies may be used only as determined by the Fund on the basis of the operational budget in effect at the time. Therefore, payments presented in discharge of a repurchase obligation could not in all cases be applied to overdue charges, which are payable in SDRs. Even if under Article V, Section 8(e) a member were permitted to pay overdue charges in its own currency (see below), there would be no certainty that at any given time the currencies acceptable in a repurchase could also be specified by the Fund for use in payment of charges. For these reasons, attribution rules could not prevent the repurchase of balances on which increased charges were being levied.

2. Payment of Overdue Charges in Member's Own Currency

a. The Fund may, under Article V, Section 8(e), permit a member to pay charges in its own currency "in exceptional circumstances". The Articles do not provide a definition of the concept of "exceptional circumstances" or prescribe any criteria that must or may be used to qualify circumstances as exceptional. The criterion for the existence of exceptional circumstances does not necessarily have to be the same as that determining the existence of an "exceptional" hardship that allows the Fund to extend repurchase periods under Article V,

Section 7(g). 1/ Exceptional circumstances, for the purpose of Section 8(e), must encompass, for instance, nonparticipation in the SDR Department. 2/ The matter is left to the judgment of the Fund, to be exercised in the light of the purpose of the provision and the principles governing all exercise of authority by the Fund. Whether the member had a reserve tranche position and whether the payment of charges in its own currency would eliminate or reduce a remunerated position would be factors that the Fund could take into account. Section 8(e) does not, and was not intended to, provide a solution for the problem of the Fund's lack of authority to impose charges on overdue charges, and the provision could not serve as a basis for a generally applicable system designed to achieve that purpose. The fact that a member is in default would not by itself preclude the Fund from exercising its authority under the provision if it finds that there are exceptional circumstances within the meaning of the provision. In those cases in which the Fund decided to permit members to pay overdue charges in their own currency, the resulting balances would be subject to charges and repurchase, provided they caused the Fund's holdings of the currency, after exclusion of balances resulting from excluded purchases, to be above quota.

b. The Articles do not prescribe a period for the repurchase of holdings not acquired as a result of purchases but require the Fund to adopt policies on repurchase under Article V, Section 7(e), which provides:

"A member shall repurchase, in accordance with policies that the Fund shall adopt by a seventy percent majority of the total voting power, the Fund's holdings of its currency that are not acquired as a result of purchases and are subject to charges under Section 8(b)(ii) of this Article."

If the Fund exercised its discretion under Article V, Section 8(e) to allow a member to pay charges in its own currency, it would be necessary to have in place at that time policies regarding the repurchase of such currency holdings.

c. The appropriate period for repurchase would have to be determined in light of the reason that motivated the permission to a member to pay charges in its own currency. If the permission was granted because of a lack of foreign assets, an obligation of immediate

1/ See Attachment I.

2/ See Commentary on the Proposed Amendment of the Articles of Agreement, Chapter F, paragraph 12. At the present time all members of the Fund are participants in the SDR Department.

repurchase would defeat the purpose which the decision to permit payment in its own currency was intended to serve. Subject to this consideration, the Fund could determine the period of repurchase in the light of the criteria that enter into determinations of repurchase periods generally. As the permission to pay charges in local currency constitutes in essence an extension of credit, an important consideration for the determination of the period of repurchase would be the temporary character of the Fund's resources, and the Fund would have to be assured that this principle would be observed. The repurchase period need not be the same for all types of holdings acquired otherwise than through purchases, but the policies adopted for a particular type of holding would have to apply in the same way to all members. A decision prescribing the period would have to be taken by seventy percent of the total voting power, even if the period fell between three and five years.

3. Any special charges introduced under Section 8(b) or (c) could only be applied prospectively as of the effective date of the Fund's decision with respect to obligations overdue at that time. The charges could not be applied retroactively in respect of periods prior to the effective date of the Fund's decision.

4. Obligation of Member to Make Good the Loss

1. Acting on the basis of powers derived from generally accepted principles of law (see II.B above on the doctrine of implied powers), the Fund could, in accordance with Article XII, Section 2(g), adopt rules and procedures under which a member would be called upon to make good the loss to the Fund occasioned by the member's failure to pay in accordance with Rule 1-2 the periodic charges owed by it. A member could thus have to pay not only the amount of the overdue charges, which it is required to do under express provisions of the Articles and the Rules, but also an amount equal to the loss sustained by the Fund because of the delay in payment of these charges. The amount of the loss would be calculated on the basis of criteria established by the Executive Board.

