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MAINTENANCE OF VALUE (MOV) AND THE SDR
IN THE MULTILATERAL DEVELOPMENT BANKS (MDBs)

Fluctuations in the exchange rates of member countries in the multilateral development banks have several consequences. First, the SDR value of an MDB's total capital may change (Section I). Second, the absolute value in SDRs of members' capital will change (Section II) and therefore relative shares will (Section III).

I. Total Capital

It could be argued that MDB capital should be valued in terms of the SDR. The composition of the SDR is such that fluctuations in constituent currencies tend to average out -- the SDR is an automatic maintenance of value device which dampens fluctuations in the SDR value of MDB capital. ?

Tables 1-6 demonstrate this conclusively. The percent change in the dollar price of the SDR resulting from a ten percent change in any one currency relative to all others is shown in Table 1. Exchange rates were taken as of end

Table 1

A 10 Percent Increase in This Currency	Changes the $ Price of the SDR this Percent	From $1.2147 To
US $	- 6.1	1.1406
Mark	+ 1.5	1.2328
Yen	+ 0.9	1.2255
Franc	+ 0.8	1.2241
Pound	+ 0.7	1.2233
Canadian $	+ 0.5	1.2212

December 1977, when the dollar value of one unit of each currency in the SDR basket was as shown in the following table:

Table 2

Exchange Rates in Dollars, 12/31/77

Mark	.4750	S. kronor	.2141
Pound	1.9060	A $	1.0864
F. Franc	.2125	D. kroner	.1730
Yen	.004167	N. kroner	.1945
C $	.9137	peseta	.0123
Lira	.001147	Aust. schilling	.0660
Guilder	.4385	Rand	1.1500
B. Franc	.0303		

To say any of the currencies in the table appreciates 10 percent relative to all others means that only one entry in the table above increases. A 10 percent increase in the dollar, on the other hand, means that every entry in the table decreases.

It is unrealistic to believe that only one currency will change at one time, or that the change will be as large as 10 percent. ? However, "ceteris paribus" assumptions must be made, and the assumption holding all currencies but one constant is particularly convenient. The effects of smaller fluctuations should be roughly proportional to those shown, and the effects of several currencies fluctuating at once will be approximately additive.

Why not take actual rates over period since SDR

Table 1 shows that changes in the U.S. dollar have the most dramatic impact on the SDR: the dollar price of the SDR drops over 6 percent for every 10 percent increase in the dollar relative to all other currencies.

The impact of a ten percent appreciation in major currencies relative to all others on the total capital of the IBRD, IDA, and ADB is calculated in Tables 3, 4 and 5, respectively. The results are summarized in Table 6. The general rule is that if a currency has a greater weight in the SDR than in one of the MDBs, an increase in that currency relative to
in $ terms
all others will decrease the SDR value of that MDB's capital. For example, the mark has a greater weight in the SDR than in the IBRD. Table 3 shows that a 10 percent increase in the mark relative to all other currencies would decrease the SDR value of the IBRD's capital by about 0.9 percent.

Conversely, if a currency has a smaller weight in the SDR than in an MDB, an increase in the currency will increase the SDR value of the MDB's capital. For example, the dollar has a smaller weight in the SDR than in the IDB. Table 4 shows that a ten percent increase in the dollar relative to all other currencies would increase the SDR value of the IDB's capital by about 0.3 percent.

The closer a currency's weight in the SDR is to that country's share in an MDB, the less effect fluctuations in

Table 3

The SDR Value of IBRD Capital
with Exchange Rate Changes

		SDR Capital after 10 percent appreciation in currency shown relative to all others					
Country	SDR Capital *	U.S. $	Mark	Yen	Franc	Pound	C $
	SDR = $1.2147	SDR = $1.1406	SDR = $1.2328	SDR = $1.2255	SDR = $1.2241	SDR = $1.2233	SDR = $1.2212
Canada	1105	1070	1089	1096	1097	1098	1209
France	1556	1507	1534	1542	1699	1545	1548
Germany	1739	1684	1885	1724	1725	1726	1730
Japan	1345	1303	1325	1467	1334	1336	1337
U.K.	2582	2499	2544	2559	2562	2820	2568
U.S.	7720	8220	7606	7651	7659	7664	7678
All Others	16224	15708	15986	16081	16099	16111	16138
Total	32271	31991	31969	32120	32175	32300	32208
% Δ		-.9	-.9	-.5	-.3	+.1	-.2

* Capital upon completion of current capital increase valued in SDRs as of 12/31/77.

Table 4

The SDR Value o. IDB Capital
with Exchange Rate Changes

SDR Capital at 10 percent appreciation in currency shown relative to all others

Country	SDR Capital* 12/31/77	U.S. $	Mark	Yen	Franc	Pound	C $
	SDR - $1.2147	SDR = $1.1406	SDR = $1.2328	SDR = $1.2255	SDR = $1.2241	SDR = $1.2233	SDR = $1.2212
Argentina	1161	1124	1144	1150	1152	1153	1154
Brazil	1161	1124	1144	1150	1152	1153	1154
Mexico	746	724	735	739	741	741	742
Venezuela	621	601	612	616	616	617	617
Canada	454	440	447	450	450	451	497
U.K.	58	56	56	58	58	63	58
France	58	58	58	58	65	58	58
Germany	59	57	64	59	59	59	59
Japan	64	62	62	69	64	64	64
U.S.	3354	3571	3304	3325	3329	3330	3336
Others	1879	1819	1851	1862	1865	1865	1869
Total	9615	9636	9477	9536	9551	9554	9608
$Δ		+.3	-1.4	-.8	-.6	-.6	-

* Capital upon completion of current capital increase valued in SDRs as of 12/31/77.

