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DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
001. memo	The Secretary to Members of Executive Board re: Special Allocation of SDRs (Special Drawing Rights) - Illustrative Calculations (IMF Document) (7 pages)	04/01/97	P1/b(1) Unclass.
002. memo	Barry S. Newman (IMF) to David Lipton & Tim Geithner re: Capital Movement Amendment (2 pages)	07/01/97	P1/b(1) Unclass.
003. memo	Karin Lissakers & Barry Newman (IMF) to Tim Geithner re: Capital Movements Amendment (4 pages)	07/16/97	P1/b(1) Unclass.
004. speech	re: Concluding Remarks by Acting Chairman on Capital Movements at Executive Board Meeting (IMF document) (6 pages)	07/18/97	P1/b(1) Unclass.
005. memo	Karin Lissakers & Barry Newman (IMF) to Tim Geithner re: Capital Movements Amendment (4 pages)	07/16/97	P1/b(1) Unclass.
006. memo	Barry S. Newman to David Lipton & Tim Geithner re: Capital Movement Amendment (2 pages)	07/01/97	P1/b(1) Unclass.

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[History of the Department of the Treasury - Supplementary Documents] [32]

jp28

RESTRICTION CODES

Presidential Records Act - [44 U.S.C. 2204(a)]

P1 National Security Classified Information [(a)(1) of the PRA]
P2 Relating to the appointment to Federal office [(a)(2) of the PRA]
P3 Release would violate a Federal statute [(a)(3) of the PRA]
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1997-SE-002028

THE DEPUTY SECRETARY OF THE TREASURY
WASHINGTON

2/25/97

UNCLASSIFIED - SENSITIVE

MEMORANDUM FOR SECRETARY RUBIN

FROM: Lawrence Summers

SUBJECT: Authority to Negotiate an IMF Quota Increase

ACTION FORCING EVENT:

We need your approval of our proposed negotiating objectives for the IMF quota increase so that we can proceed with the negotiations. We need to be in a position to give Congress the rough outlines of an agreement, including the relevant numbers, before we get too late in the budget cycle. As discussed at our February 24 meeting, we will ensure that the White House is fully supportive of our strategy before making any commitments in the negotiations.

RECOMMENDATION:

That you authorize us to negotiate a quota increase along the following lines, subject to achieving sufficient progress on a set of broad policy reforms of the IMF.

- Overall increase no greater than 45 percent, or about SDR 65 billion, with an *ad hoc* component as large as possible without a decline in the U.S. voting share significantly below 17 percent.
  - o One possibility -- elaborated at Tab A -- would limit the decline in our voting share to 17.3 percent (from the current 17.8 percent). It would entail an increase in the U.S. quota of 39.8 percent, or SDR 10.6 billion (about $14.6 billion), while reducing our quota share from 18.4 percent to 17.7 percent.
- Policy reforms, outlined at TAB B, are directed at the following broad objectives:
  - o making the IMF a more effective engine for market-oriented reform, trade liberalization and growth;
  - o adapting to new challenges in the global capital market;
  - o strengthening surveillance through increased transparency and promotion of good governance; and

o ensuring efficient use of Fund resources.

__________ Agree __________ Disagree __________________ Let's Discuss

BACKGROUND/ANALYSIS:

As we have outlined before, we believe we have to support a quota increase now if the IMF is to be strong enough to effectively promote U.S. interests over the medium term. The main arguments in favor are the following:

- The world economy is a substantially larger and potentially more dangerous place than when the last quota increase was agreed in 1990.
- The changes in international capital markets have increased the level of risk in the world economy.
- Even under relatively optimistic assumptions about the incidence of future crises and potential growth in demand for IMF resources, its substantial existing cushion of resources is likely to fall significantly over the next several years, leaving it unable to effectively fight the financial equivalent of the "two and a half" war scenario, even when the NAB is in place.
  - o The NAB and GAB in principle provide a potential bridge to a deferred quota increase, but lack the certainty of quota resources.
- The extent of U.S. strategic and economic interests around the world give us a uniquely large stake in a strong IMF.
- The time required to complete and enact a quota increase can easily take two years from the completion of the negotiations.
- We could not continue to hold off the world without significant cost to our credibility and influence in the IMF, even if the financial picture permitted some delay.
- The combination of (a) the window of opportunity provided by the first year of the second term, (b) the possibility of a multi-year budget agreement, (c) the commitment of the Administration to address the UN and IFI arrears problem, and (d) our obligation to seek Congressional action on the NAB, all seem to argue in favor of a push now for a big package.

We believe we have a reasonable prospect of gaining agreement within the IMF on quota increase along the lines outlined above. The policy reforms include some which will be very difficult for many IMF members to accept. Pushing hard on these will give us the capacity to slow down the negotiations if Congressional prospects look completely dark in 1997 and we decide to delay a formal request for appropriation of budget authority.

ATTACHMENTS:	Tab A:	IMF Quota Increase: Parameters
	Tab B:	Proposed Policy Agenda for the IMF
	Tab C:	January 31 memorandum

Strategy for Negotiating a Quota Increase

Parameters of an acceptable increase

- Aim for a deal entailing an overall increase of 45 percent composed of

  - o an equiproportional increase of 35 percent, allocated to all members in proportion to current quotas;

  - o a selective increase of 5 percent of current total quotas, allocated to all members in proportion to their calculated quotas (utilizing "Method A"); and

  - o ad hoc increases totalling 5 percent of current total quotas, allocated to the 18 members whose quotas are most out of line with their position in the world economy (comprising Japan and Germany, 7 new NAB participants, and a selection of smaller, mainly developing countries).

  This mix is termed the 35/5/5 approach.

As we share in the selective increase, our quota would increase by 39.8 percent, or SDR 10.6 billion (about $14.6 billion). Our quota share would fall by 0.7 percentage points from 18.4 percent to 17.7 percent. However, because the impact of the basic votes is diluted as quotas are raised, our voting share would decline by 0.5 percentage points, from 17.8 percent to 17.3 percent.

To mitigate the decline in our voting share, we could propose that Japan, which accounts for over one third of an ad hoc increase, forego some or all of its increase. However, Japan would probably seek to reallocate some of its ad hoc share to other Asian countries rather than to forego the entire amount. In that event, we would probably want to propose a smaller ad hoc increase and agree to Japan's reallocating some of its share.

A 45 percent increase would total SDR 65 billion, of which approximately SDR 39 billion would constitute usable resources. On the basis of the IMF's present projections of demand for its resources, which could prove to be too high, the institution would not need another quota increase until around 2007.

- Our opening proposal, however, should be for a smaller overall increase, e.g., a 35 percent increase such as 30/0/5 or a 40 percent increase such as 30/5/5.[1]

The declines in our quota and voting shares would be about the same as under the 35/5/5 version. Again, we would need to consider whether to press Japan to forego some of its ad hoc increase in order to mitigate the decline in our voting share.

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[1] Details of the calculations for the 35/5/5 approach are attached, together with a summary table of the results of calculations of alternatives of 30/0/5 and 30/5/5.

A 35 percent increase would total SDR 50.6 billion of which approximately SDR 30 billion would be usable.

- In the event that the countries seeking ad hoc increases rejected the 35/5/5 approach as providing insufficient increases for them, we would need to consider whether to accede to a greater loss of voting share.

Doubling the ad hoc component to 10 percent would reduce the U.S. share to about 16.8 percent, i.e., on a 30/5/10 or 35/0/10 approach. A 35 percent increase in the U.S. quota would amount to SDR 9.3 billion, or about $12.8 billion.

To reduce the increase in our share below $10 billion equivalent would require a decline in U.S. voting share to below 16 percent.

- We would emphasize that the price of our concurrence to a quota increase will be adoption of policy reforms along the lines of what we are preparing for circulation to other G-7 Deputies.

Informing Congress

We would keep key staffers generally informed about our intentions and progress.

2/24/97 quota-st.rgy

PROPOSED POLICY AGENDA FOR THE IMF

The IMF has undertaken a number of important reforms over the past several years. This note outlines some additional proposals which we believe would further strengthen the IMF as we approach the next century. These proposals are broadly consistent with the direction in which the IMF has been moving in recent years. They are designed to adapt the institution to the new realities and challenges of the global economy and financial integration, while preserving the monetary character of the institution. We believe it is important to consider these changes in the context of the 11th Review of quotas.

The proposals identified here are grouped in four broad categories:

- Making the IMF a more effective engine for market-oriented reform, trade liberalization and growth.
- Adapting to new challenges in the global capital market.
- Strengthening surveillance through increased transparency and promotion of good governance.
- Ensuring efficient use of Fund resources.

1. Making the IMF a more effective engine of market-oriented reform, trade liberalization and growth.

There is now a general realization that sound monetary and fiscal policies alone will not ensure high, sustainable growth rates unless they are fully complemented by measures to improve the efficiency and flexibility of economies. Stabilization and structural reform are interdependent and mutually reinforcing, and both are necessary for a successful transformation in transition and developing economies. Yet, the historic focus of the IMF on the short-term imperatives of financial stabilization -- lowering inflation and reducing fiscal and external imbalances -- often leads to insufficient attention to structural reforms in program design. To the extent this leaves structural problems unaddressed, countries may face greater challenges in achieving sustainable growth rates, even after stabilization is accomplished.

The following steps would help address this problem:

- *Give greater weight to, and tighter timetables for, market-oriented structural reforms, particularly trade liberalization, in IMF conditionality.*
- *Forge tighter linkage between Fund and World Bank lending, including, for example, through cross conditionality, to provide more effective delivery of multilateral support for rapid structural reform.*

- *On a case-by-case basis, provide higher access to Fund resources for programs that deliver more far-reaching and ambitious structural reforms.*

- *Devote more attention to the quality as well as the quantity of fiscal consolidation, by giving higher priority to strengthening education and health, and to providing a safety net for those elements of society which might otherwise suffer disproportionately from the short run effects of adjustment, and thereby undermine the political consensus necessary to sustain reform.*

2. **Adapting to new challenges in the global capital market.**

The rapid integration of national financial systems and capital markets, the huge increase in the magnitude of private capital flows across borders and the changing composition of these flows that have accompanied innovation present new opportunities and challenges to the IMF in carrying out its central mission.

The following steps would help the IMF play a more effective role in promoting stability in the international financial system and in encouraging openness.

- *Design and implement an effective role for the IMF in strengthening national financial systems.*

- *Amend the Articles of Agreement to give the IMF a formal role in encouraging capital market liberalization.*

- *Encourage the IMF to help implement the G-10's recommendations on resolution of sovereign liquidity crises without undue reliance on official financing, including a review of the IMF's policy on conditional lending to countries that are in repayment arrears to private creditors.*

3. **Strengthening surveillance through increased transparency and promotion of good governance.**

The IMF's role in preventing financial crises could be enhanced by further augmenting surveillance and transparency policies, and by implementing the Interim Committee's endorsement, in its Declaration on a "Partnership for Sustainable Global Growth", of "(p)romoting good governance in all its aspects, including by ensuring the rule of law, improving the efficiency and accountability of the public sector, and tackling corruption, as essential elements of a framework within which economies can prosper."

The following measures could be considered.

- *Formulate and adopt a set of guidelines on best practices for governance, complemented by operational procedures for promoting the adoption of these guidelines by member governments.*

- *Adopt a more concrete and systematic focus on the quality of fiscal adjustment that more actively promotes cuts in unproductive expenditures, including military spending.*

- *Support this focus by emphasizing transparency in budgeting.*

- *Formulate guidelines for continued enhanced scrutiny of members which have received all scheduled disbursements but have not repaid all the outstanding credit ("post program monitoring").*

- *Ensure that the development of a general data standard now underway does not detract from continued emphasis on broadening adherence to the SDDS.*

- *Publish the IMF's analyses of and its advice to members on their economic policies and performance except when non-disclosure is explicitly approved, on the basis of guidelines formulated in advance. Initiate an outreach program to non-governmental organizations.*

4. **Ensuring efficient use of Fund resources**

To be credible in its promotion of enhanced transparency and improved governance in member countries, the IMF should increase the transparency of its own operations and financing, and adopt economies in administrative expenses.

The following policies should be considered.