2. To require a member to indemnify the Fund for its financial loss would not, and indeed, could not, involve the application of a charge in the sense of Article V, Section 8. The Fund may levy charges only as specifically provided by Article V, Section 8. It has no other power, general or specific, to impose charges on members in relation to the holdings or the transactions and operations of the General Resources Account. The recovery, on the basis of general principles of law, of financial damages caused by a member's failure to carry out its financial obligations is independent of the power to levy charges. The power to recover damages is a limited power that can be implied only for this limited purpose, i.e., to

recover financial losses in a system that provides no assurance that the damages would be recoverable through other means, e.g., the levying of higher charges. As mentioned above, under Article V, Section 8(c) this could be assured only in respect of overdue repurchases and not in respect of overdue charges.

3. Recovery of financial damages may be effected in various ways. One way would be in the form of periodic payments similar to charges. However, as mentioned above, such payments would not be charges in the sense of the term as used in the Articles. A decision to seek recovery, and setting the measure of damages to the Fund resulting from the member's failure to pay on time, and establishing the procedures by which such damages are to be recovered, could be adopted by a majority of the votes cast.

4. The financial costs which the Fund incurs as a result of overdue financial obligations can encompass administrative costs. On the basis of the Fund's authority to recover financial costs, the Fund could require members that have overdue obligations to indemnify the Fund for these costs as well. While it would not be feasible to establish in each individual case the precise costs incurred because of a particular member's overdue payments, it would be possible to charge a member an amount representing a reasonable approximation of those costs.

IV. Overdue Payments Relating to the SDR Department

With regard to the SDR Department, the question of late payment can arise only in respect of net charges and assessments, as the system of mandatory reconstitution of SDR holdings, which might be regarded as being parallel to the repurchase system in the General Department, is no longer in effect.

1. The only charges the Fund can impose under the provisions relating to the SDR Department are those provided for in Article XX, Section 2. These charges must be at a rate equal to the rate of interest on SDR holdings. There is no provision dealing with overdue net charges in the SDR Department.

2. The question of recovery of losses to the SDR Department due to the non-payment of charges does not arise because there is no financial loss to the Fund when a participant does not pay charges to the SDR Department. In that event, the Fund creates SDRs to meet the interest due and the participant incurs an obligation to pay charges on the amount of the charges that have not been paid. The charges continue to accrue until the participant that has unpaid charges outstanding acquires SDRs. These are then applied against the unpaid charges and cancelled.

3. The non-payment of an assessment would involve a loss for the Fund in the General Department. There is no provision in the Articles dealing with the non-payment of an assessment. In particular, there is no provision, similar to the one dealing with unpaid charges, that would enable the Fund to apply SDRs acquired by the participant after the date for the payment of an assessment against the unpaid assessment, and transfer the amount to the General Department. The expenses of conducting the business of the SDR Department have been low, and the assessments made so far have been for very small amounts. Nevertheless, acting on the basis of generally accepted principles of law the Fund could, in accordance with Article XII, Section 2(g), supplement its procedures for the collection of assessments with the provision that a participant is liable to make good the loss to the Fund in the General Department occasioned by the non-payment of an assessment levied on it.

V. Overdue Repayment of Trust Fund Loans and Overdue Payment of Interest on Such Loans

When the repayment of a Trust Fund loan or the payment of interest on such a loan is overdue, financial losses result for the Fund. Action to deal with this situation could be based on the legal principles discussed hereunder.

1. The Instrument establishing the Trust Fund provides no basis for the imposition of special charges on overdue Trust Fund loans and on overdue interest on such loans. It would be possible, however, to pursue a course of action to enable the Fund, as Trustee, to recover the losses sustained by the Trust Fund. The case for such action would be based on general principles of law.

2. It is a fundamental principle of the law of trust that a trustee has a duty to the beneficiaries of the trust to use reasonable care and skill to preserve the trust property. The trustee is under an obligation to administer the trust for the benefit of all the beneficiaries, and he may not give more favorable treatment to one beneficiary to the detriment of the others. A trustee is authorized to exercise not only the powers that are expressly conferred upon him by the terms of the trust, but also such powers as are necessary or appropriate to carry out the purposes of the trust and are not forbidden by the terms of the trust.