The SDR Value of ADB Capital with Exchange Rate Changes

Country	SDR Capital*	SDR Capital after 10 percent appreciation in currency shown relative to all others					
		U.S.$	Mark	Yen	Franc	Pound	C $
	SDR = $1.2147	SDR = $1.1406	SDR = $1.2328	SDR = $1.2255	SDR = $1,2241	SDR = $1.2233	SDR = $1.2212
Japan	1166	1129	1149	1271	1157	1158	1160
Canada	447	433	440	442	445	445	489
France	146	142	144	144	158	146	146
Germany	370	358	402	367	367	367	368
U.K.	175	171	173	173	173	192	175
U.S.	1166	1242	1149	1156	1157	1158	1160
All Others	3686	3566	3629	3656	3659	3657	3664
Total	7156	7041	7086	7209	7116	7123	7162
%Δ		-1.6	-1.0	+.7	-.6	-.5	+.1

* Capital upon completion of current capital increase valued in SDRs as of 12/31/77.

in that currency have on the SDR value of the MDBs capital. For example, the Canadian dollar weight in the SDR is so close to Canada's share of the IDB that even a 10 percent change in the Canadian dollar relative to all other currencies has no effect on the SDR value of the IDB's capital. On the other hand, changes in the mark or yen have a more pronounced effect on the SDR value of the IDBs' capital than fluctuations in other currencies because there is a greater difference in their shares of the SDR and IDB.

Table 6 in $ terms

A 10 percent Increase in This Currency	Changes the ~~SDR Value~~ of IBRD Capital	Changes the SDR Value of IDB Capital	Changes the ~~SDR Value~~ of ADB Capital
Dollar	-.9	+0.3	-1.6
Mark	-.9	-1.4	-1.0
Yen	-.5	-0.8	+0.7
Franc	-.3	-0.6	-0.6
Pound	+.1	-0.6	-0.5
Canadian $	-.2	-0.0	+0.1

All figures as of completion of current capital increases.

Some significant conclusions may be drawn from these tables:

A. Even large exchange rate changes have a miniscule impact on the SDR value of MDB capital. Accountants and bondholders need have no fear that if current MOV arrangements are terminated capital would fluctuate wildly.

But what about effects LDC collateral

B. In the IDB, the European currencies and the yen are of very limited importance to the institution, but they have a more significant impact on the SDR value of IDB capital than the U.S. or Canadian dollars. Note that even so the impact of these currency fluctuations is very small. Appreciation in the mark, yen, franc, or pound would nevertheless obligate MOV payments by all Western Hemisphere members.

C. In the ADB, both an increase in the yen and a decline in the dollar increase the SDR value of capital. If the ADB chooses to maintain the SDR value of capital in these circumstances, it must pay out more than it collects. A strong yen and weak dollar decapitalizes the ADB in terms of dollars. Again, the amounts are small even for large exchange rate changes.

To conclude this section: the SDR could be an automatic stabilizer for valuing MDB capital. MOV is not required to maintain the SDR value of MDB capital.

II. Absolute Country Shares

The previous section concluded that if MDB capital is valued in SDRs, MOV is not necessary to stem undesirable fluctuations in the SDR value of capital. The question of equity among countries remains, however. Tables 3, 4 and 5 illustrate the changes which would take place in members' capital shares given a 10 percent increase in any of the major currencies. If MOV applied to all capital, MOV payments required may be calculated by subtracting the SDR value of a member's capital as of the base date from the SDR value of its capital after the exchange rate change.

For example, Table 3 shows that a 10 percent increase in the mark relative to all other currencies would increase the SDR value of Germany's capital in the IBRD by SDR 146 million but decrease the value of the UK's capital SDR 38 million. Germany would receive that amount, but the U.K. (and all other members) would pay. Changes in the U.S. dollar have the largest absolute impact: a ten percent increase in the dollar would increase the SDR value of U.S. capital by a half billion SDR.

In the IDB changes in the U.S. and Canadian dollars have the biggest absolute impact. But the European currencies and yen could also change the SDR value of member shares. For example, if MOV were retained with the SDR as unit of value, a ten percent appreciation in the mark relative to all other currencies would obligate MOV payments of SDR 17 million by Argentina and Brazil, SDR 11 million by Mexico, and SDR 9 million by Venezuela, even though Germany has only a one-half of one percent share of the IDB's capital (see Table 4).

If [illegible], then shares so drawn

In the ADB the yen and U.S. dollar are the most important, as Table 5 shows.

If MOV applied only to the 9 percent of MDB stock which is paid-in but not in gold, the MOV amounts would be only 9 percent of the differences calculated as above.

III. Relative Member Shares

Changes in relative values of member shares in the MDBs are also of interest. Conclusions on relative shares can be drawn from Tables 3, 4 and 5, but for convenience selected figures have been expressed as percentages in Tables 7, 8 and 9.

Table 7 shows that a ten percent increase in the dollar would increase the U.S. share of the IBRD's capital from 23.9 percent to about 25.7 percent; all other members would split 74.3 percent instead of 76.1 percent. A ten percent increase in the mark would increase Germany's share from 5.4 percent to 5.9 percent but leave the U.S.

?