- *Adopt a surcharge on exceptional financing in order to provide an incentive for early repayment and underline the revolving character of IMF resources.*

- *Base charges on a medium-term interest rate in order to increase the incentive for early repayment and provide a differential over the cost of funds that would better enable the IMF to finance the accumulation of adequate reserves.*

- *Allocate administrative expenses among members in proportion to quota rather than financing them from a conglomeration of fees, service charges and interest-free resources. In addition to increasing transparency, such an approach could provide stronger incentives to restrain expenses.*

- *Hold administrative expenses to zero real growth. Consolidate staff, management and Executive Board salary reviews under common parameters and guidelines, and on the same schedule.*

Draft: 2/20/97 newagend.imf

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

Listserv

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January 31, 1997

MEMORANDUM FOR SECRETARY RUBIN

FROM: Timothy F. Geithner TG
Deputy Assistant Secretary (International Monetary & Financial Policy)

SUBJECT: IMF Quota Increase

You asked for a summary of the case for the IMF quota increase. The main arguments in favor are the following:

- The world economy is a substantially larger and potentially more dangerous place than when the last quota increase was agreed in 1990. Yet, the resources the IMF has available to finance adjustment and reform have declined significantly relative to growth in the world economy, world trade, and international capital flows. If they continue to shrink relative to the size of the world economy and financial flows, the IMF risks becoming marginalized to the point that it could no longer effectively support or influence members' policies, or serve as a credible international lender of last resort.

    o In 1990, quotas were equal to 1.2 percent of world GDP. By 1995 they were 0.8 percent, and by 2002 will be around 0.5 percent. As a percent of global current account payments, quotas were 6 2 percent in 1990 and 3.7 percent in 1995, and are projected to decline to 2 3 percent in 2002.

- The changes in the international capital markets have increased the level of risk in the world economy. Countries are able to finance larger balance of payments deficits for longer periods of time, thus increasing the risk that, if things go badly, a much more substantial amount of external financing relative to the country's current account could be needed to address the problem Daily financial flows on the order of $1.5 trillion greatly exceed the IMF's lending capacity

- Even under relatively optimistic assumptions about the incidence of future crises and potential growth in demand for IMF resources, its substantial existing cushion of resources is likely to fall significantly over the next several years. Under some circumstances, a lack of useable resources could also raise questions about the liquidity of our reserve position in the IMF, including any claims arising from activation of the NAB (and therefore undermine one of the foundations for the existing no-outlay budgetary treatment).

- Without a quota increase at some time in the next couple years, the IMF could be left without sufficient resources to effectively fight the financial equivalent of the Pentagon's two and a half or three war scenario -- a series of major financial crises in a number of large emerging market economies -- even when the NAB is in place.

- The extent of U.S. strategic and economic interests around the world give us a uniquely large stake in a strong IMF.

  - o A world in which the IMF was too weak to act in countries with an external financing problem would force us to provide a greater share of resources bilaterally or expose us to the damaging economic consequences -- lost output and employment, currency depreciation -- and the associated political consequences.

  - o The IMF often tends to be more responsive to our policy priorities than our European allies (who might, for instance, have blocked activation of the GAB to finance a program for Mexico, had the IMF lacked resources).

  - o Without adequate resources, the IMF will be less able to promote the market oriented reforms, trade liberalization, and growth-oriented policies that have played such an important role in growth in the emerging markets and transition economies.

- There is no real alternative to a quota increase at this time to provide the resources the IMF will need over the next several years The NAB and GAB in principle provide a potential bridge to a deferred quota increase, but lack the certainty of quota resources.

  - o There is strong opposition to allowing the Fund to borrow from the private capital markets. Even if that opposition could be overcome and the other complications resolved, the IMF is unlikely to be able to raise a sufficient amount of money in a short enough period of time to substitute for an increase in quotas.

- The time required to complete and enact a quota increase can easily take as long as two years from the completion of the negotiations (the previous increase was agreed in 1990 but didn't take effect until 1992) It is thus important to begin the process several years ahead of the point when resources might fall to uncomfortably low levels

- We have held the world off for almost two years and do not believe we could continue to do so indefinitely without significant cost to our credibility and influence in the organization, even if the financial picture permitted some delay.

- The combination of the window of opportunity provided by the first year of the second term, a possible multi-year budget agreement, the commitment of the Administration to address the UN and IFI arrears problem, our obligation to seek Congressional action on the NAB, all seem to argue in favor of a big push now for a big package.

While these are sound and, we believe, compelling arguments, you should be aware of the arguments likely to be used by opponents of an increase:

- Just as past Secretaries of Defense have sometimes found it hard to win support for substantial increases in defense spending on the basis of scary but remote two-and-a-half war scenarios, in the current environment of relative peace and prosperity the IMF's scenarios aren't as compelling as they might be if specific threats could be cited.

    However, citing such threats would risk their becoming a self-fulfilling prophecy.

- The huge increase in the availability of private capital to developing countries and the stronger financial position of many emerging market countries -- and the example of developed countries' "graduation" from the IMF -- suggest to many that the need for IMF financing has receded, not increased

- On the basis of its own forecasts of the pace of likely normal lending, the IMF's existing cushion of resources is substantial (roughly $70 billion).

    However, there is no actuarially sound basis for forecasting the probability of shocks on the scale of Mexico. Moreover, many members' reserve positions are held by central banks which insist on assurance of liquidity of these claims, which they derive from the cushion (akin to our own justification for treatment of our claims as an exchange of assets rather than an expenditure/outlay).

- Many argue, even some within the IMF, that the bulge in demand for Fund resources due to the huge increase in IMF membership in the early 1990's has passed and that the future demand may actually decline gradually

- Without a major crisis or strategic imperative, like Russia in the early 1990s, the case for any vote on the IMF is tough to sell

- While many may buy the case for the NAB, a quota increase and the NAB together are hard to swallow, particularly because the arguments for the quota increase overlap with many of the arguments for the NAB

- There is a bit of tension in arguing that IMF programs work and get countries back on their feet and that the IMF should keep getting more and more money. If adjustment programs on the scale the IMF has conducted were really successful on an enduring basis, some argue, then the institution should need less money over time, not more.

Attached is the recommendation we sent you in early December on our negotiating objectives and strategy, including some tables and charts on the financial case.

cc. Assistant Secretary Lipton

ATTACHMENT: December 2 memorandum from D/S Summers

Final - Lister

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

12/2/96

UNDER SECRETARY

MEMORANDUM FOR SECRETARY RUBIN

FROM: Lawrence Summers
Deputy Secretary

SUBJECT: IMF Quota Increase

We have recently undertaken a careful review of the case for an IMF quota increase. This note outlines the conclusions of our review.

- We believe we should now enter into serious negotiations on the next IMF quota increase with the objective of reaching agreement by April 1997.

- We should be prepared to support an increase of about 50 percent. A 50 percent increase, which is one half the Managing Director's favored proposal (and below what we believe is his 60 percent minimum), would restore the IMF's financial capacity relative to world output, trade, and current account imbalances to the level that prevailed at the time the last quota review was completed. A 50 percent increase also would provide a reasonable cushion to meet projected demand for IMF resources over the next five to seven years.

  A 50 percent quota increase would increase IMF quotas by $105 billion, from $209 billion to $314 billion.

  The exact size of the increase in the U.S. quota won't be known until agreement is reached on apportionment of the entire quota increase between equiproportional (general flat rate) and selective or ad hoc (targeted adjustments for certain countries) components. However, assuming a 50 percent increase in total quotas and a minimum 18 percent U.S. share of the total (a 25bp drop from the current share size), the U.S. quota would rise by roughly $18.2 billion, from $38.4 billion to about $56.6 billion. (These are the dollar equivalent estimates of the SDR totals at the current $/SDR exchange rate.)

- The increase would combine a general equiproportional increase with a small selective or ad hoc increase to adjust relative quotas for a number of countries whose current quotas are seriously out of line with their relative size in the world economy. We should seek to limit the size of the selective or ad hoc element to the minimum necessary so that we mitigate the resulting erosion in our voting share.

  Our current quota of 18.25 percent now conveys 17.78 percent in voting power, which is a comfortable, but not large margin over the critical 15 percent threshold required to block quota increases, changes to the IMF Articles, and certain other key votes (e.g., gold sales).

- As a condition for agreeing to an increase, we should seek agreement by the members of the IMF to a series of policy and financial reforms, designed to make it possible for the IMF to:

  - provide larger financing programs for countries that commit to strong policies and reforms;

  - make IMF programs more supportive of sustainable growth, fiscal transparency, good governance, trade liberalization and other market-oriented policies; and to impose stronger conditions on military expenditures;

  - make the institution more transparent and accountable; and

  - ensure that the financial costs of the institution are more transparent and equitably shared. *(A separate note outlining our policy conditions is being prepared.)*

- We should make the case for an agreement along these lines to key members of Congress and staff over the next few weeks. Subject to further consultation with the White House, our current views on the sequencing of how we approach the Congress for the necessary authorization and appropriation are as follows:

  - Include a general marker in the President's initial FY1998 budget, stating that we are in the process of negotiations on an IMF quota increase without specifying numbers. This allows us to preserve the possibility of seeking Congressional authoritization in FY 1998 without committing us to do so.

  - Seek to include an "adjustment" for a quota increase in the discretionary spending caps on budget authority in the budget resolutions and the budget statute amendments in the spring of 1997.

  - Defer a decision on whether to submit a formal request in FY1998 (as an amendment to the President's budget request) until we see how the negotiations in the IMF and our Congressional consultations are proceeding.

In addition to whatever we decide to do on a quota increase, we are committed to seeking Congressional approval for us to participate in the New Arrangements to Borrow (authorization and appropriation for roughly $3.8 billion). We have also committed in principle to reach agreement by April 1997 to amend the IMF Articles of Agreement to provide for a special allocation of SDRs. We have not yet begun serious negotiations on the size of the allocation, but believe we can hold the increase to SDR 20 billion. This will require Congressional authorization for the United States to agree to the change in the Articles, but not any budget action or appropriation.

We would like to meet with you soon to discuss these issues and to outline in more detail the considerations involved in designing our legislative strategy.

BACKGROUND:

Current State of Play

Other Members of the IMF have been prepared for about a year to agree to a substantial quota increase. We have blocked agreement and forced a delay in the beginning of serious negotiations because we had other priorities, including the NAB, that we thought would be undermined by an early conclusion of the quota negotiations, and because we believed the IMF had sufficient resources to withstand a modest delay. We are now at the point where we will not be able to delay agreement any longer without serious potential costs to our credibility in the institution and potential practical damage to our agenda for the institution, potentially including a delay in other countries' willingness to ratify the NAB.

The Managing Director proposed a 100 percent increase in January 1996, with a minimum acceptable increase of about 70 percent. We believe his bottom line at this time is probably close to 60 percent. The rest of the membership of the IMF appears willing to accept an increase in the range of 50 to 80 percent. Few countries, if any, are now opposed to an increase. The G-7 publicly support going ahead in April with a decision to increase quotas, although privately some view the case for a large, early increase as weak. (The U.K. at one point argued for an increase of only about 25 percent.)

The support for a quota increase among the IMF membership reflects several factors.

- IMF Members generally accept the IMF's case that the Fund needs an increase in resources relatively soon if it is to be able to meet expected demand through 2002 and to be adequately prepared for an unanticipated crisis.

- IMF Members regard the NAB as a supplemental credit line that should be reserved only for the remote contingency of a severe financial crisis. They believe that the IMF should have adequate resources on its own to respond to the new potential demand of the current global financial system.

- Related to this, IMF Members generally want the IMF to remain a quota-based institution, with the Fund resources supplied through members' quotas and voting shares keyed to quotas.

- Many IMF Members want an increase in their relative quota shares to reflect the increase in their relative importance in the world economy. This is more easily accommodated as part of a general increase that expands the pie, rather than through what is called an "ad hoc" increase.

- It is relatively easy for most countries to agree to an IMF quota increase. Few face a formal parliamentary approval process and, for those that do, the issue is not entangled in budget negotiations as it is in the United States.