3. As the assets of the Trust Fund are to be used for specified purposes, the Fund, as Trustee, has the duty to take appropriate and lawful steps to recover outstanding debts as they become due in order to ensure that the funds become available for the purposes specified in the Instrument. These considerations lead to the conclusion that action by the Fund as Trustee to recover losses on overdue repayments of Trust Fund loans and/or on overdue payments of

interest on such loans, whether or not they are themselves overdue, would be consonant with the Trustee's duty to enforce timely repayment of obligations owed to the Trust and to ensure that the Trust assets will be available to all eligible beneficiaries. The authority to take such action is neither provided in, nor expressly prohibited by, the Trust Instrument. It would therefore be based on the Trustee's implied powers. An amendment of the Trust Instrument would not be required. The existence of the authority to recover losses would not, of course, deprive the Trustee of the possibility in any given case, or in any class of cases, or in all cases, to find it appropriate and consistent with its duties in the light of the purposes of the Trust, not to take such action.

7. The adoption of a decision to require recipients of Trust Fund loans to make good losses resulting from overdue repayments and/or interest would require a majority of the votes cast. Adherence to the principle of uniformity for all participants would not be mandatory, and thus the Trustee would be able to establish different obligations on the basis of reasonable categories of cases. The losses to be made good would be measured on the basis of criteria adopted by the Executive Board.

VI. Summary and Conclusions

1. The Fund sustains financial losses as a result of the fact that repurchase obligations and charges in the General Department are sometimes not paid on time. In addition, the Fund as Trustee of the Trust Fund experiences financial losses due to the late repayments of certain loans from the Trust Fund and late payment of interest on loans by some recipients. In addition, charges and assessments in the SDR Department are sometimes not paid on time. While the non-payment of net SDR charges does not involve the Fund in any financial losses, unpaid assessments do give rise to a loss, albeit a small one, to the Fund. This memorandum concludes that there are courses of action, set forth below, that the Fund could follow to prevent or recover the losses mentioned above. The mere fact that these types of action are available in certain cases does not mean that the Fund would be obligated to resort to them in cases where it did not judge that course of action to be consistent with its general purposes.

2. In the General Department, when repurchases are not carried out in time, the Fund can take action in individual cases or by a general decision. When a member is not meeting an obligation to repurchase balances of the Fund's holdings of its currency, the Fund has the authority under Article V, Section 8(c) to impose such charges as it deems appropriate on its holdings of that member's currency that should have been repurchased. The rates imposed under that provision do not have to be uniform for all members. These rates could be determined in light of the circumstances of the particular member

and its relations with the Fund, and also of the Fund's losses resulting from the member's failure to repurchase on time. The rates applicable under that provision could be prescribed either by an ad hoc decision for a particular case or under a general decision prescribing special rates of charge applicable in all cases in which repurchases are overdue, provided that the required consultation has taken place. While charges established under this provision could be designed to enable the Fund to recover financial damages, they need not be limited to that purpose, but could take into account other factors and serve other relevant objectives, as discussed in EBS/85/121, as well.

3. When a member that is failing to meet a repurchase obligation is also overdue in respect of charges the Fund could, either in an individual case or by a generally applicable decision, take the effect of the non-payment of the charges on its financial position into account in determining the rate of charge to be imposed on the holdings that should have been repurchased.

4. The Articles do not authorize the Fund to levy periodic charges otherwise than on holdings of currency. Consequently, the Fund has no authority to impose charges on unpaid charges. When a member that fails to pay charges is not overdue in respect of a repurchase it is not possible for the Fund to employ the methods mentioned above. Three techniques to deal with such cases are discussed: (i) to increase the rate of charge on the Fund's currency holdings in respect of which charges are overdue; (ii) to permit the member to pay the overdue charges in its own currency, which would then be subject to charges; and (iii) to require the member to indemnify the Fund for the losses resulting from its failure to pay the charges on time.

