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SM/84/89
Correction 1

May 15, 1984

To: Members of the Executive Board
From: The Secretary
Subject: The Role of the Fund in the Settlement of Disputes Between
Members Relating to External Financial Obligations

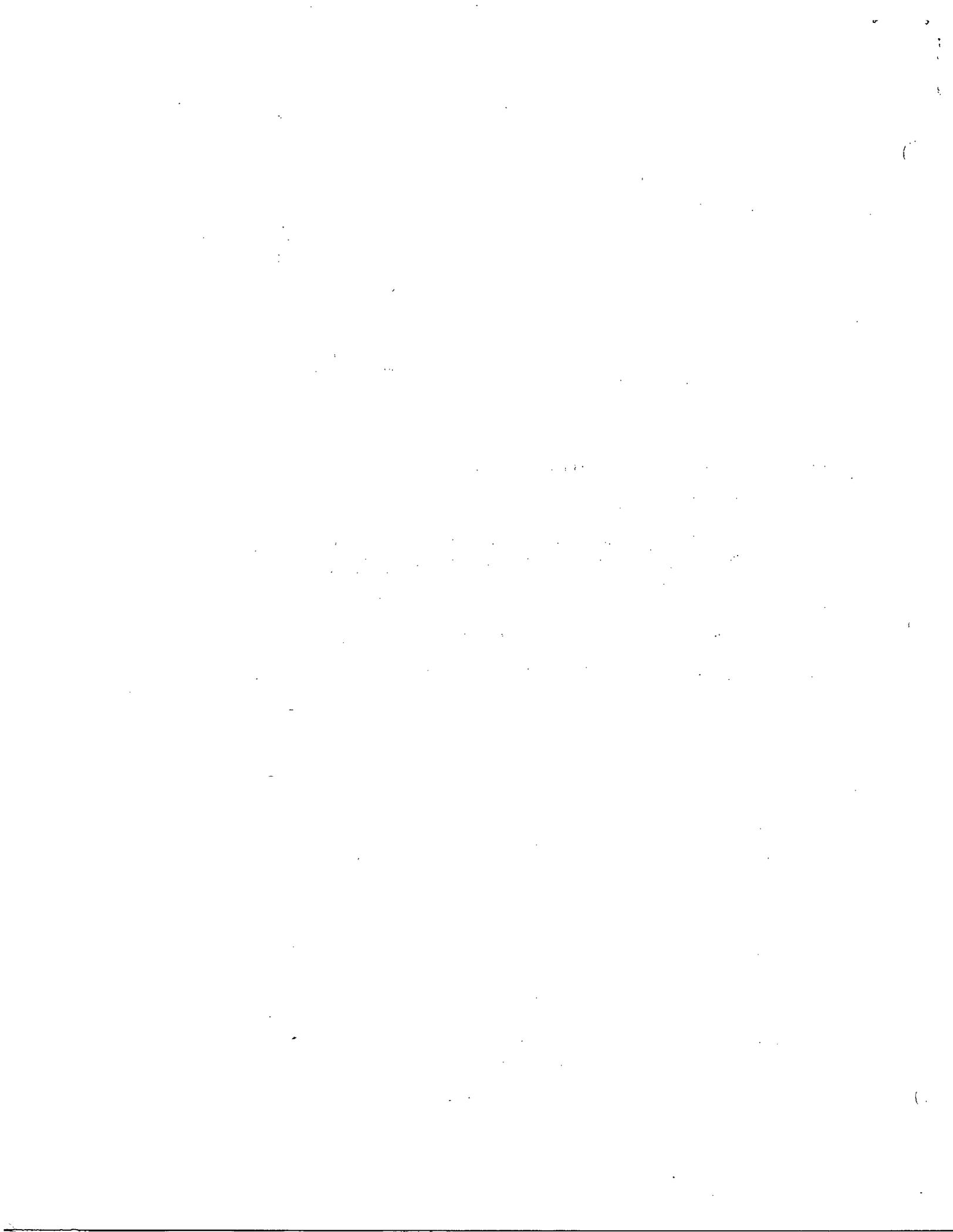
The following correction has been made in SM/84/89 (4/25/84):

Page 8, first full para., last line: for "EBS/80/90" read "EBS/80/190"

A corrected page is attached.