But the US would then [illegible] [illegible] + its share would remain

Table 8

IDB: Relative Member Shares
and Exchange Rate Changes

Country	Share 12/31/77	U.S. $	Mark	Yen	Franc	Pound	C $
		Share after 10 percent appreciationin currency shown.					
Canada	4.7	4.6	4.7	4.7	4.7	4.7	5.2
U.K.	.6	.6	.6	.6	.6	.7	.6
France	.6	.6	.6	.6	.7	.6	.6
Germany	.6	.6	.7	.6	.6	.6	.6
Japan	.7	.6	.7	.7	.7	.7	.7
U.S.	35.0	37.0	34.9	34.9	34.9	34.9	34.7
her	57.9	56.0	57.8	57.9	57.8	57.8	57.6
	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Table 9

ADB: Relative Member Shares and Exchange Rate Changes

		Share after 10 percent appreciation in currency shown relative to all others					
Country	Share SDR=$1.2147	U.S.$ SDR = $1.1406	Mark SDR = $1.2328	Yen SDR = $1.2255	Franc SDR = $1.2241	Pound SDR = $1.2233	C $ SDR = $1.2212
apan	16.3	16.0	16.2	17.6	16.3	16.3	16.2
anada	6.2	6.1	6.2	6.1	6.2	6.2	6.8
rance	2.0	2.0	2.0	2.0	2.2	2.0	2.0
ermany	5.2	5.1	5.6	5.1	5.2	5.2	5.1
.K.	2.4	2.4	2.4	2.4	2.4	2.7	2.4
.S.	16.3	17.6	16.2	16.0	16.3	16.3	16.2
thers	51.5	50.8	51.4	50.8	51.4	51.3	51.3
	100.0	100.0	100.0	100.0	100.0	100.0	100.0

share virtually unchanged. A ten percent increase in the yen or pound would increase the Japanese share from 4.2 percent to 4.6 percent and the British share from 8.0 percent to 8.7 percent, respectively. In either case the U.S. share would be relatively unaffected.

The conclusion is that only fluctuations in the dollar affect World Bank capital shares in any major way -- and even then the only share to be significantly altered is the U.S. share. Others simply aren't affected very much by changes in their own or any other currency. ?

In the IDB, a ten percent appreciation in the U.S. dollar would increase the value of the U.S. share by about 2 percentage points. Conversely, a depreciation of that magnitude would have the opposite effect. Changes in other currencies affect members' shares in the IDB to a much smaller degree. A ten percent appreciation in the Canadian dollar, for example, would raise Canada's share from 4.7 to 5.2 percent -- other members would split 94.8 percent instead of 95.3 percent. In the IDB as in the World Bank, only large fluctuations in the U.S. dollar have much impact on the relative SDR value of member capital shares.

In the ADB the situation is slightly different because Japan is also an important subscriber. A ten percent appreciation in the yen would increase Japan's share from 16.3 percent to 17.6 percent and reduce the share of other members accoordingly. A ten percent appreciation in the U.S. dollar would also raise the U.S. share from 16.3 to 17.6 percent. Note that these figures are as of completion of the present capital increase.

REC'D FROM E. MEIGHER 5/16/78

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

Notes to Financial Statements

June 30, 1978 and June 30, 1977 **Appendix G**

[New language underscored, deletions marked by -----]

UNDERSCORE ENTIRE PAGE

SUMMARY OF SIGNIFICANT ACCOUNTING AND RELATED POLICIES

CAPITAL STOCK

From ~~[illegible]~~ 1973 until March 31, 1978, the Bank's capital stock which is expressed in the Bank's Articles of Agreement in terms of "United States dollars of the weight and fineness in effect on July 1, 1944" (1944 dollars), has been translated by the Bank for purposes of its financial statements into current United States dollars at the rate of 1.20635 per 1944 dollar. That rate represented the par value of current United States dollars. Since the effectiveness on April 1, 1978, of the Second Amendment of the Articles of Agreement of the International Monetary Fund (the Fund), currencies no longer have par values in terms of gold. The Bank is examining the implications of this change on the valuation of its capital stock. No decisions on this matter have been taken. For purposes of the financial statementS for the year ending June 30, 1978, the Bank HAS ~~will~~ expressED the value of its capital stock on the basis of the Special Drawing Right (SDR) in terms of United States dollars as computed by the Fund ($ ____________ per SDR) on June 30, 1978. (See Note B . This note ~~will~~ also showS what the value of the Bank's capital stock would be as expressed in terms of $1.20635 equals one 1944 dollar.)

TRANSLATION OF CURRENCIES

The financial statements are expressed in ~~terms of the current~~ United States dollar solely for the purpose of summarizing the Bank's financial position and the results of its operations for the convenience of its members and other interested parties.

The Bank is an international organization which conducts its operations in the currencies of all of its members. The Bank's resources are derived from its capital, borrowings and accumulated earnings in the various currencies of its members and Switzerland and are held, invested or lent in those same currencies. The Bank matches its borrowing obligations in any one currency with assets in the same currency, as prescribed by its Articles of Agreement, by holding, investing or lending the proceeds of its borrowings in the same currencies in which they are borrowed. The Bank maintains a neutral currency position with respect to its other resources by not converting one currency into another except for insignificant amounts required to meet certain obligations and operational needs of the Bank.

In general, the Bank translates its assets and liabilities in currencies other than United States dollars at market rates of exchange to the United States dollar at the end of each fiscal quarter with the exception of buildings and deferred charges which are translated at exchange rates in effect when the buildings were acquired or the charges incurred. Income and expenses other than depreciation and amortization charges are translated at an average of the market rate of exchange in effect during each quarter. ~~The capital stock, which is expressed in terms of the United States dollar of the weight and fineness in effect on July 1, 1944 (the 1944 dollar), is translated by the Bank into current United States dollars at the rate of $1.20635 per 1944 dollar. (See Note B.)~~

Under the Bank's present policies, adjustments arising from the translation of currencies to the current United States dollar equivalent would not now or in the future result in realized gains or losses such as would result from the conversion of the various currencies into United States dollars. Accordingly, translation adjustments, with the exception of those relating to capital subscriptions described in Note B, are charged or credited to the General Reserve rather than income. (See Note A.) In those few instances where currencies are converted to another currency, the resulting gain or loss, if any, is included in the determination of net income.