5. With respect to (i), in order to increase the rate on holdings in respect of which charges are overdue the present schedule of charges would be amended to provide for the application of a higher rate on such balances. The rates of charge would have to be uniform for all members and consequently would have to be the same for all members having overdue charges. This technique, however, would not necessarily enable the Fund to recover losses resulting from overdue charges in all cases. The reason is that members have an unqualified right to repurchase at any time any of the Fund's balances of their currency subject to charges, and thus it would be possible for a member to repurchase the balances on which charges were levied without paying the amount of the overdue charges.

6. The Fund may permit a member to pay charges in its own currency "in exceptional circumstances". What would constitute exceptional circumstances is a matter left to the judgment of the Fund to be exercised in the light of the purpose of this authority and the

principles governing all exercise of authority by the Fund. While this provision could be applied in the case of an individual member if the member has exceptional circumstances, it was not intended to overcome the lack of authority on the part of the Fund to levy charges on overdue charges and could not serve as a basis for a generally applicable system designed to achieve that purpose. If a member paid overdue charges in its own currency, the resulting balances would be subject to charge if they caused the Fund's holdings of the currency, after exclusion of balances resulting from excluded purchases, to be above quota. The Fund would have to decide a period for the repurchase of such holdings as were subject to charge. The appropriate period would be determined in light of the criteria that enter into the determination of repurchase periods generally and the purpose of the authority to permit charges to be paid in members' own currencies.

7. On the basis of generally accepted principles of law the Fund could, in accordance with Article XII, Section 2(g), supplement the rules and procedures for the collection of charges with a provision rendering a member liable to make good the financial loss to the Fund occasioned by its failure to pay periodic charges on time. A decision establishing such a claim of the Fund against a member could be taken by the Executive Board by a majority of the votes cast.

8. While the non-payment of charges in the SDR Department does not cause a financial loss to the Fund, unpaid assessments do result in a loss, albeit a small one, to the Fund in the General Department. On the basis of generally accepted principles of law the Fund could, in accordance with Article XII, Section 2(g), require a participant to make good the loss.

9. With respect to overdue payments of Trust Fund loans and overdue payment of interest on such loans the Fund has the authority as Trustee to recover the losses sustained by the Trust Fund. The authority to take action would not be inconsistent with any specific provision in the Trust Instrument; it would be based on the principle of implied powers that the Fund could exercise. An amendment of the Trust Instrument would not be required.

Article V, Section 7(a)

A member shall be entitled to repurchase at any time the Fund's holdings of its currency that are subject to charges under Section 8(b) of this Article.

Article V, Section 7(e)

A member shall repurchase, in accordance with policies that the Fund shall adopt by a seventy percent majority of the total voting power, the Fund's holdings of its currency that are not acquired as a result of purchases and are subject to charges under Section 8(b)(ii) of this Article.

Article V, Section 7(g)

The Fund, on the request of a member, may postpone the date of discharge of a repurchase obligation, but not beyond the maximum period under (c) or (d) above or under policies adopted by the Fund under (e) above, unless the Fund determines, by a seventy percent majority of the total voting power, that a longer period for repurchase which is consistent with the temporary use of the general resources of the Fund is justified because discharge on the due date would result in exceptional hardship for the member.

Article V, Section 8(b)

The Fund shall levy charges on its average daily balances of a member's currency held in the General Resources Account to the extent that they

(i) have been acquired under a policy that has been the subject of an exclusion under Article XXX(c), or

(ii) exceed the amount of the member's quota after excluding any balances referred to in (i) above.

The rates of charge normally shall rise at intervals during the period in which balances are held.

Article V, Section 8(c)

If a member fails to make a repurchase required under Section 7 of this Article, the Fund, after consultation with the member on the reduction of the Fund's holdings of its currency, may impose such charges as the Fund deems appropriate on its holdings of the member's currency that should have been repurchased.

Article V, Section 8(d)

A seventy percent majority of the total voting power shall be required for the determination of the rates of charge under (a) and (b) above, which shall be uniform for all members, and under (c) above.

Article V, Section 8(e)

A member shall pay all charges in special drawing rights, provided that in exceptional circumstances the Fund may permit a member to pay charges in the currencies of other members specified by the Fund, after consultation with them, or in its own currency. The Fund's holdings of a member's currency shall not be increased as a result of payments by other members under this provision above the level at which they would be subject to charges under (b)(ii) above.

Article XX, Section 1 - Interest

Interest at the same rate for all holders shall be paid by the Fund to each holder on the amount of its holdings of special drawing rights. The Fund shall pay the amount due to each holder whether or not sufficient charges are received to meet the payment of interest.