Budgetary Treatment of IMF Quota Transactions

Since 1980, it has been established that an increase in the U.S. quota in the IMF requires authorization and appropriation of budget authority even though any amount appropriated for this purpose will not be scored as an increase in the deficit or as a budget outlay. No budget outlay occurs when the Treasury transfers dollars to the IMF because the United States receives in exchange another monetary asset in the form of a liquid, interest-bearing claim on the IMF (which is backed by the IMF's strong financial position, including its significant holdings of gold). Congress has accepted this approach since 1968. The Senate Foreign Relations has described the treatment of transactions with the IMF as follows:

> *A budget expenditure occurs only as cash is actually transferred to the IMF, either through the 25 percent reserve asset payment, or through drawdowns of the letters of credit or borrowing arrangements. However, simultaneously with such transfers, the U.S. receives an equal offsetting receipt, representing an increase in the U.S. reserve position in the IMF -- an interest-bearing, liquid monetary asset that is available unconditionally to the U.S. in case of balance of payments need. As a consequence of these offsetting transactions, transfers to the IMF result in no net budgetary outlay.*

The Case for a Quota Increase

Our case for a moderate quota increase rests on the arguments outlined below.

- It is critical to U.S. interests and to the stability of the international monetary system that the IMF has adequate resources to do its job.

- The size of the IMF has declined significantly relative to the size of the world economy, international trade and global capital markets over the past two decades. Overall, an increase of roughly 60 percent in current quotas would be necessary to restore the Fund to the relative size prevailing before the last decision to increase quotas in 1990.

- At present the Fund has about $67 billion in uncommitted available resources, but the IMF projects that demand for Fund resources (net of repayments) will be $7-8 billion annually over the next 6 years. This could reduce the Fund's existing cushion of available resources quickly, leaving it dangerously exposed to unforeseen demands.

- The growth and liberalization of international capital markets have increased the level of risk in the international financial system. Countries are able to finance larger balance of payments deficits for longer periods of time, thus increasing the risk that an external financing problem will arise and the level of external finance that will be needed to address the problem.

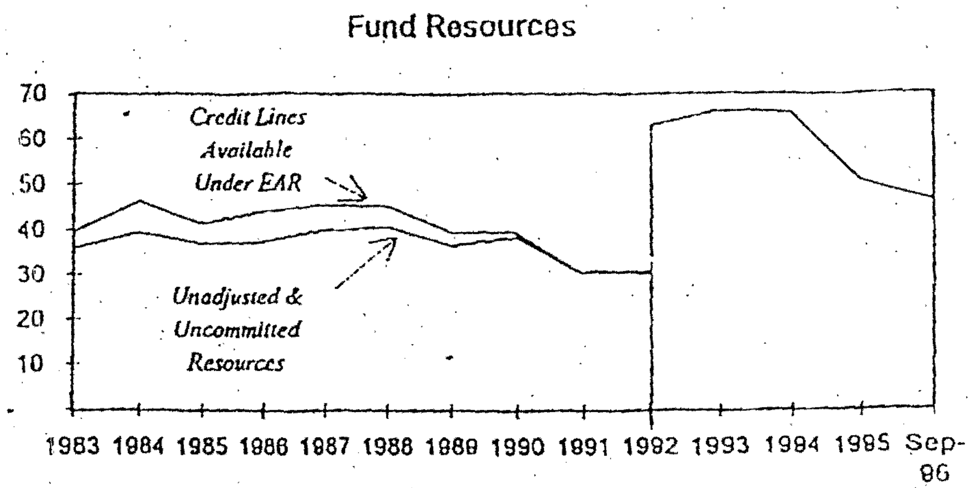
- There is a significant number of large emerging market countries now facing increased risk of financing crisis. If more than one of these countries were to face a financing requirement even half as large as was needed by Mexico, the Fund could be left with dangerously low levels of resources.

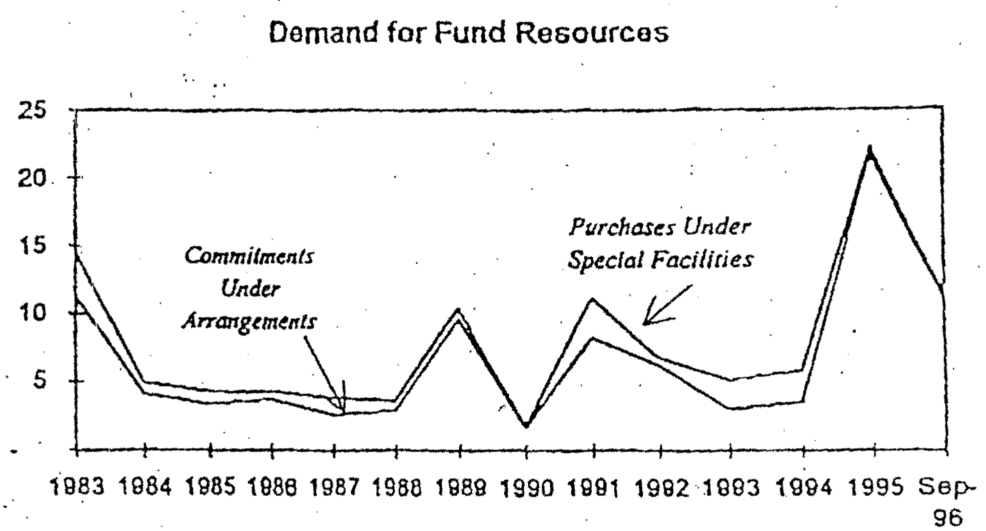
These arguments left the other Members of the IMF prepared as early as 18 months ago to go ahead with a quota increase. We have delayed agreeing to commence serious negotiations on the size and timing of a quota increase, while pressing for agreement on the NAB. At this point, our international credibility would be damaged by further delay on the quota issue, let alone a late hour refusal to support a modest increase. Our ability to promote internal reform and programmatic changes at the Fund would be seriously compromised, and the IMF's ability to serve U.S. economic interests would be undermined.

Economic Indicator	Amount of Quota Increase Required to Restore the Relative Size of the Fund to the Level Achieved in Past Quota Reviews (In percent of present quotas)				
	Sixth Review 1976 1/ (1968-72) 2/	Seventh Review 1978 1/ (1972-76) 2/	Eighth Review 1983 1/ (1976-80) 2/	Ninth Review 1990 1/ (1981-85)2/	Tenth Review 1995 1/ (1986-90)2/ 3/
Calculated Quotas	193	137	70	62	31
Current Payments	182	128	80	66	37
GDP	98	85	58	58	19
Reserves	66	76	44	87	34
Variability of Current Receipts	385	79	69	52	16

Source: IMF, "Eleventh General Review of Quotas - The size of the Overall Increase in Quotas - Quantitative Factors," January 17, 1996, EB/CQuota/96/1. 1/ Year in which the review was completed. No quota increase was provided under the Tenth Review; however total quotas increased due to influx of new members. 2/General review period. 3/ Calculations made for the Eleventh Review, currently underway, are based on data available through the end of 1993.

(In billions of SDRs)





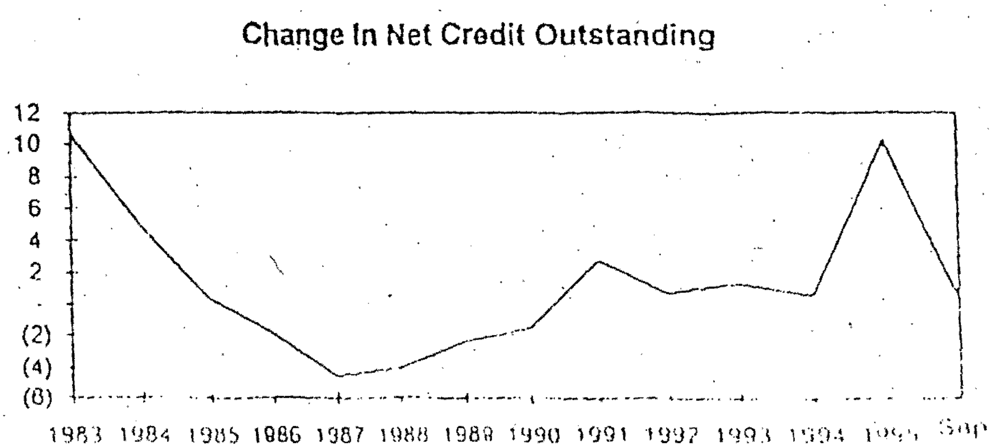


Table 1. Selected Financial Data, 1992-1997

(In billions of SDRs)

	1992	1993	1994	1995	End-July 1996	Projected 1996	Projected 1997
Total Quotas	141.4	144.8	144.9	145.3	145.3	...	...
Usable Ordinary Resources unadjusted	68.2	69.3	68.4	58.0	55.8	...	...
of which:							
(a) Uncommitted 1/	63.0	66.4	65.9	50.8	43.3	...	...
(b) Uncommitted and adjusted 2/	51.0	53.9	53.4	39.3	32.3	34.4	28.6
of which: SDR holdings	(8.6)	(6.7)	(5.5)	(0.7)	(0.9)	(1.3)	(1.3)
Gold at SDR 35 per fine ounce	3.6	3.6	3.6	3.6	3.6	3.6	3.6
Unused GAB and Associated 3/	12.3	12.3	12.3	12.3	12.3	12.3	12.3
Total Liquid Liabilities	33.9	32.8	31.7	36.7	38.0	39.8	42.4
(a) Reserve tranche positions	30.4	29.6	28.8	35.5	38.0	39.8	42.4
(b) Outstanding borrowing	3.5	3.2	2.9	1.1	--	--	--
Total Fund credit outstanding	27.8	29.1	30.3	41.6	42.7	44.3	47.6
of which:							
(a) General Resources Account	24.0	25.2	25.6	35.9	36.9	38.3	40.9
of which: overdue repurchases	(2.2)	(1.7)	(1.7)	(1.1)	(1.1)	...	...
(b) SAF and ESAF	3.6	3.8	4.5	5.6	5.7	5.9	6.6
(c) Trust Fund	0.2	0.1	0.1	0.1	0.1	0.1	0.1

1/ Excludes undrawn balances of commitments at July 31, 1996 which are considered likely to be drawn. These are estimated to be equal to the total amount of undrawn balances under arrangements of SDR 15.1 billion at July 31, 1996, less SDR 2.6 billion to adjust for: (i) undrawn balances under arrangements that are inoperative and are not likely to be drawn upon; and (ii) the possibility that existing operative arrangements may not be fully utilized.

2/ Usable currency holdings that are included in this total are reduced to provide for the possible exclusion of the Fund's holdings of the currencies of creditor members with weakening balance of payments positions and for working balances. The adjustment factor was 0.20 for 1992 through July 31, 1996. At July 31, 1996, the adjustment yielded a reduction in resources of SDR 11.0 billion.

3/ The amounts shown are as defined in the Guidelines for Borrowing which were in effect through November 15, 1991, and which provided that the amount included would equal outstanding borrowing by the Fund under the GAB and associated borrowing agreements or two thirds of the total under these agreements, whichever is greater. The present total of these agreements is SDR 18.5 billion.

(Source: EBS/96/136, 8/28/96)

1997-se-002361

97-SE-002361

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

ASSISTANT SECRETARY

ACTION

March 6, 1997

MEMORANDUM FOR DEPUTY SECRETARY SUMMERS

FROM: David A. Lipton MBfor

SUBJECT: Background Paper on IMF Quota Increase for NEC Meeting

ACTION FORCING EVENT:

At our request, Dan Tarullo has arranged an NEC meeting (presently scheduled for 2 p.m. on Friday, March 7) to discuss the possible IMF quota increase. Secretary Rubin had asked that we enlist full Administration support before launching detailed negotiations within the G-7 and in the IMF, and a public campaign to back the increase. We have told NEC staff that you would send a package of background material to participants ahead of the meeting.

RECOMMENDATION:

That you sign the attached memorandum transmitting a package of background material to participants in the upcoming NEC meeting.