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NOTE B - CAPITAL STOCK, RESTRICTED CURRENCIES AND MAINTENANCE OF VALUE

Capital Stock. In the Articles of Agreement, the capital stock of the Bank is expressed in terms of "United States dollars of the weight and fineness in effect on July 1, 1944" (1944 dollar). ~~It comprises 340,000 authorized shares (270,000 - 1976) of the par value of $100,000 each, of which 255,890 shares have been subscribed (255,818 - 1976). Ten percent of the capital subscriptions has been called and paid in; the remaining ninety percent is subject to call by the Bank only when required to meet the obligations of the Bank created by borrowing or by guaranteeing loans. As to $24,695,403,000 ($24,688,454,000 - 1976), the restriction on calls is imposed by the Articles of Agreement and, as to $3,086,925,000 ($3,086,057,000 - 1976), by resolutions of the Board of Governors.~~

On April 30, 1976, the Board of Governors of the ~~International Monetary~~ Fund ~~(the Fund)~~ approved proposed amendments to the Fund's Articles of Agreement (the Second Amendment) which ~~will become effective upon their acceptance by 60% of its members representing 80% of the voting power~~ entered into force on April 1, 1978. Under ~~these amendments~~ the Second Amendment, currencies ~~will~~ no longer have par values, gold ~~will be~~ is abolished as a common denominator of the monetary system and all calculations for the purposes of the Fund's Articles ~~will be~~ are made on the basis of the Special Drawing Right (SDR). ~~The United States has accepted these amendments which are not yet effective. Since July 1, 1974, the value of an SDR expressed in United States dollars has been based upon~~

~~the weighted relative values of a number of major currencies, including the United States dollar. This method of valuation will not be changed by these amendments. The Bank has under consideration the effect of these amendments on the valuation of the Bank's capital and the rights and obligations of members with respect thereto. If the SDR were to be substituted for the 1944 dollar in the Articles, it is not expected that this would have a material effect on the financial position or results of the operations of the Bank. Since the value of the SDR in terms of current dollars may vary from day to day and, therefore, may differ from the value of the 1944 dollar in terms of current dollars, as valued by the Bank, such a substitution might result in the amounts of the Bank's capital and subscriptions thereto expressed in current dollars varying from the amounts shown in these financial statements. If such a substitution were to have taken place at June 30, 1977, the Bank's capital expressed in current dollars would have been as follows subscribed $29,8333,319,000, uncalled $26,849,988,000 and paid in $2,983,331,000.~~ Since July 1, 1974, the value of an SDR in terms of United States dollars has been based on the weighted relative values of a number of major currencies, including the United States dollar (the basket). The value of the SDR on July 1, 1974, expressed in terms of United States dollars, was $1.20635,

which was the equivalent of one 1944 dollar. On March 31, 1978 the Fund made certain changes in the basket of currencies effective July 1, 1978 and established a method for further adjustment, at five-yearly intervals, to reflect changes in the relative importance of currencies over time, while ensuring continuity and reasonable predictability for the valuation of the SDR. The amounts of the currencies in the revised basket effective July 1, 1978, are such that the value of the revised basket in terms of any currency was exactly the same, at June 30, 1978, under the revised valuation as under the then existing valuation.

As a result of the Second Amendment and the simultaneous repeal of Section 2 of the Par Value Modification Act (31 U.S.C. 449), the provision of United States law defining the par value of the United States dollar in terms of the SDR and gold, the pre-existing basis for translating the term "United States dollar of the weight and fineness in effect on July 1, 1944" into current United States dollars or into any other currency no longer exists.

The General Counsel of the Bank has rendered a legal opinion concluding in substance that upon the entry into force of the Second Amendment (i) references in the Bank's Articles of Agreement to the 1941 dollar must be read as referring to the SDR, as determined from time to time by the Fund; and (ii) the mutual obligations of each member and the Bank with respect to maintenance of value of certain currency holdings will be measured by the value of the currency in question in terms of the SDR at any given time.

The General Counsel has also stated that in the exercise of their statutory power under Article IX of the Bank's Articles, the Executive Directors could properly arrive at a different conclusion, namely, that the 1944 dollar would be taken to mean 1.20635 current dollars. Furthermore, Questions have been raised whether ~~some member governments may feel that a~~ THE substitution of a new unit of value, insofar as it would give rise to any new obligations with respect to maintenance of value and capital stock subscriptions and payments, should be made only by amendment of the Articles. ~~There are other issues that may be~~ QUESTIONS WERE ALSO raised, ~~such~~ as TO the desirability of retaining the principle of maintenance of value, the form in which it is applied, and the appropriateness of substituting a unit of value other than the SDR. ~~Some time will be required to resolve these issues.~~

PENDING resolution of these questions, These financial statements have been drawn up in accordance with the General Counsel's ~~recommendation~~ OPINION, that is, the value of the capital stock is expressed in SDR.

The Bank's capital comprises 340,000 authorized shares of the par value of SDR100,000 (100,000 1944 dollars - 1977) each, of which shares have been subscribed (255,890 - 1977). Ten percent of the capital subscriptions has been called and paid in; the remaining ninety percent is subject to call by the Bank only when required to meet the obligations of the Bank created by borrowing or by guaranteeing loans. As to SDR (1944 dollars $24,695,403,000 - 1977), the restriction on calls is imposed by the Articles of Agreement and as to SDR (1944 dollars $3,086,925,000 - 1977) by resolutions of the Board of Governors.

