

SM/14/138
Supplement 2
Correction 1

June 30, 2014

To: Members of the Executive Board

From: The Secretary

Subject: **Bhutan—Staff Report for the 2014 Article IV Consultation—Informational Annex**

The attached corrections to SM/14/138, Sup. 2 (6/2/14) have been provided by the staff:

Evident Ambiguity

Page 4, after para. 1: add “Staff is in the process of assessing other measures imposed by the authorities with respect to their consistency with Bhutan’s obligations under Article VIII, Sections 2(a) and 3.”

Comment: This statement corrects a possible misinterpretation of the list of exchange restrictions presented in the Informational Annex as an exhaustive list. The list of exchange restrictions will be finalized and included in the final Aide Memoire of the Article VIII mission.

Factual Errors Affecting the Presentation of Staff’s Analysis or Views

Page 3, para. 2, line 9: for “personal travel” read “personal and business travel”

Comment: The statement implies that this particular exchange restriction refers only to access to rupees for personal travel. This statement is factually incorrect because the relevant law also includes an exchange restriction on access to rupees for business travel.

Page 3, footnote 3, after the second sentence add: “While such approval is granted based on documentary evidence, this is not specified in any RMA guidance. Thus, the limits create a “chilling effect” with respect to potential customers, since in the absence of any published guidance, they do not know that the limits are indicative.”

Comment: The statement implies that this particular exchange restriction arises from absolute limits on transfers for family remittances. This statement is factually incorrect because in practice the authorities approve all bona fide requests and thus, the exchange restriction arises from the “chilling effect” of the absence of any published guidance on such practice similarly to the exchange restrictions mentioned in footnotes 2, 4, 5, 7 and 8.

Page 3, footnote 4, line 1: for "Limits are imposed on the purchase of Indian rupee amounts for personal travels to India by residents (up to 10,000 Indian rupee per day and 50,000 Indian rupee per month)" read "Limits are imposed on the purchase of Indian rupee amounts for personal and business travels to India by residents (up to 10,000 Indian rupee per day and 50,000 Indian rupee per month for personal travel, while the access to pay for business travel daily expenses in Indian rupee is limited to the amount equal to the daily allowance imposed by the Ministry of Finance on government officials)"

Comment: The statement implies that this particular exchange restriction arises from absolute limits on transfers for family remittances. This statement is factually incorrect because in practice the authorities approve all bona fide requests and thus, the exchange restriction arises from the "chilling effect" of the absence of any published guidance on such practice similarly to the exchange restrictions mentioned in footnotes 2, 4, 5, 7 and 8.

Typographical Error

Page 4, line 2: for "(iv) banning the access to Indian rupee for unrelated current international transactions" read "(vi) banning the access to Indian rupee for unrelated current international transactions".

Questions may be referred to Ms. Jain-Chandra, APD (ext. 35881).

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Exchange System

Since its introduction in 1974, the ngultrum has been pegged to the Indian rupee at par. Bhutan continues to avail itself of transitional arrangements under Article XIV, Section 2, pursuant to which it maintains exchange restrictions in connection with: (i) the availability of foreign exchange for travel, except for medical travel abroad by Bhutanese citizens¹, invisibles², and private transfers³; (ii) foreign exchange balancing requirement on remittances of income in convertible currencies or other foreign currencies from FDI; and (iii) the availability of foreign exchange for importers who are not able to provide the identity of the seller.

Bhutan also maintains exchange restrictions subject to Fund approval under Article VIII, Section 2(a) in connection with: (i) the FX balancing requirements for imports of capital goods (for projects involving FDI) and primary raw materials (for certain industrial projects); (ii) banning residents who do not comply with the requirement to repatriate export proceeds from accessing foreign exchange for unrelated imports; (iii) requiring foreign direct investment businesses to pay for their establishment and operational expenses from their own convertible currency resources; (iv) requiring Bhutanese companies to pay the interest on and amortization of external loans from their own convertible currency resources; (v) restricting the availability of Indian rupee for making payments and transfers to India in the following current international transactions: personal and business travel and study-abroad living arrangement⁴, family⁵ and salary remittances⁶, advance

¹ For Bhutanese citizens, the annual private travel FX allowance is set at \$3,000 (plus \$1,000 per each credit or debit card), the annual FX allowance for living expenses and stipend for education-related travel are set at \$1,500 and \$900, respectively, and the daily FX allowance for business travel is limited to the amount imposed by the Ministry of Finance on government officials. The RMA may provide access to FX above the private and education-related travel limits on a case-by-case basis, but does not publish any guidance on it. For medical travel by Bhutanese citizens, the exchange restriction has been removed since FX is made available upon provision of supporting documents. Resident non-citizens, however, must use their own foreign currency sources for all types of travel.