Agree LS Disagree __________ Let's Discuss __________

ATTACHMENT: Transmittal memorandum and background package

EXECUTIVE

THE DEPUTY SECRETARY OF THE TREASURY
WASHINGTON

March 6, 1997

MEMORANDUM FOR DAN TARULLO
JACK LEW
AL LARSON
JEFF FRANKEL

FROM: Lawrence Summers

SUBJECT: Possible IMF Quota Increase

The IMF Executive Board has been conducting one of its periodic reviews of the adequacy of current quotas. We have for some time been resisting pressure to reach a conclusion but have decided that we should move ahead now. Apart from the ill will we could generate by refusing to negotiate seriously, the Congressional budget cycle requires that we provide the key committees with the outlines of an agreement sometime in the spring, if an increase is to be considered as part of the FY 98 budget. (Most legislative experts believe that Congress would find it easier to deal with the NAB and a quota increase together.) In this regard, I will be testifying on April 9 before the Senate Foreign Relations Subcommittee on International Economic Policy, Export, and Trade Promotion on our 150 account requests and will need to say something about a quota increase, although we are unlikely to have a deal until end-April at the earliest.

I attach a background note outlining the case for a quota increase. Also attached is a set of proposals on IMF policy reforms which could serve as a *quid pro quo* for our agreement to an increase.

We propose to insist that a quota increase be kept below 50 percent. Our own quota would increase by a smaller percentage than the overall increase, as a number of countries would receive an upward adjustment to their shares. However, we would also resist an adjustment that would result in an excessive erosion of our voting power in the IMF. (Our voting share is now 17.8 percent. Major IMF decisions, including quota increases, require an 85 percent majority.)

The principle considerations in reaching our conclusion are that agreeing to an increase would:

- help to maintain IMF credibility and restore some of the erosion in the relative size of the institution in the world economy;
- enhance our leverage in pushing our policy agenda for reform at the IMF;

- spread the burden of maintaining the stability of the international monetary system more fairly by providing additional quota increments for a few countries whose current quotas are seriously out of line with their relative importance in the global economy; and

- honor our commitment to our G-7 partners and to other participants in the New Arrangements to Borrow that the NAB would not be a substitute for a quota increase.

ATTACHMENTS:	Tab A:	Background Paper: The Case for an IMF Quota Increase
	Tab B:	Proposed Policy Agenda for the IMF

The Case for an IMF Quota Increase

The IMF's liquidity position is approaching a point at which an increase in quota resources will be necessary if it is to be able to perform its mission of enabling its members "to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity." A corollary need is to maintain sufficient liquidity to assure members holding creditor positions in the IMF that they would be able to encash some of that claim if needed -- such assurance is the basis for the budgetary treatment of cash transfers under our quota subscription whereby they are not scored as outlays, as they are an exchange of monetary assets.

This judgment is based on the following considerations.

1. **The IMF is a critically important institution in support of the economic and strategic interests of the United States by fostering growth, financial stability and democracy around the world.**

- o It is the only institution capable of promoting the macroeconomic policies necessary to achieve the stable economies essential for reform to succeed.

2. **A continued decline in the relative size of the IMF could undermine its credibility as an insurance policy for systemic risks and leave it too weak to respond to financial crises in countries of key political importance to the United States. We have a uniquely large stake in ensuring that the IMF has adequate resources because our economic and security interests are global in nature.**

- o Countries of key importance include:
  - oo with respect to stability of the international financial system,
    - Mexico as a recent example;
    - China, other emerging economies in Southeast Asia or Latin America, Canada (in the event of renewed threat of Quebec secession) and smaller European countries (amid tensions caused by the approach of EMU) as prospective cases;
  - oo with respect to U.S. geopolitical interests,
    - Russia, other FSU, Haiti, Pakistan and Bosnia as past or present examples;

TREASURY CLEARANCE SHEET

NO.__________
DATE:_________

MEMORANDUM FOR: ☐ SECRETARY ☐ DEPUTY SECRETARY ☐ EXECUTIVE SECRETARY
☐ ACTION ☐ BRIEFING ☐ INFORMATION ☐ LEGISLATION
☐ PRESS RELEASE ☐ PUBLICATION ☐ REGULATION ☐ SPEECH
☐ TESTIMONY ☐ OTHER __________

FROM: Assistant Secretary Lipton
THROUGH:
SUBJECT: Paper for NEC Meeting on IMF Quota Increase

REVIEW OFFICES (Check when office clears)

- ☐ Under Secretary for Finance
  - ☐ Domestic Finance
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  - ☐ Treasurer
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    - ☐ Savings Bonds
  - ☐ Other __________

NAME (Please Type)	INITIAL	DATE	OFFICE	TEL. NO.
INITIATOR(S)				
S. Hart/J. Lister	[illegible] 3/6/97	3/6/97	International Monetary Policy	622-0112
REVIEWERS				
T. Geithner	TG 3/9?		Senior DAS (Intl. Affairs)	622-0656
R. Sinkfield	RS 3/9?		Deputy to the Asst. Sec. (Leg. Affairs & Public Liaison)	622-1960

SPECIAL INSTRUCTIONS

☐ Review Officer Date ☐ Executive Secretary Date

DO F 70-02.1 (04/89)

1997-SE-004110

THE DEPUTY SECRETARY OF THE TREASURY
WASHINGTON

4/18/97

ACTION

MEMORANDUM FOR SECRETARY RUBIN

FROM: Lawrence Summers

SUBJECT: IMF Special Allocation of Special Drawing Rights (SDRs)

ACTION FORCING EVENT:

We need to decide whether to support closure by the April 28 Interim Committee on an amendment of the IMF Articles of Agreement to provide for a one-time special allocation of SDRs.

RECOMMENDATION: That you adopt the following approach:

Seek to defer a decision on an amendment to the IMF Articles of Agreement for a one-time special ("equity") allocation of SDRs that would permit all members to participate fully in the SDR system pending resolution of the debate on a quota increase.

- If we decide to delay a quota increase and there is strong Executive Board pressure to go ahead with an SDR allocation, then we should be prepared to support an allocation for a maximum of SDR 21 billion. (We should keep any allocation below the level of SDR 21.3 billion, which is the cumulative allocations to date.)

- However, we should make it clear that we will not seek congressional authorization of our support for it until agreement has been reached on additional amendment to the Articles for which we require congressional approval -- notably, formalization of the Fund's role in promoting capital market liberalization.

_________ Agree _________ Disagree _________ Other

BACKGROUND:

The purpose of the proposed amendment to the IMF Articles is to permit full participation in the SDR system by all IMF members, including those that joined the IMF after the previous allocation in 1981 such as Russia and FSU countries.

- In its September 1996 communique, the Interim Committee endorsed the proposed one-time allocation of SDRs, based on a common benchmark ratio of cumulative allocations to present quotas, and it "requested the [IMF] Executive Board to finalize its work on the amendment by the time of the Committee's next meeting" in the Spring.

- We have opposed the Managing Director's proposal for a large allocation of SDR 26.6 billion and have indicated our preference for a level closer to the SDR 16 billion endorsed by the G-7 in 1994. We informally signalled that we might be prepared to support an allocation of as much SDR 20 billion.

- Camdessus recently indicated that he would reluctantly accept an increase of SDR 22.4 billion, which would bring net cumulative allocations up to 30 percent of quotas.

  - This may reflect his discussion Wednesday, April 16, with developing countries. We undertand that some developing countries are prepared to accept the SDR 20/21 billion level, while others resist on the grounds that they had agreed to withdraw their insistence on a general allocation on the basis that a special allocation would amount to SDR 26.6 billion.

Our suggested maximum SDR 21 billion allocation would constitute an increase of 31 percent from the SDR 16 billion we proposed in 1994 (but 21 percent less than the SDR 26.6 billion proposed earlier by Camdessus).

- This flexibility on our part could be viewed as the quid pro quo for the concession by developing countries to accept the concept of a special, one-time "equity" allocation rather than continue to press for a general allocation (which we believe cannot be justified on the basis of a "long-term global need" as required under the Articles).

- Anything more would arguably be tantamount to a general allocation.

- Developing countries would have to decide whether this allocation, which would also benefit developed countries including the United States, is better than nothing.

There are several reasons for informally linking the decision on the size and timing of an SDR allocation to a decision on a quota increase.

- If we decide to delay support for an IMF quota increase, it may be useful to delay a decision on the SDR allocation so that the budget request for the NAB could proceed independently in FY 98.

- If we decide to support a quota increase at this time, our support for closure on the SDR allocation issue could strengthen our negotiating position for a small quota increase.

- Developing countries often need to use their SDR holdings to cover the amount of any quota increase that they must pay in as reserve assets (SDRs, along with certain currencies that qualify).

- Note that Camdessus insists that the Board make a final decision on size and format next week and has invited the G-7 Executive Directors to meet with him in the afternoon on Tuesday, April 22. His sense of urgency may be driven by his acute frustration with our stated preference for a quota increase in the 35 percent range.

The attached table (of recent IMF staff calculations) illustrates certain anomalies that arise from the proposed benchmark ratio approach to an allocation on the order of one that we would propose (see column 3).

- G-10 countries would receive about 46 percent of the total allocation.

- The group of new members since 1981 (a key target of the "equity amendment) would take up only about 18 percent of the total, and Switzerland would receive 19 percent of that share.

Although there is broad support for a special one-time allocation of SDRs, we can anticipate that critics of the IMF and of the SDR will attack the proposed amendment to the Articles on the following fronts at least.

- An allocation is inflationary because it creates international reserve assets.

    - This is less than persuasive because of the relatively small contribution (roughly $30 billion) to global liquidity, most of which would accrue to countries that won't seek to use them to increase spending. Total international reserves, excluding gold, amount to about $1.5 trillion.

- An allocation is an exercise in poor public policy because it provides an unconditional financial asset to developing countries.

    - This is more difficult to counter, although developing countries would receive less than half of the total allocation.

Attachment

Withdrawal/Redaction Marker
Clinton Library

DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
001. memo	The Secretary to Members of Executive Board re: Special Allocation of SDRs (Special Drawing Rights) - Illustrative Calculations (IMF Document) (7 pages)	04/01/97	P1/b(1) Unclass.

This marker identifies the original location of the withdrawn item listed above. For a complete list of items withdrawn from this folder, see the Withdrawal/Redaction Sheet at the front of the folder.

COLLECTION:

Clinton Administration History Project

OA/Box Number: 24126

FOLDER TITLE:

[History of the Department of the Treasury - Supplementary Documents] [32]

jp28

RESTRICTION CODES

Presidential Records Act - [44 U.S.C. 2204(a)]

P1 National Security Classified Information [(a)(1) of the PRA]
P2 Relating to the appointment to Federal office [(a)(2) of the PRA]
P3 Release would violate a Federal statute [(a)(3) of the PRA]
P4 Release would disclose trade secrets or confidential commercial or financial information [(a)(4) of the PRA]
P5 Release would disclose confidential advise between the President and his advisors, or between such advisors [a)(5) of the PRA]
P6 Release would constitute a clearly unwarranted invasion of personal privacy [(a)(6) of the PRA]

C. Closed in accordance with restrictions contained in donor's deed of gift.
PRM. Personal record misfile defined in accordance with 44 U.S.C. 2201(3).
RR. Document will be reviewed upon request.

Freedom of Information Act - [5 U.S.C. 552(b)]

b(1) National security classified information [(b)(1) of the FOIA]
b(2) Release would disclose internal personnel rules and practices of an agency [(b)(2) of the FOIA]
b(3) Release would violate a Federal statute [(b)(3) of the FOIA]
b(4) Release would disclose trade secrets or confidential or financial information [(b)(4) of the FOIA]
b(6) Release would constitute a clearly unwarranted invasion of personal privacy [(b)(6) of the FOIA]
b(7) Release would disclose information compiled for law enforcement purposes [(b)(7) of the FOIA]
b(8) Release would disclose information concerning the regulation of financial institutions [(b)(8) of the FOIA]
b(9) Release would disclose geological or geophysical information concerning wells [(b)(9) of the FOIA]

TREASURY CLEARANCE SHEET

NO.__________
DATE:__________

MEMORANDUM FOR: ☑ SECRETARY ☐ DEPUTY SECRETARY ☐ EXECUTIVE SECRETARY
☑ ACTION ☐ BRIEFING ☐ INFORMATION ☐ LEGISLATION
☐ PRESS RELEASE ☐ PUBLICATION ☐ REGULATION ☐ SPEECH
☐ TESTIMONY ☐ OTHER __________

FROM: Deputy Secretary Summers
THROUGH:
SUBJECT: IMF Special Allocation of SDRs

REVIEW OFFICES (Check when office clears)

☐ Under Secretary for Finance
☐ Domestic Finance
☐ Economic Policy
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☐ Mint
☐ Savings Bonds

☐ Other __________

NAME (Please Type)	INITIAL	DATE	OFFICE	TEL. NO.
INITIATOR(S)				
Susan Hart	SH	4/1~~6~~/97	OASIA/IMF	622-0112
REVIEWERS				
Geithner	Cleared			
David Lipton/AS	DL	4/18/97	OASIA/I	2-1270
Lister	Cleared			

SPECIAL INSTRUCTIONS

☐ Review Officer Date

☐ Executive Secretary Date

DO F 70-02.1 (04/89)

Drafted by : Susan Hart/IMF SH 4/17/97 2-0129

Reviewed by: Jim Lister/IMF JL 4/16/97 2-0112
Timothy Geithner/I TG 2-0656

OASIA/IMF
4/17/97 4:30 pm.