Restricted currencies. The portion of capital subscriptions paid in to the Bank is divided into two parts: (1) SDR (1944 dollars $308,693,000 - 1977) initially paid in gold or United States dollars, and (2) SDR (1944 dollars $2,778,232,000 - 1977) paid in the currencies of the respective members. Of this latter portion an amount of SDR __________ (1944 dollars $134,217,000 - 1977) was subsequently converted by members into United States dollars, subject to the right of the Bank or the members to reverse the transactions. The amounts paid in gold or United States dollars or subsequently converted by members into United States dollars are freely usable by the Bank in any of its operations; however, the remaining amounts paid in the currencies of the members, hereinafter called restricted currencies, are usable by the Bank in its lending operations only with the consent of the respective members. The equivalent of SDR __________ (1944 dollars $1,826,888,000 - 1977) has been used with such consent.

Maintenance of Value. Article II, Section 9 of the Articles of Agreement provides for maintenance of the value, as of the time of subscription, of such restricted currencies, requiring (1) the member to make additional payments to the Bank in the event that the par value of its currency is reduced or the foreign value of its currency has, in the opinion of the Bank, depreciated to a significant extent in its territories, and (2) the Bank to reimburse the member in the event that the par value of its currency is increased. On March 16, 1973, the Executive Directors resolved that, for all members that established central rates for their respective currencies, pending establishment of new par values, maintenance of value obligations be settled on the basis of those central rates. These obligations of the members and of the Bank become effective immediately upon the happening of those events with respect to holdings of restricted currencies represented by currency balances and demand obligations. With respect to restricted currencies out on loan, these obligations become effective only as and when such currencies are recovered by the Bank, except that in several cases the Bank and the members concerned have agreed to make provisional settlements of such obligations, by means of one or more payments over periods not exceeding five years. The amounts thus receivable SDR (1944 dollars $372,000 - 1977) or payable, SDR (1944 dollars $ 6,158,000 - 1977) by the Bank are included in Amounts Required to Maintain Value of Currency Holdings under the headings Receivable on Account of Subscribed Capital and under Liabilities, respectively.

At June 30, 1977: Where market rates of exchange are not related to par values or central rates, as in the cases of a majority of members, and where there are differences between market rates of exchange and the rates at which capital subscriptions of members have been paid or are payable, such differences are shown as Translation Adjustments on Capital Subscriptions under the heading Other Assets. The amount thus established, $271,444,000 ~~($269,910,000---1976)~~ consists of notional receivables, $326,644,000 ~~($287,058,000---1976)~~ and notional payables, $55,200,000 ~~($17,148,000---1976)~~. These will become maintenance of value obligations if and when the provisions of Article II, Section 9 of the Articles of Agreement or the resolution of the Executive Directors described above can be applied.

At June 30, 1978: ~~According to the~~ legal opinion of the Bank's General ~~Counsel~~ referred to ~~in this Note~~d B under "Capital Stock", maintenance of value pursuant to Article II, Section 9 of the Articles of Agreement would be determined on the basis of the SDR, and notional obligations of members to the Bank and of the Bank to members are shown in the Financial Statements on this basis. Since the Bank is still considering the implications of the Second Amendment for maintenance of value obligations and in view of the ~~issues~~ Price of loans referred to above that have to be resolved, the timing of any establishment and settlement of maintenance of value obligations is uncertain. For the time being payments on account of subscriptions will continue to be accepted at the equivalent of $120,635 per share of capital stock.

Effect of Valuation in terms of the SDR. Expressing the value of the Bank's capital stock in terms of the SDR rather than in terms of $1.20635 does not have a material eff~~ort~~ECT on the financial position or results of the operations of the Bank. If the value of the capital stock were expressed in terms of $1.20635 subscribed capital would have been $ ________ instead of $ ________, the uncalled portion of subscriptions $ ________ instead of $ ________ and paid-in capital $ ________ instead of $ ________. Maintenance of value obligations and translation adjustments would have been $ lower [higher].

~~In view of the proposed amendments to the Fund's Articles of Agreement as described in paragraph two of this Note, the timing of the establishment and settlement of maintenance of value obligations is uncertain. On May 13, 1977, the Board of Governors approved a resolution increasing the authorised capital to $41,015,851,000 ($34,000,000,000 in terms of 1944 dollars). The Board of Governors also authorised certain members of the Bank to make additional subscriptions in the aggregate amount of $8,529,005,000. Subscribing members are required to pay ten percent of their subscriptions. No such subscriptions had been made up to June 30, 1977.~~

DRAFT

May 15, 1978

Reply from the Bank to U.S.

This is in reply to your letter, dated regarding the valuation of the Bank's capital stock in terms of the SDR.

The Bank takes note of the statement that the United States will have to obtain legislation to enable it to meet any obligation to the Bank arising from the adoption of such valuation which may be in excess of the amount of the obligation which would arise if the capital stock were valued in terms of one 1944 dollar equals current dollars $1.20635.

The Bank appreciates the fact that the U.S. (and other member countries as well) will have to enact such legislation to enable it to make such payments, a process which will take some time. In this connection, we call to your attention the statement in the Note to the Financial Statements that (a) the Bank will have to establish rules uniformly applicable to all members for the timing of the settlement of maintenance of value ~~obligations~~ PAYMENTS, (b) since members may have to take legislative or other governmental action in order to meet these obligations, the Bank will for the time being neither make nor request settlement of maintenance of value ~~obligations~~ PAYMENTS, and (c) payments on account of subscriptions will continue to be accepted at the equivalent of $120,635 per share of capital stock, subject to subsequent adjustment. The rules which the Bank will have to establish for that purpose are likely to require considerable study and discussion before they are adopted. For that reason and because of the fact that legislation will be required in the U.S. and other member countries, I can assure the U.S. that the Bank will not for the time being seek to request any member government to make settlement of a maintenance of value ~~obligation~~ PAYMENT.