Article XX, Section 2 - Charges

Charges at the same rate for all participants shall be paid to the Fund by each participant on the amount of its net cumulative allocation of special drawing rights plus any negative balance of the participant or unpaid charges.

Article XX, Section 3 - Rate of interest and charges

The Fund shall determine the rate of interest by a seventy percent majority of the total voting power. The rate of charges shall be equal to the rate of interest.

Article XX, Section 4 - Assessments

When it is decided under Article XVI, Section 2 that reimbursement shall be made, the Fund shall levy assessments for this purpose at the same rate for all participants on their net cumulative allocations.

Article XX, Section 5 - Payment of interest, charges, and assessments

Interest, charges, and assessments shall be paid in special drawing rights. A participant that needs special drawing rights to pay any charge or assessment shall be obligated and entitled to obtain them, for currency acceptable to the Fund, in a transaction with the Fund

conducted through the General Resources Account. If sufficient special drawing rights cannot be obtained in this way, the participant shall be obligated and entitled to obtain them with a freely usable currency from a participant which the Fund shall specify. Special drawing rights acquired by a participant after the date for payment shall be applied against its unpaid charges and cancelled.

Article XXX(c)

Reserve tranche purchase means a purchase by a member of special drawing rights or the currency of another member in exchange for its own currency which does not cause the Fund's holdings of the member's currency in the General Resources Account to exceed its quota, provided that for the purposes of this definition the Fund may exclude purchases and holdings under:

(i) policies on the use of its general resources for compensatory financing of export fluctuations;

(ii) policies on the use of its general resources in connection with the financing of contributions to international buffer stocks of primary products; and

(iii) other policies on the use of its general resources in respect of which the Fund decides, by an eighty-five percent majority of the total voting power, that an exclusion shall be made.

The Doctrine of Implied Powers

1. The PCIJ developed its doctrine on the implication of powers through a series of advisory opinions that concerned the competence of the International Labor Organization (ILO). 1/

In its Advisory Opinion No. 13 of July 23, 1926, the PCIJ stated:

"It results from the consideration of the provisions of the Treaty that the High Contracting Parties clearly intended to give to the International Labor Organization a very broad power of co-operating with them in respect of measures to be taken in order to assure humane conditions of labour and the protection of workers. It is not conceivable that they intended to prevent the organization from drawing up and proposing measures essential to the accomplishment of that end. (...). If such a limitation of the powers of the International Labour Organization, clearly inconsistent with the aim and the scope of Part XIII, had been intended, it would have been expressed in the Treaty itself." 2/

The same principles were applied in Advisory Opinion No. 59 of November 15, 1932 also dealing with the competence of the ILO, in which the Court noted that:

"...the Court is not disposed to regard the sphere of activity of the International Labour Organization as circumscribed so closely, in respect of persons with which it was to concern itself, as to raise any presumption that a labour convention must be interpreted as being restricted in its operation to manual workers, unless a contrary intention appears. (...) An examination of the opinions referred to above [Nos. 2, 3 and 13] is sufficient to show that the limits of the sphere of the International Labour Organization are not fixed with precision or rigidity in Part XIII..." 3/

1/ Advisory Opinions Nos. 2 and 3 (PCIJ, Series B, Nos. 2-3) and No. 13 (PCIJ, Series B, No. 13). These and other advisory opinions of the PCIJ, as well as decisions of other tribunals, were examined by Mr. Nicoletopoulos in a position paper of November 21, 1949 (Legal Department Paper No. 31, p. 10 et seq.). See also Gordon "The World Court and the Interpretation of Constitutive Treaties" 59 AJIL, (1965), pp. 794, 816-817.

2/ Series B, No. 13, at p. 18.

3/ Series A/B, No. 50, p. 374-5.