1997-SE-006148

THE DEPUTY SECRETARY OF THE TREASURY
WASHINGTON

6/9/97

ACTION

MEMORANDUM FOR SECRETARY RUBIN

FROM: Lawrence H. Summers

SUBJECT: Increase in Quota Subscription for the International Monetary Fund

ACTION-FORCING EVENTS

With the inclusion in the budget agreement of the requisite 5-year cap adjustment for an IMF quota increase, we need to consider our next steps with respect both to reaching an agreement in the IMF and to the timing of a Congressional request. A decision to request Congressional approval this year would require very near-term action to finalize an agreement and prepare the ground on the Hill. IMF members are pushing very hard for a final deal no later than the September Bank/Fund annual meetings in Hong Kong, and we are likely to encounter pressure at the Denver summit to commit to a completion date.

RECOMMENDATION

That we proceed with negotiations in the Fund, with the objective of concluding an acceptable agreement (as outlined below) at the September meetings. On the basis of such an agreement, we then would request Congressional authorization in FY 1999. This is the consensus recommendation of D. Lipton, T. Geithner, J. Lew (OMB) and the Fed.

______________Agree ______________Disagree ______________Let's Discuss

BACKGROUND

(A) We have been considering three basic options on how we might proceed. Briefly stated, they are:

(1) Act now on both fronts: Push for a deal at the IMF as soon as possible - within the next few weeks - and request Congressional approval for FY98. Based on consultations with Alan Cohen, Legislative Affairs and OMB, such a request for Congressional approval would need to be based on a conclusive agreement at the Fund. (Congress would be very unlikely to consider a request for an increase of "up to" some number, prior to a deal.) A deal in September would permit a request only at the end of the fiscal year, severely limiting the chances of approval this calendar year. Hence, if we want to attempt FY98 approval, we must have a deal by late June (at the very latest) to be able to present a formal request to the Hill prior to final Senate Appropriations action.

(2) September IMF Deal, FY99 Legislative Request: Work to achieve an acceptable deal by the Annual Meetings (but without committing to a deadline in advance), and request legislative approval next year. This is our recommendation and, as elaborated below, is based on our assessment that Congress is unlikely to say yes this year under any predictable circumstances and that an all-out push for an IMF deal within the next few weeks could damage prospects on the Hill for the NAB and our other objectives in the 150 Account.

(3) Stall Indefinitely: Push IMF agreement off until after the September meetings. The best justification for this position is that Congressional approval will not occur this year and the Fund's need for additional resources is not immediate.

(B) *We believe that Option #2 is preferable for the following reasons:*

- While not impossible, the chances for Congressional approval this year are slim. It is fairly late in the process for submission of such a large request, and we are already encountering stiff resistance to the NAB in the House, with friendlier but non-committal signals at best from the Senate. The favorable budget result on cap adjustments should not be interpreted to mean imminent or easy appropriation of the requests themselves, especially of requests that have yet to be submitted.

  o As stated above, it is generally believed that we should have an IMF agreement before we request legislative approval. This would mean an immediate and probably very visible acceleration of IMF negotiations, with a clearly implied near-term deadline, which also might raise unjustifiable hopes in the IMF of imminent favorable action on the Hill.

- There is a real risk that a highly visible quota negotiation - and subsequent Congressional request of this size - could damage the prospects for passage of the NAB or, perhaps, other components of our 150 agenda.

- With IMF liquidity now at a ratio of about 125%, there appears to be no compelling case for an immediate augmentation of resources. Barring unforeseen financial problems of very significant magnitude and breadth, the Fund should have no great difficulty meeting members' financial needs for the next year or two. This will be especially true if the NAB is approved and available.

- However, to delay a final IMF agreement beyond September would be costly in terms of our relations with the G-7 and other IMF members, and we need to begin soon to make the case on the Hill given that passage ultimately may take several years to achieve. The basic outline of an acceptable deal has been in place since the April meetings. To stall indefinitely would damage our credibility and reliability, and there is a very good chance of obtaining an acceptable result by September.

- o A September deal would permit us to include a formal request in the President's FY99 Budget Proposal and begin the process of winning Congressional support. Even if election-year politics eventually kill the request next year, having prepared the ground will increase prospects for FY2000 approval. Finally, a September agreement keeps open the option, however remote, of an opportunistic request in the waning days of legislative activity this year.

(C) *Our recommended negotiating strategy and objectives are as follows:*

- Resume negotiations in the IMF (primarily with other G-7 countries), with an internal but undisclosed target completion date of September. Resist pressure to commit to a deadline at Denver, pushing instead for language in the Summit Statement suggesting a desire "for progress" by the annual meetings. Such a deadline limits our negotiating leverage and tactics, and the reaction in Congress to such a public declaration may be unfavorable.

- Negotiate for an overall increase in the 35%-45% range, with the U.S. increase coming in somewhat below the total percentage because of distributional issues. (For example, the U.S. increase would be about 40% if the overall hike is 45%. In the negotiations so far, we have suggested that the data do not support an overall increase in excess of 35%.) Depending on the ultimate outcome on distribution of the increase, the most contentious and uncontrollable aspect of the negotiations, this could mean a U.S. increase of about $15 billion.

- We would be willing to accept a reduction in our voting share from the current level of 17.8%, with proposals now on the table that would reduce it to somewhere in the 17% - 17.5% range. This would still be comfortably above the 15% veto share. Given the complexities of negotiations over distribution and the likelihood that this would be the last quota increase for some time, we may have to consider agreeing to a share somewhat lower than the 17% floor now under discussion.

- Subject to your approval of the recommendations herein - and White House concurrence - we would brief key members of Congress and staff privately on our decision and negotiating strategy.

Attachment: Tab 1: 6/5/97 Kasich-Raines letter on cap adjustments

TREASURY CLEARANCE SHEET

NO.

Date June 9, 1997

MEMORANDUM FOR: x SECRETARY ☐ DEPUTY SECRETARY ☐ EXECUTIVE SECRETARY
☐ ACTION ☐ BRIEFING ☐ INFORMATION ☐ LEGISLATION
☐ PRESS RELEASE ☐ PUBLICATION ☐ REGULATION ☐ SPEECH
☐ TESTIMONY ☐ OTHER

TO: Secretary Rubin
FROM: Deputy Secretary Summers
SUBJECT: IMF Quota Increase

REVIEW OFFICES (Check when office clears)

☐ Under Secretary for Finance
- ☐ Domestic Finance
- ☐ Economic Policy
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- ☐ Management

☐ Other

NAME (Please Type)	INITIAL	DATE	OFFICE/ROOM NO.	TEL. NO.
INITIATOR(S)				
IMF/M Jaskowiak		6/9/97	Office of International Monetary Policy	622-5052
REVIEWERS				
IMF/J Fister/S. Hart		6/9/97	Director, Office of Int'l Monetary Policy	622-0112
IMF/K Lissakers/B Newman			Executive Director, IMF	623-7759
LF/R Sinkfield		6/9/97	Deputy to the A/S, Legislative Affairs	622-1960
ID/ W Schuerch	WES	6/9/97	Deputy Assistant Secretary (Int'l Dev)	622-0154
I/M/T Geithner		6/9/97	Senior Deputy Assistant Secretary (Int'l Affairs)	622-0656
UII/ D Lipton	DL	6/9/97	Assistant Secretary, International Affairs	622-1270

SPECIAL INSTRUCTIONS

☐ Review Officer ______ Date: ______ ☐ Executive Secretary ______ Date ______

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U.S. House of Representatives
COMMITTEE ON THE BUDGET
Washington, DC 20515

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SCOTTY BAESLER, KENTUCKY
KEN BENTSEN, TEXAS
JIM DAVIS, FLORIDA
BRAD SHERMAN, CALIFORNIA
ROBERT A. WEYGAND, RHODE ISLAND
EVA M. CLAYTON, NORTH CAROLINA

THOMAS S. KAHN, MINORITY STAFF DIRECTOR
AND CHIEF COUNSEL
(202) 226-7200

June 5, 1997

The Honorable Franklin D. Raines
Director
Office of Management and Budget
Old Executive Office Building
17th St. & Pennsylvania Ave., N.W.
Washington, DC 20503

Dear Frank:

This letter responds to your concerns regarding two specific allowances that are included in the Concurrent Resolution on the Budget for Fiscal Year 1998 [H. Con. Res.84].

As you know, the Resolution contains an allowance in both the House of Representatives and the Senate for the International Monetary Fund (IMF) and international arrearages, after the appropriate policies have been resolved between the White House and Congress. The Bipartisan Budget Agreement assumes a cap adjustment for these two purposes, but was silent on the conforming changes in the allocations and aggregates set forth in the budget resolution and the duration of any cap adjustment.

For the House of Representatives, the Resolution provides for both adjustments in fiscal years 1998 and 1999; the Senate provides for both adjustments for fiscal years 1998 through 2002. I understand that providing two years of adjustments may not be of sufficient duration to address the Clinton Administration's concerns. Consequently, when the Congress considers an extension of the Budget Enforcement Act's (BEA) discretionary spending caps, I intend to provide for adjustments in the "statutory" caps of 3 years for the arrearages and 5 years for the IMF. Of course, these new BEA discretionary cap adjustments would be contingent on the appropriation of funds, pursuant to an agreement between the White House and Congress.

I hope this letter addresses your questions.

Sincerely,

John R. Kasich
Chairman
House Committee on the Budget

1997-SE-007145

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

July 3, 1997

MEMORANDUM FOR DEPUTY SECRETARY SUMMERS
ASSISTANT SECRETARY LIPTON

FROM: Timothy Geithner
Senior Deputy Assistant Secretary (International Affairs)

SUBJECT: Capital Account: Amendment of IMF Articles

This note is intended to provide the basis for a discussion with you on the key issues that will have to be settled in preparing an amendment of the IMF Articles of Agreement to promote liberalization of restrictions on capital movements. While decisions will be taken in the Executive Board, G-10 Deputies will have a chance to influence the debate in the forthcoming July 9 meeting and perhaps subsequent meetings.

In a series of largely general discussions to date, the Executive Board has endorsed the concept of giving the Fund a mandate in this area. It is now beginning to come to grips with the myriad specific questions to be settled but has not yet dealt with the most important ones -- e.g., defining the scope of the obligations and the approval process, and sanctions for non-compliance. A first round on these issues is likely to take place at the July 11 Board meeting.

We are moving toward recommending that you support an approach that is modelled on the present arrangement for restrictions on current operations as set forth in Articles VIII and XIV, which provide for IMF approval of all restrictions (Article VIII) but a flexible "transitional" procedure enabling countries to delay acceptance of the Article VIII obligation while undertaking not to adopt new restrictions. However, it may be necessary to extend the "grandfathering" provision in order to avoid a situation in which virtually all countries opt for transitional status. It will also be necessary to provide virtually complete latitude for restrictions imposed for national security reasons and significant latitude for those imposed for prudential reasons.

Set forth below are recommended provisional U.S. positions on these and selected other significant issues, with a fallback option in some cases in event of resistance from other countries. Note that decisions on one issue may greatly influence the decision on another, and that different treatment for classes of countries or categories of transactions is possible.

Attached at Tab A is a schematic of a more complete list of issues with an indication of the range of possible approaches or of the key subsidiary points to be settled.