Copy Ruth to Bergsten MONK

DRAFT

May 15, 1978

Letter from U.S. to the Bank

The United States Government notes the draft pro forma statement at June 30, 1978 of the item "capital stock" in the Bank's Balance Sheet and the corresponding June 30, 1977 statement and drafts of the Notes at June 30, 1977 and June 30, 1978 pertaining to those Statements. We note in particular that in the Financial Statements the capital stock of the Bank is valued in terms of the SDR, rather than in terms of one 1944 dollar equals current dollars $1.20635, and that maintenance of value pursuant to Article II, Section 9 of the Articles of Agreement is SHOWN ~~to be determined on the basis of the SDR and that the respective obligations of members to the Bank and of the Bank to members are shown in the Financial Statements~~ on that basis.

CAPITAL

Without passing on the propriety of the procedure followed by the Bank in ~~deciding to~~ EXPRESSING ITS ACCOUNTS valuING its capital stock in terms of the SDR, this is to advise you that existing U.S. legislation permits the U.S. to make commitments and payments to the Bank in terms of one 1944 dollar equals current dollars $1.20635, but not in terms of the SDR. ~~Accordingly,~~ The U.S. would have to obtain legislation to enable it to ~~meet~~ MAKE PAYMENT any obligation to the Bank arising from the adoption of such valuation which may be in excess of the amount of the PAYMENT obligation which would HAVE ~~arise~~ if the capital stock were valued in terms of one 1944 dollar equals current dollars $1.20635.

~~The U.S. Government intends to seek the enactment of such legislation as soon as possible.~~

Rec'd from R. Monk
5/12/78

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

Notes to Financial Statements

June 30, 1978 and June 30, 1977 Appendix G

SUMMARY OF SIGNIFICANT ACCOUNTING AND RELATED POLICIES

CAPITAL STOCK

Since , 1973, the Bank's capital stock, which is expressed in the Bank's Articles of Agreement in terms of "United States dollars of the weight and fineness in effect on July 1, 1944" (1944 dollars), has been translated by the Bank into current United States dollars at the rate of $1.20635 per 1944 dollar. Until March 31, 1978, that rate represented the par value of current United States dollars. Since the effectiveness of April 1, 1978 of the Second Amendment of the Articles of Agreement of the International Monetary Fund (the Fund), currencies no longer have par values in terms of gold. The Bank is examining the implications of this change on the valuation of its capital stock; for the time being the Bank will continue to value its capital stock on the basis of $1.20635 equals one 1944 dollar, (See Note B).

TRANSLATION OF CURRENCIES

The financial statements are expressed in terms of the current United States dollar solely for the purpose of summarizing the Bank's financial position and the results of its operations for the convenience of its members and other interested parties.

The Bank is an international organization which conducts its operations in the currencies of all of its members. The Bank's resources are derived from its capital, borrowings and accumulated earnings in the various currencies of its members and Switzerland and are held, invested or lent in those same currencies.

The Bank matches its borrowing obligations in any one currency with assets in the same currency, as prescribed by its Articles of Agreement, by holding, investing or lending the proceeds of its borrowings in the same currencies in which they are borrowed. The Bank maintains a neutral currency position with respect to its other resources by not converting one currency into another except for insignificant amounts required to meet certain obligations and operational needs of the Bank.

In general, the Bank translates its assets and liabilities in currencies other than United States dollars at market rates of exchange to the United States dollar at the end of each fiscal quarter with the exception of buildings and deferred charges which are translated at exchange rates in effect when the buildings were acquired or the charges incurred. Income and expenses other than depreciation and amortization charges are translated at an average of the market rate of exchange in effect during each quarter. The capital stock, which is expressed in terms of the United States dollar of the weight and fineness in effect on July 1, 1944 (the 1944 dollar), is translated by the Bank into current United States dollars at the rate of $1.20635 per 1944 dollar. (See Note B.)

Under the Bank's present policies, adjustments arising from the translation of currencies to the current United States dollar equivalent would not now or in the future result in realized gains or losses such as would result from the conversion of the various currencies into United States dollars. Accordingly, translation adjustments, with the exception of those relating to capital subscriptions described in Note B, are charged or credited to the General Reserve rather than income. (See Note A.) In those few instances where currencies are converted to another currency, the resulting gain or loss, if any, is included in the determination of net income.

****

NOTE B - CAPITAL STOCK, RESTRICTED CURRENCIES AND MAINTENANCE OF VALUE

Capital Stock. In the Articles of Agreement, the capital stock of the Bank is expressed in terms of "United States dollars of the weight and fineness in effect on July 1, 1944" (1944 dollars). ~~It comprises 340,000 authorized shares (270,000 - 1976) of the par value of $100,000 each, of which 255,890 shares have been subscribed (255,818 - 1976). Ten percent of the capital subscriptions has been called and paid in; the remaining ninety percent is subject to call by the Bank only when required to meet the obligations of the Bank created by borrowing or by guaranteeing loans. As to $24,695,403,000 ($24,688,454,000 - 1976), the restriction on calls is imposed by the Articles of Agreement and, as to $3,086,925,000 ($3,086,057,000 - 1976), by resolutions of the Board of Governors.~~