2. The ICJ has applied the principle of implied powers in many instances dealing with the United Nations. In the Reparations for Injuries case of April 11, 1949, the Court followed the caselaw of the PCIJ (to which it referred explicitly) but put more emphasis on the need for implied powers if the organization was to be enabled to perform its functions than it did on the intention of the members that established the organization:

"The Charter does not expressly confer upon the Organization the capacity to include, in its claim for reparation, damage caused to the victim or to persons entitled through him. The Court must therefore begin by enquiring whether the provisions of the Charter concerning the functions of the organization, and the part played by its agents in the performance of those functions, imply for the organization power to afford its agents the limited protection...of a claim on their behalf....
Under international law the organization must be deemed to have those powers which, though not expressly provided in the charter, are conferred upon it by necessary implication as being essential to the performance of its duties." 1/ (emphasis added)

The ICJ thereby established the principle of effectiveness as the primary principle of interpretation of implied powers, 2/ in that the Court stands ready to interpret the constitutive charter of an organization flexibly if this is necessary in order that the purposes of the treaty and the functions of the organization can be effectively carried out.

Thus in the Reparations case, the Court stated that:

"Whereas a state possesses the totality of international rights and duties recognized by international law, the rights and duties of an entity such as the [United Nations] Organization must depend upon its purposes and functions as specified or implied in its constituent documents and developed in practice." 3/

In the Effect of Awards case, the Court decided that the General Assembly could validly establish an administrative tribunal

1/ ICJ Reports (1949), p. 182.

2/ Gordon, op. cit., p. 820; Greig, International Law (1976), p. 487.

3/ ICJ Reports (1949), p. 180.

in spite of Article 22 of the Charter that only enabled it to establish subsidiary organs that it deemed necessary to the performance of its own functions (and it was clear that the General Assembly had no judicial functions of the type that the Administrative Tribunal would carry out). In doing so, the Court again referred to the purposes of the Charter and the efficient performance of the Organization's functions:

"It would, in the opinion of the Court, hardly be consistent with the expressed aim of the Charter to promote freedom and justice for individuals and with the constant preoccupation of the United Nations Organization to promote this aim that it should afford no judicial or arbitral remedy to its own staff for the settlement of any disputes which may arise between it and them. In these circumstances, the Court finds that the power to establish a tribunal, to do justice as between the Organization and the staff members, was essential to ensure the efficient working of the Secretariat, and to give effect to the paramount consideration of securing the highest standards of efficiency, competence and integrity. Capacity to do this arises by necessary intendment of the Charter". 1/ (emphasis added)

3. The Court of Justice of the European Communities has applied the theory of implied powers in a number of cases, by giving effect to Article 235 of the EEC Treaty which provides the Community with implied powers. 2/ Article 235 reads as follows:

"If action by the Community should prove necessary to attain, in the course of the operation of the common market, one of the objectives of the community and this Treaty has not provided the necessary powers, the Council shall, acting unanimously on a proposal from the Commission and after consulting the Assembly, take the appropriate measures."

In the "Federation Charbonniere de Belgique v. Haute Autorite" of November 29, 1956, 3/ the CJCE formulated the "reasonable and useful" test in relation to implied powers:

1/ ICJ Reports (1954), 57.

2/ See on Article 235: Giardina, "The Rule of Law and Implied Powers in the European Communities" 1 Italian YIL (1975), 99; Schermers, International Institutional Law (1980), pp. 209-210.

3/ Case 8/55, [1954 to 1956] ECR, p. 299.

"The Court considers that without having recourse to a wide interpretation it is possible to apply a rule of interpretation generally accepted in both international and national law, according to which the rules laid down by an international treaty or a law presuppose the rules without which that treaty or law would have no meaning or could not be reasonably and usefully applied."

4. It does not seem that the expression of certain powers in the treaty should be construed as precluding the existence of further (implied) powers in the same field or with broadly similar purposes. 1/ Indeed, in the Effect of Awards case, already referred to above, the ICJ considered that Article 22 of the Charter which only granted the power to establish subsidiary organs was not exhaustive and did not prohibit the establishment of organs other than those covered by Article 22. A similar reasoning prevailed in the case of Application for Review of Judgement No. 158 of the United Nations Administrative Tribunal 2/, where the ICJ confirmed the legality of the creation of the Committee on Applications for Review of Administrative Tribunal Judgments, even though that Committee might have judicial or quasi-judicial responsibilities which would place it outside of the scope of Article 22. 3/

1/ Campbell, "The Limits of the Powers of International Organizations" in 32 *Internat. and Comp. Law Quart.* (1983), pp. 524-527.

2/ ICJ Reports (1973), p. 166.

3/ Campbell, *op. cit.*, p. 526.