Scope of liberalization obligation

- No restrictions[1] unless approved or subject to an exclusion
  (Alternative: existing restrictions grandfathered)

Transition arrangements

- Existing restrictions grandfathered; no new restrictions unless approved or subject to exclusion
  (Alternative: grace period for new restrictions)

Nature of approval process

- Explicit *ex post* approval required (50 percent majority)
  (Alternative: above approach for restrictions imposed for macroeconomic purposes; those imposed for other purposes automatically approved unless explicitly disapproved by 70 percent majority)

Enforcement

- In addition to the provisions of Article XXVI[2], which have never been applied with respect to violations of Articles VIII and XIV, maintenance of unapproved restrictions would trigger critical reports and render the country ineligible to receive technical assistance (70 percent vote).
  (Alternative: applicability of Article XXVI could be reduced.)

Exceptions for national security, prudential and other restrictions without macroeconomic motive

- Notification and justification required, but approval not required.

- However, Board can recommend removal of restrictions and, in specified circumstances, initiate disapproval process.

Coverage of Inward Direct Investment

- Broad restrictions on economic grounds covered; restrictions on non-economic grounds and right of establishment not covered. (Main need is to create notification and non-discrimination obligation.)

---

1 A restriction would be defined as less favorable treatment of a non-resident than of a resident.

2 Comprising progressively: ineligibility to use IMF resources, suspension of voting rights and expulsion.

Restrictions of subnational units

- Not covered if national authorities are not empowered to override.

Discrimination among non-residents

- Prohibited.

cc. Karin Lissakers, Meg Lundsager, Russ Munk, Caroline Atkinson

Attachments: TAB A: Principal Issues to be Settled
TAB B: Report on June 30 Executive Board Discussion

TREASURY CLEARANCE SHEET

NO.__________
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MEMORANDUM FOR: ☐ SECRETARY ☐ DEPUTY SECRETARY ☐ EXECUTIVE SECRETARY
☐ ACTION ☐ BRIEFING ☐ INFORMATION ☐ LEGISLATION
☐ PRESS RELEASE ☐ PUBLICATION ☐ REGULATION ☐ SPEECH
☐ TESTIMONY ☐ OTHER __________

FROM: Senior Deputy Assistant Secretary Geithner
THROUGH: Assistant Secretary Lipton
SUBJECT: Capital Account: Amendment of IMF Articles

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NAME (Please Type)	INITIAL	DATE	OFFICE	TEL. NO.
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REVIEWERS				

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☐ Review Officer Date

☐ Executive Secretary Date

DO F 70-02.1 (04/89)

Principal Issues to be Settled on Capital Account Amendment

The following listing of principal issues presents the range of potential outcomes under each heading (in ascending order of toughness), or questions

I. **Nature and Scope of Obligations**

- o Exhortation for progressive liberalization (no approval required)
- o No new restrictions without approval (stand-still)
- o No restrictions without approval, unless subject to an exclusion (see V & VII)

II. **Approval Process**

- o Non-binding (i.e., recommendations only)
- o Approval in principle unless explicit disapproval, possibly with a qualified majority of 70 or 85 percent
- o Explicit ex-post approval required (50 percent majority)

Under each approach, provision could be made for periodic review and, if approval is required, confirmation of the earlier approval

III. **Enforcement**

- o No explicit sanction other than peer pressure and periodic reviews.
- o Maintenance of unapproved restrictions subjects the country to being declared ineligible to receive IMF financial and/or technical assistance.
- o Maintenance of unapproved restrictions subjects the country to graduated sanctions under the provisions of Article XXVI (including suspension of voting rights, inability to participate in quota increases and SDR allocations, and eventual compulsory withdrawal).

IV. **Transitional Arrangements**

- o Permit a country to postpone adherence to specific obligations until it considers that it is able to do so.
- o Prohibit such countries from introducing new measures without approval

- o Require specific commitments to liberalize within an agreed schedule

V. <u>Exceptions for non macro-economic reasons</u>

- o Should a country be allowed to have a blanket exception for national security and prudential reasons?

    - oo If so, should it be required to notify and justify such measures?
    - oo If not, should the IMF's approval process be less demanding than for restrictions imposed for macro-economic reasons?

VI. <u>Definition of "Restrictions"</u>

- o Should determination of the existence of a restriction be based on specific laws/regulations and authority, or on the economic effect of actual government practices?

- o Should discrimination among non-residents be prohibited (i.e., an MFN test)?

- o Should subnational restrictions be covered?

- o Should transactions between residents involving a foreign asset be covered?

VII. <u>Coverage of capital transactions</u>

- o Should IMF jurisdiction be extended to include some or all aspects of inward direct investment, or should these be left to the MAI and WTO?

- o Should government proprietary operations be covered (e.g., sovereign defaults, privatization, debt operations) and what would be the implications for orderly work-out operations?

The definition of a capital control could have important implications for the enforceability of IMF decisions on approval/non-approval in the courts of major financial centers (Article VIII:2(b)).

VIII. <u>How Obligations are Determined</u>

- o Specify general obligations in Articles, leaving substantial scope for interpretation to Executive Board

- o Specify specific obligations in Articles

- o Confer on Board of Governors or Executive Board authority to establish or extend obligations, possibly on the basis of high majority vote.

Draft: 7/1/97 cap-acct.sch

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DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
002. memo	Barry S. Newman (IMF) to David Lipton & Tim Geithner re: Capital Movement Amendment (2 pages)	07/01/97	P1/b(1) Unclass.

This marker identifies the original location of the withdrawn item listed above. For a complete list of items withdrawn from this folder, see the Withdrawal/Redaction Sheet at the front of the folder.

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RESTRICTION CODES

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P1 National Security Classified Information [(a)(1) of the PRA]
P2 Relating to the appointment to Federal office [(a)(2) of the PRA]
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RR. Document will be reviewed upon request.

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b(6) Release would constitute a clearly unwarranted invasion of personal privacy [(b)(6) of the FOIA]
b(7) Release would disclose information compiled for law enforcement purposes [(b)(7) of the FOIA]
b(8) Release would disclose information concerning the regulation of financial institutions [(b)(8) of the FOIA]
b(9) Release would disclose geological or geophysical information concerning wells [(b)(9) of the FOIA]

TREASURY CLEARANCE SHEET

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MEMORANDUM FOR: ☐ SECRETARY ☐ DEPUTY SECRETARY ☐ EXECUTIVE SECRETARY
☐ ACTION ☐ BRIEFING ☐ INFORMATION ☐ LEGISLATION
☐ PRESS RELEASE ☐ PUBLICATION ☐ REGULATION ☐ SPEECH
☐ TESTIMONY ☐ OTHER __________

FROM: Senior Deputy Assistant Secretary Geithner
THROUGH: Assistant Secretary Lipton
SUBJECT: **Capital Account: Amendment of IMF Articles**

REVIEW OFFICES (Check when office clears)

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  - ☐ ATF
- ☐ Customs
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J. Lister	JML cap-acct.701	7/2/97	International Monetary Policy	622-0112
REVIEWERS				

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☐ Review Officer Date __________ ☐ Executive Secretary Date __________

DO F 70-02.1 (04/89)

1997-SE-008892

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

August 14, 1997

MEMORANDUM FOR DEPUTY SECRETARY SUMMERS

FROM: Timothy F. Geithner TFG
Senior Deputy Assistant Secretary (International Affairs)

SUBJECT: Capital Account Transactions and Amendment of IMF Articles

ACTION FORCING EVENT:

The IMF Executive Board has been having preliminary discussions on how to frame an amendment of the Articles of Agreement that would impose obligations to liberalize capital account transactions. It aims to reach conclusions on key elements to be reflected in such an amendment which the Interim Committee could endorse at its September 21 meeting in Hong Kong, as requested at the Committee's April meeting. This memorandum requests your approval of guidelines for the U.S. Executive Director for use at forthcoming Board meetings (August 26 and September 3) -- we will probably have to come back to you on some of these and perhaps other issues as the debate develops.

RECOMMENDATION:

That you approve the recommended positions set forth in the attachment at TAB A.

[These represent a consensus of views among Karin Lissakers and Barry Newman, Caroline Atkinson and Jim Lister on the overall approach, as well as comments/clearance from the office of the Assistant General Counsel for International Affairs and Meg Lundsager. (We are consulting Tax Policy on how to ensure that legitimate tax measures are not questioned.) The Federal Reserve is in general agreement, but awaiting further detail on the treatment of prudential measures -- we have also reached out to the regulatory community beyond the Fed, and will need to clear final positions with them. The Fed is also interested in the treatment of restrictions imposed for monetary policy purposes, on which we will be back to you if there are differences of view.]

_________ Agree _________ Agree as amended _______________ Let's discuss

BACKGROUND/ANALYSIS:

The Executive Board has made considerable progress, but many hard decisions lie ahead. (See USED/IMF's report on July 15 discussion and Chairman's summing-up at TAB B.)

As indicated in my July 3 memorandum (copy at TAB C), we are recommending that you support an approach that is modeled on the procedures in the present Articles governing current account transactions, i.e.,

- an Article VIII equivalent which provides for IMF approval of any restrictions (existing and new); and

- an Article XIV equivalent which grandfathers existing restrictions of "transitional" countries but requires approval of any new restrictions (including intensification of existing restrictions) and which effectively allows the countries to decide when they are ready to give up their grandfathered restrictions.

This implies a brief, general text in an amendment coupled with considerable exercise of Executive Board discretion, which over time would establish precedents for subsequent decisions -- i.e., case law. However, the task will be much more complex than under the present Articles VIII and XIV, as the capital account obligations will almost certainly extend to underlying transactions as well as the payments side of the transactions, and to inflows as well as outflows.

- The feasibility of such an approach depends on whether countries are confident that it provides sufficient assurance that they will be able to impose -- without significant embarrassment or sanctions -- restrictions that they deem essential to their economic interests or are justified on other grounds such as national security or prudential concerns.

- However, if the approval and sanction process is very weak or if a very large number of countries decide to obtain assurance by relying on the transitional arrangements, particularly if that group includes some advanced countries and most emerging economies, the above approach will have little meaning.

- Resolving this basic tension may be difficult. It also means that decisions on individual issues cannot be easily taken in isolation

Our general support of open markets and a meaningful commitment by IMF members to removing controls must be articulated in a manner which provides us reasonable assurance with respect to our own measures in three areas:

- national security restrictions

- prudential requirements

- individual U.S. states' restrictions.

At the same time, we will need to avoid doing so in a manner that is transparently an effort to avoid all scrutiny by others. In this regard, we are in touch with the regulatory community (OCC, SEC and CFTC, as well as the Fed) and will be consulting with them on relevant matters.

Another significant issue to be decided is how to treat inward direct investment -- IMF staff and a number of Executive Directors (e.g., the Canadian) favor excluding inward DI from the scope of an amendment. We are proposing its inclusion in some manner.

These central issues are addressed in items (4) through (6) of TAB A.

<u>Attachments</u>:	TAB A:	Recommended positions
	TAB B:	Reports on July 15 Executive Board Discussion
	TAB C:	July 3 memorandum

CAPITAL ACCOUNT AMENDMENT: ISSUES AND RECOMMENDED U.S. POSITIONS

1. Structure of Liberalization Obligation

- Support "Article VIII" approach whereby countries accepting the obligation agree not to maintain any existing restrictions or impose new ones without the IMF's approval.

  However, we may need to revisit this view if a critical mass of countries will only accept a meaningful overall obligation if certain categories of restrictions can be maintained through a less onerous mechanism, e.g., self-executing procedures such as the right to lodge a reservation) or a weakened form of approval. The categories of restrictions that are most likely to require such an approach are those imposed to deal with "volatile" flows such as certain short-term transactions.

  A similar approach might also be applied to restrictions deemed outside -- in part or in whole -- the competence of the IMF to assess, such as those motivated by national security and prudential concerns and those imposed on inward direct investment -- see discussion in (4) and (5) below.

_________ Agree ___________ Disagree ____________________________ Let's Discuss

2. Transitional Arrangements

- Support "Article XIV" approach, whereby countries not ready to assume full liberalization obligations may maintain existing restrictions, subject to representations by the IMF recommending their removal or partial liberalization, but require approval for new restrictions. Maintain potential to declare a country that ignores representations ineligible to use IMF resources, and in principle subject to the full range of penalties for non-compliance with obligations of membership (see (3) below).