NEW BUT OK

~~On April 30, 1976, the Board of Governors of the International Monetary Fund (the Fund) approved proposed amendments to the Fund's Articles of Agreement which will become effective upon their acceptance by 60% of its members representing 80% of the voting power.~~ On April 1, 1978, amendments to the Articles of Agreement (the Second Amendment) of the International Monetary Fund (the Fund) entered into force. Under ~~these amendments~~ the Second Amendment, currencies ~~will~~ no longer have par values, gold ~~will be~~ is abolished as a common denominator of the monetary system and all calculations for the purposes of the Fund's Articles ~~will be~~ are made on the basis of the Special Drawing Right (SDR). ~~The United States has accepted these amendments which are not yet effective. Since July 1, 1974, the value of an SDR expressed in United~~

~~States dollars has been based upon the weighted relative values of a number of major currencies, including the United States dollar. This method of valuation will not be changed by these amendments. The Bank has under consideration the effect of these amendments on the valuation of the Bank's capital and the rights and obligations of members with respect thereto. If the SDR were to be substituted for the 1944 dollar in the Articles, it is not expected that this would have a material effect on the financial position or results of the operations of the Bank. Since the value of the SDR in terms of current dollars may vary from day to day and, therefore, may differ from the value of the 1944 dollar in terms of current dollars, as valued by the Bank, such a substitution might result in the amounts of the Bank's capital and subscriptions thereto expressed in current dollars varying from the amounts shown in these financial statements. If such a substitution were to have taken place at June 30, 1977, the Bank's capital expressed in current dollars would have been as follows subscribed $29,8333,319,000, uncalled $26,849,988,000 and paid in $2,983,331,000.~~

Since July 1, 1974, the value of an SDR in terms of United States dollars has been based on the weighted relative values of a number of major currencies, including the United States dollar (the basket). The value of the SDR on July 1, 1974, expressed in terms of United States dollars, was $1,20635, which was the equivalent of one 1944 dollar. Effective July 1, 1978, the Fund has made certain changes in the basket and established a method for further adjustment, at five-yearly intervals, to reflect changes in the relative importance of currencies over time, while ensuring continuity and reasonable predictability for the valuation of the SDR. The amounts of the currencies in the revised basket in terms of any currency was exactly the same, at June 30, 1978, under the revised valuation as under the then existing valuation.

NEW
OK

As a result of the Second Amendment and the simultaneous repeal of Section 2 of the Par Value Modification Act (31 U.S.C. 449), the provision of United States law defining the par value of the United States dollar in terms of the SDR and gold, the pre-existing basis for translating the term "United States dollar of the weight and fineness in effect on July 1, 1944" into current United States dollars or into any other currency no longer exists.

GC omitted A-A p5

The Bank has under consideration the effect of the Second Amendment on the valuation of the Bank's capital stock and the rights and obligations of members with respect thereto. For the time being, the Bank will continue to value its capital stock on the basis of $1.20635 equals one 1944 dollar, and the Financial Statements for the fiscal year ending June 30, 1978 have been drawn up on that basis. In the future, it may determine that the SDR will replace the 1944 dollar as the unit for valuing its capital stock, and the mutual obligations of each member and the Bank with respect to maintenance value of certain currency holdings will be measured by the value of the currency in question in terms of the SDR, as determined from time to time by the Fund.

If the SDR were to be substituted for the 1944 dollar in the Articles, it is not expected that this would have a material effect on the financial position or result of the operations of the Bank. Since the value of the SDR in terms of current dollars may vary from day to day and, therefore, may differ from the ~~value-of-the-1944-dollar~~ $1.20635, such a substitution might result in the amounts of the Bank's capital and subscriptions thereto expressed in current dollars varying from the amounts shown in these financial statements. If such a substitution were to have taken place at June 30, ~~1977~~ 1978, the Bank's capital expressed in current dollars would have been as follows:

subscribed $ --uncalled $ and paid-in $

The Bank's capital comprises 340,000 authorized shares of the par value 1944 dollars $100,000 each, of which shares have been subscribed (255,890 - 1977). Ten percent of the capital subscriptions has been called and paid in; the remaining ninety percent is subject to call by the Bank only when required to meet the obligations of the Bank created by borrowing or by guaranteeing loans. SDR omitted As to 1944 dollars $ (1944 dollars $24,695,403,000 - 1977), the restriction on calls is imposed by the Articles of Agreement and as to SDR omitted 1944 dollars $ (1944 dollars $3,086,925,000 - 1977) by resolutions of the Board of Governors.

Restricted currencies. The portion of capital subscriptions paid in to the Bank is divided into two parts: (1) SDR omitted 1944 dollars $ (1944 dollars $308,693,000 - 1977) initially paid in gold or United States dollars, and (2) 1944 dollars $ (1944 dollars $2,778,232,000 - 1977) paid in the currencies of the respective members. Of this latter portion an amount of SDR omitted 1944 dollars $ (1944 dollars $134,217,000 - 1977) was subsequently converted by members into United States dollars, subject to the right of the Bank or the members to reverse the transactions. The amounts paid in gold or United States dollars or subsequently converted by members into United States dollars are freely usable by the Bank in any of its operations; however, the remaining amounts paid in the currencies of the members, hereinafter called restricted currencies, are usable by the Bank in its lending operations only with the consent of the respective members. The equivalent of SDR omitted 1944 dollars $ (1944 dollars $1,826,888,000 - 1977) has been used with such consent.