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In this process of consultation, and in the context of the exercise of the Fund's jurisdiction, national authorities, as well as particular creditors, frequently inform the Fund about unsettled external financial obligations. Often, nongovernmental creditors have contacted the Fund's management and staff regarding unpaid financial claims and requesting Fund assistance; in these types of cases the petitioner is normally informed that the Fund cannot be of assistance. 1/ When, however, the member is the creditor, or when a member decides to espouse the claims of a nongovernmental creditor, the matter might be pursued either informally with the Fund's management and staff or by raising the matter for consideration by the Executive Board. It is also open to a member to lodge a complaint to the Executive Board under Rules H-2 and H-3 if another member is in breach of its obligations concerning exchange controls. 2/

Despite this general involvement of the Fund in situations involving overdue external obligations, in the context of the exercise of its jurisdiction under Articles VIII and XIV, certain additional qualifications need to be added. As noted in Section II above, a debtor's nonpayment of an external obligation may be due to a wide variety of causes, and the Fund is clearly limited in its capacity to examine each factual situation in order to determine the cause of nonpayment of a particular external obligation. The Fund does, however, examine the circumstances of an exchange measure, including its implementation, so that it can be decided whether or not an exchange restriction exists. In doing so, however, two additional inhibitions qualify the exercise of the Fund's jurisdiction over exchange restrictions.

First, the Fund has found it necessary, in the exercise of its jurisdiction, to distinguish between nonpayment of obligations because of exchange restrictions, on the one side, and nonpayment of obligations that are to be treated as defaults, on the other side. Thus a member's refusal to make payments according to its own contractual commitments that it has undertaken in connection with current international transactions would be classified as a default and not a restriction, except

1/ In the context of judicial and administrative proceedings involving the application of Article VIII, Section 2(b) of the Articles of Agreement, the Executive Board has decided that the Fund "is prepared to advise whether particular exchange control regulations are maintained or imposed consistently with the Fund Agreement". (Executive Board Decision No. 446-4, adopted June 10, 1949, Selected Decisions, Tenth Issue, p. 233.)

2/ "H-2. If a member complains to the Executive Board that another member is not complying with its obligations concerning exchange controls, discriminatory currency arrangements, or multiple currency practices, the complaint shall give all facts pertinent to an examination.

H-3. Upon receipt of a complaint from a member, the Executive Board shall make arrangements promptly for consultation with the members directly involved."

insofar as the refusal is made in the context of a restrictive system applicable to all such payments, when the nonpayment of a foreign obligation by the government or one of its agencies would constitute an exchange measure subject to the Fund's jurisdiction. In the 1980 Executive Board paper on payments arrears, the category of default was extended to governmental obligations as follows:

"There are payments arrears which do not result from governmentally imposed delays on payments and transfers for current international transactions. Such arrears may arise when a government or government entity whose financial operations form part of the budgetary process fails to meet an external payments obligation. It is difficult to treat these arrears as coming within the jurisdiction of the Fund although their economic effects are the same as those that involve exchange restrictions. Such arrears should therefore be treated as a default. On the other hand, where a public sector entity is clearly independent of the government's day-to-day budgetary controls and has at its disposal domestic currency resources with which to meet its external payments obligations, payments arrears which arise because of an inability to obtain the requisite foreign exchange are evidence of an exchange restriction. The financing arrangements of public entities and the relationship of these entities to the central government therefore need to be examined on a case-by-case basis to arrive at the correct determination." (EBS/80/190, (8/27/80), p. 9.)

A second qualification to the exercise of the Fund's jurisdiction must be added: according to current Fund practice, in situations where a debtor disputes the validity of an external financial obligation, or some feature of it, the Fund is not in a position to determine whether there is or is not a particular payments arrear and the Fund ceases to have a role under its Article VIII approval jurisdiction. In such situations, furthermore, the Fund has taken the view that a member's representation that the debtor disputes the validity of an obligation should be taken as being made bona fide and accepted on that basis. Nonetheless, the Fund retains the right to conclude that the debtor's contention is clearly without merit and that, therefore, the dispute should not have the effect of removing the related nonpayment from the Fund's jurisdiction.

In summary, in terms of the jurisdiction of the Fund under Article VIII, it is apparent that the Fund is called upon to examine situations of overdue external financial obligations. This involves the Fund in a continuing dialogue with members. In applying Fund policy on payments arrears, the Fund must determine, as for other exchange measures, whether or not an exchange restriction subject to Fund jurisdiction is involved, in which case the Fund's policies for approval come into play. As already noted, in many situations concerning external financial obligations the matter will be subject to Fund jurisdiction under Article VIII,