- In a departure from the existing provisions for restrictions on current payments, define "new restrictions" on capital flows to include adaptation of existing restrictions that result in significant intensification.

  A country which ignores the IMF's "representations" can in principle be declared ineligible to use the Fund's resources; however, the IMF has never done so on that basis.

  Under Article XIV, a member may maintain and also "adapt to changing circumstances" restrictions in effect when it became a member. This provision, if carried forward to *capital account transactions, could become too much of a loophole. It may be necessary to amend the existing provision for current payments to assure parallel treatment.*

__________ Agree __________ Disagree ____________________________ Let's Discuss

3. <u>Enforcement</u>

- Support -- as the ultimate sanction -- application of Article XXVI[1] if obligations are not met under both Article VIII and Article XIV equivalents, as well as consideration of intermediate steps such as the publication of a report.[2]

  The application of the full range of sanctions to the Article XIV equivalent would be a departure from the present regime for current payments, the only sanction for which, in the IMF's view, is ineligibility to use IMF resources.

  We would, however, acknowledge that considerable discretion exists with respect to application of Article XXVI and note it has never been applied to breaches of Article VIII.

__________ Agree __________ Disagree ____________________________ Let's Discuss

4. <u>Approval Process</u>

A. Restrictions imposed for balance of payments or macroeconomic purposes

- Endorse staff's recommended approach that would provide for approval on determination that the restrictions are <u>needed</u> for the stated purpose, are <u>temporary</u> and do <u>not discriminate</u> among IMF members.

---

1 Comprising, progressively, ineligibility to use IMF resources, suspension of voting rights and expulsion.

2 Article XII (8) provides for such a published report, by a 70 percent weighted vote, "made to a member regarding its monetary or economic conditions and developments which directly tend to produce a serious disequilibrium in the international balance of payments of members." A comparable provision could be inserted in the article(s) governing restrictions on capital account transactions.

- o If such restrictions are imposed on an emergency basis after amended articles take effect, approval might be virtually automatic for a brief period (e.g., 30 days) on the representation of the country. Continued imposition could then require a more considered examination and approval (via a simple majority of the Board).

- o Existing restrictions for these purposes would require approval in advance of acceptance of the obligation for Article VIII equivalent countries, while all countries would require such approval for new restrictions.

The Board would have to develop criteria for granting approval – including whether fiscal and monetary/exchange rate policies were consistent with macroeconomic objectives or being appropriately adjusted.

IMF staff suggest greater tolerance for restrictions on short-term speculative flows and the use of price-based, transparent measures. This is probably an allusion to Chile's controls, although it is difficult to see how they could meet the "temporary" test – i.e., unless the Board developed criteria providing for a more permanent form of approval, Chile would likely opt for transitional status. Similarly, Singaporean-like controls on non-residents' ability to borrow local currency above a de minimus level without proof of an underlying commercial or financial transaction would probably cause countries imposing them to take transitional status.

__________ Agree __________ Disagree __________________________ Let's Discuss

B. Restrictions Imposed for Other Purposes

- Support broad scope for the liberalization obligation rather than strict limitation of IMF's role to restrictions for macroeconomic and balance of payments purposes. Permit exceptions only as specified in the amended articles or, preferably, Executive Board decisions rather than self-executing. See discussion of specific categories in (5) below.

- Express preference for decisions on the basis of normal (i.e., approval requiring 50 percent of voting power) rather than qualified (e.g., 70 percent majority required to disapprove) but be ready to consider issue further.

There is considerable sentiment in the Executive Board in favor of creating obligations only on those restrictions imposed for macroeconomic/balance of payments purposes. However, a blanket, self-executing exclusion of other restrictions would create huge loopholes. At the same time, we must be certain that our own restrictions would pass muster, so we could achieve Article VIII equivalent status. Finding the correct balance between these various considerations is probably our greatest challenge.

It is preferable to specify grounds for exceptions in Board decisions rather than in the amended articles, largely on the grounds that drafting provisions for the articles, which could not subsequently be changed without another amendment, would be more difficult and reduce the scope to reflect new developments. However, we should indicate a willingness to consider the issue further.

Provision for qualified majorities would have to be made in the amended articles.

__________ Agree __________ Disagree ____________________ Let's Discuss

- Resist staff's proposal providing for limited approval of restrictions for market and institutional evolution reasons.

  IMF staff argue that less advanced countries need scope to impose restrictions after a new financial market or instrument emerges for structural reasons. However, unless convincing arguments to the contrary can be mounted, the transitional provisions (see below) should provide sufficient protection.

__________ Agree __________ Disagree ____________________ Let's Discuss

5. Exceptions from Normal Approval Procedures

National Security

- Be prepared to accept approach now afforded to national security motivated restrictions on current operations -- whereby they are *de jure* subject to approval but are traditionally approved on a lapse of time basis in accordance with a 1952 Board decision -- i.e., via a separate decision that could take effect with the amended articles. However, support greater protection if suggested by others.

  In the 1952 decision, the Executive Board conceded that the IMF lacked competence to assess such restrictions and provided for automatic approval on a lapse of time basis. While the decision retains the possibility of the IMF's objecting to them, this has never been done.

Choosing this approach would imply a readiness to accept comparable procedures for remaining categories.

_________ Agree __________ Disagree __________________________ Let's Discuss

Prudential

- Support approach similar to that adopted for national security restrictions but with greater scope for challenging assertions of prudential motivation.

  The challenge here is to ensure that countries have reasonable scope for the application of prudential measures such as the SEC's registration and disclosure requirements, or our entry requirements for foreign banks, without creating too large a loophole for disguised protection. We have not yet determined how best to do so, and will need to work closely with the Fed and the SEC to design something with the right balance.

_________ Agree __________ Disagree __________________________ Let's Discuss

Restrictions by Subnational Governments

- Seek definition of restrictions that would exclude those imposed by subnational governments (e.g., individual U.S. states). If pressed, agree to consider provisions for communication of IMF's views and "best efforts" by national governments to achieve removal of restrictions.

  Individual U.S. states' restrictions are generally prudential in nature, would relate to national treatment issues or would fall under a possible broad right of establishment exception to inward DI. However, some could fall outside these categories. Also, at least in the financial services area, some states maintain reciprocity provisions that would be contrary to the MFN principle we are seeking.

_________ Agree __________ Disagree __________________________ Let's Discuss

6. Inward Direct Investment

- Preserve some role for the IMF with respect to restrictions on inward DI regardless of purpose (i.e., not just for balance of payments or macroeconomic purposes). However, leave open for now whether to achieve this objective via

  o an approval requirement as for other restrictions, but with criteria for approving non-bop/macro restrictions analogous to those for exceptions discussed under (5) above; or

  o permitting countries to claim an exception on the grounds that the restrictions are not for bop/macro purposes, subject to the right of IMF to challenge that assertion

  depending on the nature and workability of the respective criteria for the "approval" and "challenge" approaches (they could turn out to be much the same in practice -- although for negotiating purposes we should express a preference for the "approval" approach).

- Consider provisions that would defer to other organizations (WTO, MAI) if the potential for conflict exists and if something reasonable and feasible could be drafted, either in the amended articles or Board decisions.

The next Board discussion (August 26) will be reconsidering the coverage of inward DI. IMF staff, with the support of most Executive Directors, initially proposed exclusion of inward DI from the IMF's jurisdiction in order to avoid the complex, often political issues entailed and to avoid potential conflict with the WTO and MAI. These are legitimate concerns; however, total exclusion would leave some gaps (given the limited coverage of the WTO and limited membership of the MAI) and omit a category of capital flows that is central to economic development. Exclusion would also constrain information gathering and the ability to require MFN treatment. Finally, excluding inward DI would require drafting a precise definition of such a category in the amended articles -- discussion to date indicates that this would be a difficult task.

Partial exclusion, e.g., of "right of establishment" restrictions such as licensing requirements applied to residents as well as non-residents, could make the "approval" approach more acceptable (it would probably not be necessary for the "challenge" approach), but would still pose definitional problems.

Other countries would likely try to justify many of their restrictions on inward DI flows on national security or prudential grounds, in order to be accorded less onerous treatment as outlined in (5) above. However, it would be difficult to justify many U.S. restrictions on either basis. Most other restrictions not justifiable on these grounds probably reflect a desire to protect "independence" in critical industries, e.g., cultural;

they could also be granted some special consideration, although we have more to lose as U.S. firms are frequently targets of such restrictions.

Some restrictions may be based on macroeconomic or balance of payments reasons, although such cases are likely to be limited. The French and Belgian Executive Directors proposed that this category be subject to IMF approval, and that the IMF could challenge assertions that restrictions were for other purposes (e.g., national security, prudential).

__________ Agree __________ Disagree ________________________ Let's Discuss

7. Implications for IMF Financing

- Reject assertions that capital account liberalization will require greater use of IMF financing, but support revision of Article VI to remove prohibition of financing a large capital outflow. (The provision now refers to "large or sustained outflow of capital . . .")

- Continue to advance U.S. proposal to limit excessive use of resources via a price-based measure such as a surcharge on large use of IMF resources, but be prepared to accept revision of existing text to read "large and sustained . . ."

The Japanese and some European EDs have argued for retention of the "large or sustained" phrase. However, Mexico is a prime example of the need to allow for the possibility of financing large capital outflows. There are sufficient safeguards under Article V (e.g., authorizing policies "that will establish adequate safeguards for the temporary use of the general resources of the Fund") to justify deletion of this provision of Article VI.

__________ Agree __________ Disagree ________________________ Let's Discuss

8. <u>IMF's Ability to Request Imposition of Capital Controls</u>

This question is linked to (7) above, as the IMF's right to request imposition of capital controls must be aimed at preventing use of IMF resources to finance the "large or sustained" capital outflows referenced above.

- Favor retention of the provision in Article VI that "the Fund may request a member to exercise controls to prevent such use of the general resources of the Fund". However, be prepared to accept deletion if necessary to reach a consensus, <u>provided</u> that deletion would not impede the Fund from requiring imposition of controls as part of the conditions for an IMF program.

__________ Agree ___________ Disagree _____________________________ Let's Discuss

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DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
004. speech	re: Concluding Remarks by Acting Chairman on Capital Movements at Executive Board Meeting (IMF document) (6 pages)	07/18/97	P1/b(1) Unclass.

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DEPARTMENT OF THE TREASURY
Washington

July 17, 1997

TO: Deputy Secretary Summers
Assistant Secretary Lipton

FROM: Timothy Geithner TFG

SUBJECT: Capital Account Liberalization and the IMF

Ms. Lissakers and Mr. Newman provided the attached cogent summary of the state of the debate in the IMF. In general, this is moving in a direction we can support, but there are still large gaps on key substantive issues. Camdessus' objective of agreement on principles by Hong Kong may be met only with a very general statement, but this is better than trying to force agreement now on a less desirable outcome.

cc: Atkinson, Lissakers, Lister

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DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
005. memo	Karin Lissakers & Barry Newman (IMF) to Tim Geithner re: Capital Movements Amendment (4 pages)	07/16/97	P1/b(1) unclass.

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006. memo	Barry S. Newman to David Lipton & Tim Geithner re: Capital Movement Amendment (2 pages)	07/01/97	P1/b(1) Unclass.