² Resident non-citizens must use their own foreign currency sources for subscriptions, application and testing fees and professional membership fees. Resident Bhutanese citizens may access FX exceeding the limits (currently US\$300 without documentation and US\$3,000 upon providing documentary evidence) with RMA approval. While such approval is granted based on documentary evidence, this is not specified in any RMA guidance. Thus, the limits create a “chilling effect” with respect to potential customers, since in the absence of any published guidance, they do not know that the limits are indicative.

³ Restrictions are maintained on residents’ family remittances in convertible currency. Residents who are not Bhutanese citizens may transfer only 50 percent of their monthly salaries and the rest of the funds at the end of the employment. While such approval is granted based on documentary evidence, this is not specified in any RMA guidance. Thus, the limits create a “chilling effect” with respect to potential customers, since in the absence of any published guidance, they do not know that the limits are indicative. Nonresidents may remit their salary only after deduction of estimated living expenses.

⁴ Limits are imposed on the purchase of Indian rupee amounts for personal and business travels to India by residents (up to 10,000 Indian rupee per day and 50,000 Indian rupee per month for personal travel, while the access to pay for business travel daily expenses in Indian rupee is limited to the amount equal to the daily allowance imposed by the Ministry of Finance on government officials), and living expenses of citizen students studying in India (in forms of limits on maximum 20,000 Indian rupee stipend and 20,000 Indian rupee living allowances/incidental expenses per month). The RMA may provide access above these limits on case-by-case review, but does not publish any guidance on it. Thus, the limits create a “chilling effect” with respect to potential customers, since in the absence of any published guidance, they do not know that the limits are indicative.

payments for imports from India⁷ and to recruit Indian workers⁸, imports of certain construction materials and vehicles from India⁹; and ~~(vii)~~ banning the access to Indian rupee for unrelated current international transactions for those who contravene RMA 's 2012 guidelines on Indian rupee transactions.¹⁰

Staff is in the process of assessing other measures imposed by the authorities with respect to their consistency with Bhutan's obligations under Article VIII, Section 2(a) and 3.

Article IV Consultation

Bhutan is on a 24-month consultation cycle. The 2011 Article IV consultation was concluded by the Executive Board on May 27, 2011.

⁵ Limits are imposed on family remittances by Indian expatriates, who are Bhutanese residents, to pay for their children's certain education expenses in India (in forms of limits on maximum 20,000 Indian rupee stipend and 20,000 Indian rupee living allowances/incidental expenses per month). The RMA may provide access above these limits on case-by-case review, but does not publish any guidance on it. Thus, the limits create a "chilling effect" with respect to potential customers, since in the absence of any published guidance, they do not know that the limits are indicative. Workers in specified industries are allowed to make family remittances, but with respect to workers on private housing projects, the RMA's 2012 guidelines on Indian rupee transactions only allow access to Indian rupee for remittances by Indian expatriate workers on housing projects approved by March 8, 2012. There is no provision for family remittances by resident Bhutanese citizens to India.

⁶ Current regulations only allow residents in Bhutan to make limited salary remittances, and there is no provision for salary remittances in Indian rupee by nonresidents.

⁷ Importers making advance payments for imports in Indian rupee must submit evidence that the relevant goods entered Bhutan within 91 days. The RMA states that advance payments can be contracted for a longer period of time, but this is not reflected in any published guidelines or documents. Thus, the requirement creates a "chilling effect" with respect to potential customers, since in the absence of any published guidance, they do not know that the limit is indicative.

⁸ The RMA's 2012 guidelines on Indian rupee transactions limit amounts for making advance payments to recruit Indian expatriate workers (up to 8,000 or 1,000 Indian rupee, depending on the type of employers). Moreover, these 2012 guidelines only specify certain employers who can purchase Indian rupee for making such advance payments, although the RMA states that in practice other employers may purchase India rupee for such purposes as well. The specific provision of the 2012 guidelines create a "chilling effect", since in the absence of any published guidance, other employers do not know that they would be entitled to make advance payments. With respect to private housing projects, the guidelines allow access to Indian rupee for advance recruitment payments only to Indian expatriate workers on housing projects approved by March 8, 2012.

⁹ Pursuant to a circular issued by the RMA in 2012, no access to Indian rupee is allowed for the import of construction materials from India for housing projects approved after March 8, 2012, or for the import of vehicles from India. The RMA intends to remove these measures by July, 2014.

¹⁰ The RMA's 2012 guidelines on Indian rupee transactions impose an immediate ban to access Indian rupee for unrelated transactions by any person violating any provision of the guidelines. There are also some specific provisions in these guidelines that state, for example, that failure to submit medical expense documentation (with respect to both citizens and residents), or personal travel documentation (with respect to residents only) would deprive the relevant person from accessing Indian rupee in the future. The authorities have stated that they are willing to modify these penalties into fines, so as to remove the exchange restriction.