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TREASURY CLEARANCE SHEET

NO.______
DATE:______

MEMORANDUM FOR: ☐ SECRETARY ☐ DEPUTY SECRETARY ☐ EXECUTIVE SECRETARY

☐ ACTION ☐ BRIEFING ☐ INFORMATION ☐ LEGISLATION

☐ PRESS RELEASE ☐ PUBLICATION ☐ REGULATION ☐ SPEECH

☐ TESTIMONY ☐ OTHER ______________

FROM: Senior Deputy Assistant Secretary Geithner
THROUGH:
SUBJECT: Capital Account Transactions and Amendment of IMF Articles

REVIEW OFFICES (Check when office clears)

☐ Under Secretary for Finance
☐ Domestic Finance
☐ Economic Policy
☐ Fiscal
☐ FMS
☐ Public Debt

☐ Under Secretary for International Affairs
☐ International Affairs

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☐ ATF
☐ Customs
☐ FLETC
☐ Secret Service
☐ General Counsel
☐ Inspector General
☐ IRS
☐ Legislative Affairs
☐ Management
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☐ Public Affairs/Liaison
☐ Tax Policy
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☐ E & P
☐ Mint
☐ Savings Bonds

☐ Other ______________

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REVIEWERS				
K. Lissakers/B. Newman	KL BN		USED/IMF	623-7759
C. Atkinson (DRAFT)			Senior Adviser (Intl. Affairs)	622-0489
R. Munk/A. Salladin	AWS		Asst. General Counsel (Intl.)	622-1899
M. Lundsager	ML		DAS Trade & Investment Policy	622-5304

SPECIAL INSTRUCTIONS

☐ Review Officer　　Date

☐ Executive Secretary　　Date

DO F 70-02.1 (04/89)

1997-SE-007687

DEPARTMENT OF THE TREASURY
Washington

July 17, 1997

TO: Deputy Secretary Summers
Assistant Secretary Lipton

FROM: Timothy Geithner TFG

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1997-SE-009807

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

9807

ACTION

September 11, 1997

MEMORANDUM FOR DEPUTY SECRETARY SUMMERS
ASSISTANT SECRETARY LIPTON

FROM: Timothy Geithner TFG
Senior Deputy Assistant Secretary for International Affairs

SUBJECT: IMF Quotas

The time has come to reach some final decisions on the basic parameters of the IMF quota increase if agreement is to be reached in Hong Kong. Attached is a background paper and tables on quota distribution which should facilitate consideration of this complex issue. This memo was prepared by Barry Newman and reflects the general views of Caroline Atkinson, Karin Lissakers, Barry and myself. We have consulted with Fed staff and they are comfortable with this approach.

The key issues are the following:

o Size: The likely negotiating range now appears to be an increase of 40-45 percent which would involve an increase in the U.S. quota of about $14-15 billion.

-- The lower end of the range would be more consistent with Hill perceptions of the U.S. position and the Fund's current financial position. Therefore, a 40 percent increase might be more acceptable.

-- The upper end of the range would be marginally more consistent with efforts to enhance the Fund's role in crisis resolution; create goodwill with other IMF members; and facilitate attainment of other Fund objectives.

Recommendation: The key is actually implementing whatever is agreed and therefore I favor sticking to the lower end of the range, while recognizing that we may move a little off 40 percent itself.

Agree ✓ Disagree ____

o Distribution: The U.S. could live with any of the distribution options currently on the table (which divide an overall increase into three parts: equiproportional based on current quotas, selective based on calculated quotas, and ad hoc). The LDCs strongly support a 75 percent equiproportional element while the European and Japanese focus on the size and distribution of the ad hoc

EXECUTIVE SECRETARIAT

increase. The U.S. objective of enhancing the position of the emerging Asian economies could be achieved either by concentrating the ad hoc increase on those countries most out of line, which include Singapore, Korea, Malaysia, Thailand, or providing these Asians a special increase on top of the general increase (see Table 1). I believe that the first is preferable, given the difficulty of justifying a further special increase for these four countries and not others, and to minimize the China problem. However, this would likely be opposed by France, the smaller Europeans and Canada as it excludes them from an ad hoc increase.

Recommendation: That we support a distribution formula that favors the Asians even if it comes at the expense of the smaller European countries and Canada. The cleanest way to accomplish this is with a distribution of 75 percent equiproportional, 15 percent selective, and 10 percent ad hoc with a cut-off of 1.3 (i.e., only those countries whose calculated quotas are now 1.3 or more times their current actual shares would benefit). We should oppose a special additional increase for the four Asians.

Agree ✓ Disagree ______

o China: The Executive Board at lunch on September 11 agreed to defer China's request for a special quota increase based on the Hong Kong reversion until the next review of quotas. The Chinese have indicated privately that they do not intend to make a big push on this issue at Hong Kong; however, we need to be careful not to let this understanding unwind at the meetings.

Recommendation: That the U.S. be prepared, if necessary, to express opposition to a special increase for China now or to a commitment to provide them one anytime in the near future.

Agree ✓ Disagree ______

o Access: The IMF traditionally reduces the access limits (presently 100 percent of quota annually and 300 percent for outstanding loans) when quotas increase, in order to keep access in absolute amounts constant for the membership as a whole. This makes little sense in the context of today's capital markets and would force the Fund to rely increasingly on the exceptional access provisions to deal with financial crises. We favor no change in the access limits, thereby permitting the absolute size of Fund programs to increase. The Europeans, particularly the Germans, can be expected to oppose.

Recommendation: That we side with those who favor retaining the current access limits following the quota increase.

Agree ✓ Disagree ______

IMF Quota Distribution Issues

General Approach

- o There is broad agreement on the general approach for distributing the quota increase.

  -- an **equiproportional** element provided to all members on the basis of **current** quota shares,

  -- a **selective** element provided to all members on the basis of **calculated** quota shares; and

  -- an **ad hoc** element provided to **a subset** of the members which have calculated shares exceeding current shares.

- o However, there is continuing, albeit narrower, disagreement over the magnitude of each of the elements and which countries should receive the ad hoc increase.

Country Positions

- o United States: We have argued that the bulk of the increase should be distributed equiproportionally and have expressed sympathy for the position of developing countries. A high equiproportional element would tend to limit any U.S. share loss although we would not lose much from a smaller equiproportional and larger selective as our actual and calculated quota shares are similar. A large ad hoc element would, however, impact our quota share as we would not be a recipient.

- o Developing countries: They are insisting that at least 75 percent of the increase be distributed equiproportionally to minimize their share losses. They also prefer a small ad hoc for the same reason.

- o Germany/Japan: They support a lower equiproportional increase of 70 percent in order to provide greater scope for share adjustments through the selective and ad hoc elements. They have differed in the past, however, over the size and distribution of the ad hoc increase.

  -- The Germans have favored an ad hoc of 10 percent which would be provided to all countries with a ratio of calculated to actual quota shares exceeding 1.0. This would provide ad hoc increases to 37 countries, including a wide range of European members.

- -- The Japanese have also favored an ad hoc of 10 percent but with a higher cut-off ratio of 1.3 which would reduce the number of eligible countries to 21 and concentrate more of the benefits on Asian countries, including Japan. They have even indicated a willingness to consider a smaller ad hoc that would be provided to even fewer countries.

- -- We understand that the Germans and Japanese have discussed the possibility of supporting a 10 percent ad hoc with a cut-off of 1.0 and a further special increase for Korea and possibly a few other Asian countries.

<u>Asian country problem</u>

o Some of the fast growing Asian countries will obtain substantial increases in quota share as part of the current review under any of the proposals currently on the table (i.e., Singapore, Korea, Thailand, Malaysia).

o However, others in the region will experience share losses (i.e., China, Philippines, Indonesia).

o It has been suggested, nevertheless, that the increased role of these countries in the world economy would not be adequately addressed by the general distribution approaches and that further special measures should be taken. In particular, Japan suggested a special increase for Korea as part of a bargain with the Europeans on the size and distribution of the ad hoc, although the Japanese now seem to be pulling back somewhat and may be amenable to a higher cut-off.

o Suggestions for maximizing the gains for the first group are:

- -- An increase in the cut-off ratio for the ad hoc increase would benefit those countries with high ratios but is opposed by the Europeans because it would reduce their increase (it would have no effect on the U.S., U.K., and developing/transition countries which do not receive ad hoc increase).

- -- A special increase for selected Asian countries on top of the general increase applied to all members.

- -- A difficulty, however, is deciding on which countries should receive the special increase given their disparate situations and the fact that other non-Asian countries also have high calculated to actual quota ratios (i.e., Luxembourg, Botswana, Bahrain, Oman, San Marino).

China

- o The Chinese have made a formal request for a special quota increase to reflect the Hong Kong reversion.

  -- They are concerned that the loss of quota share that would otherwise occur because their current share is above calculated could threaten their ability to retain a seat on the IMF Executive Board.

  -- However, a Chinese increase based on Hong Kong reversion would appear inconsistent with the one country, two system agreement and could create difficult congressional problems.

  -- The Executive Board at lunch on September 11 agreed to defer the Chinese request until the next review of quotas. The Chinese have indicated privately that they do not intend to make a big push on this issue at the Annual Meetings; however, we need to be careful not to let this understanding unwind at Kong Kong.

Timing of special increase

- o A closely related issue is whether any special increase for some Asian countries should be included as part of the current review or decided separately after the review is completed.

  -- Special treatment for Asia as part of the current review would increase pressure from China for similar treatment and complicate completion of the quota negotiations and eventual implementation.

  -- Special increases separate from and later than the general review could maximize U.S. leverage in obtaining other objectives, e.g., in the financial area (a special increase outside a general review requires a decision by an 85 percent majority vote and is thus subject to the U.S. veto).

  -- Moreover, a separate special increase does not require congressional approval as no change in the U.S. quota is involved.

TABLE I. Countries with IMF Calculated Quotas Above Current Quotas
(Ranked by Excess Over Present Quotas)

	Ratio of Calculated to Present Quota Shares
Singapore	6.41
Luxembourg	3.13
Korea	3.04
Botswana	2.63
San Marino	2.43
Thailand	2.19
Bahrain	1.90
Oman	1.90
Malaysia	1.81
Japan	1.76
Ireland	1.69
Antigua and Barbuda	1.63
Germany	1.60
Austria	1.57
Spain	1.55
Turkmenistan	1.49
United Arab Emirates	1.49
Portugal	1.46
Slovenia	1.38
Italy	1.36
Denmark	1.36
Norway	1.26
Malta	1.25
Turkey	1.21
Netherlands	1.16
Maldives	1.16
Belgium	1.14
Sweden	1.14
Mexico	1.10
Seychelles	1.10
Kazakstan	1.09
France	1.09
Canada	1.08
Finland	1.08
Congo, Rep. of	1.06
Lesotho	1.05

Table 2

Illustrative Quota Shares Under Various
Overall Increases and Distribution Approaches [1]

Country (current share)	35 percent increase 75/15/10 (1.0)	35 percent increase 75/15/10 (1.3)	35 percent increase 70/20/10 (1.0)	45 percent increase 75/15/10 (1.0)	45 percent increase 75/15/10 (1.3)	45 percent increase 70/20/10 (1.0)
G-7						
U.S. (18.363)	17.843	17.744	17.831	17.737	17.618	17.723
Germany (5.705)	6.189	6.288	6.233	6.283	6.387	6.336
Japan (5.705)	6.283	6.545	6.339	6.397	6.696	6.464
France (5.133)	5.214	5.147	5.219	5.227	5.151	5.234
U.K. (5.133)	5.032	5.032	5.032	5.032	5.032	5.032
Italy (3.178)	3.358	3.266	3.373	3.391	3.279	3.409
Canada (2.991)	3.035	2.999	3.038	3.042	3.000	3.046
Asian						
China (2.343)	2.256	2.243	2.247	2.238	2.223	2.228
Korea (0.554)	0.662	0.778	0.677	0.685	0.833	0.703
Singapore (0.248)	0.338	0.436	0.355	0.357	0.494	0.377
Malaysia (0.576)	0.637	0.669	0.644	0.650	0.686	0.657
Thailand (0.397)	0.452	0.496	0.458	0.463	0.517	0.471
Philippines (0.438)	0.423	0.421	0.422	0.420	0.417	0.419
Indonesia (1.037)	1.000	0.995	0.997	0.993	0.986	0.989
Other						
Russia (2.986)	2.862	2.846	2.847	2.837	2.818	2.819
Saudi Arabia (3.552)	3.372	3.353	3.343	3.336	3.313	3.301
India (2.115)	2.007	1.996	1.990	1.985	1.972	1.965
Mexico (1.214)	1.236	1.218	1.238	1.240	1.219	1.242
Brazil (1.503)	1.459	1.450	1.457	1.450	1.440	1.448
Spain (1.340)	1.445	1.454	1.454	1.465	1.473	1.476

[1] Equiproportional/selective/ad hoc (cut-off) with caps and floors so that share adjustments do not cause a widening of the divergence between calculated and actual shares.

September 10, 1997