Maintenance of Value. Article II, Section 9 of the Articles of Agreement provides for maintenance of the value, as of the time of subscription, of such restricted currencies, requiring (1) the member to make additional payments to the Bank in the event that the par value of its currency is reduced or the foreign value of its currency has, in the opinion of the Bank, depreciated to a significant extent in its territories, and (2) the Bank to reimburse the member in the event that the par value of its currency is increased. On March 16, 1973, the Executive Directors resolved that, for all members that established central rates for their respective currencies, pending establishment of new par values, maintenance of value obligations be settled on the basis of those central rates. These obligations of the members and of the Bank become effective immediately upon the happening of those events with respect to holdings of restricted currencies represented by currency balances and demand obligations. With respect to restricted currencies out on loan, these obligations become effective only as and when such currencies are recovered by the Bank, except that in several cases the Bank and the members concerned have agreed to make provisional settlements of such obligations, by means of one or may payments over periods not exceeding five years. The amounts thus receivable SDR omitted 1944 dollars $ (1944 dollars $372,000 - 1977) or payable, SDR omitted 1944 dollars $ (1944 dollars $6,158,000 - 1977) by the Bank are included in Amounts Required to Maintain Value of Currency Holdings under the headings Receivable on Account of Subscribed Capital and under Liabilities, respectively.

NEW ok ~~Where market rates of exchange are not related to par values or central rates, as in the cases of a majority of members, and~~ Where there are differences between market rates of exchange and the rates at which capital subscriptions of members have been paid or are payable (that is, on the basis that one share of capital stock is worth $120,635), such differences are shown as Translation Adjustments on Capital Subscriptions under the heading Other Assets. The amount thus established, $ ($271,444,000 - 1977) consists of notional receivables, $ ($326,644,000 - 1977) and notional payables, $ ($55,200,000 - 1977). These will become maintenance of value obligations if and when the provisions of Article II, Section 9 of the Articles of Agreement can be applied. In view of the ~~proposed amendments to the Fund's Articles of Agreement as described in paragraph two of this Note~~ Bank's consideration of what unit it should use to value its capital stock, the timing of the establishment and settlement of maintenance of value obligations is uncertain.

Br B GC etc
vretted
p 8-9

Rec'd from R. Monk
May 2/78

The United States Governor of the Bank has informed the Bank that his government takes the position that it is improper in these Financial Statements to value the capital stock of the Bank in terms of the SDR, rather than in terms of one 1944 dollar equals current dollars \$1.20635 as the Bank has done since the change in the par value of the dollar in 1973. According to him, existing United States legislation permits the United States to make committments and payments to the Bank in terms of the one 1944 dollar equals current dollars \$1.20635, but not in terms of the SDR. He said that it was his view that [there is], at the present time, the Bank has not taken action which would be an appropriate basis for going forward to the Congress for the necessary changes in existing authorization and appropriation legislation to permit the United States to meet any maintenance of value obligations or to make any payment on account of subscription to capital stock, in terms of the SDR.

Record Removal Notice

The World Bank Group Archives & Records Management

File Title	Barcode No.
Valuation of the Bank's capital - US, Asian Development Bank, Inter-American Development Bank - 1977 to 1978	1851279

Document Date	Document Type
March 9, 1978	Note

Correspondents / Participants
L. Nurick

Subject / Title
U.S. commitments and payments to Bank - in discussion with Russell Munk (Assistant General Counsel)

Exception(s)
Attorney-Client Privilege

Additional Comments

The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group.

Withdrawn by	Date
Shiri Alon	April 20, 2017

Record Removal Notice

File Title	Barcode No.
Valuation of the Bank's capital - US, Asian Development Bank, Inter-American Development Bank - 1977 to 1978	1851279

Document Date	Document Type
March 8, 1978	Memorandum

Correspondents / Participants
To: Mr. Edward R. Fried, U.S. Executive Director, World Bank
from: Russell L. Munk, Assistant general Counsel

Subject / Title
Unit of value in the international development banks

Exception(s)
Attorney-Client Privilege

Additional Comments

The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group.

Withdrawn by	Date
Shiri Alon	April 20, 2017

Mr. Broches May 3, 1978

Hugh Scott

<u>Asian Development Bank Prospectus</u>

Rainer Buhler has spoken to one of the people we work with at the Deutschebank about the prospectus for the ADB's recent DM issue and has been given the underlined changes which are set out below. The preliminary prospectus was filed with the Stock Exchange about three weeks ago and Rainer guesses that it will probably be another four weeks before the Stock Exchange comments are given to ADB and the prospectus can be distributed publicly. We have some questions about the accuracy of the text which has not been underlined and, if this were desirable, we could cable Graeme Rea for an accurate extract.

> <u>On April 1, 1978 amendments of the Articles of Agreement of the IMF became effective</u>. Under these amendments, currencies no longer have par values, gold is abolished as a common denominator of the monetary system and all calculations for purposes of the Fund's Articles are made on the basis of the Special Drawing Right (SDR). <u>Accordingly, it is necessary for the ADB to find a new basis for determining in current monetary terms the value of the 1966 dollar</u>. Since July 1, 1974, the value of a SDR expressed in United States dollars has been based upon the weighted relative values of a number of major currencies, including the United States dollar. This method of valuation has not been changed by these amendments. If the SDR were to be substituted for the 1966 dollar in the Articles, it is not expected that this would have a material effect on the financial position or results of the operations of the Bank. Since the value of the SDR in terms of current dollars may vary from day to day and, therefore, may differ from the value of the 1966 dollar in terms of current dollars, as valued by the Bank, such a substitution might result in the amounts of the Bank's capital and subscriptions thereto expressed in current dollars varying from the amounts shown in this Prospectus.
>
> <u>Pending a decision to redenominate ADB's capital, the ADB will continue to attribute to its shares the value which such shares had in each member currency at the exchange rate prevailing on the ADB's books as of March 31, 1978.</u>

HNScott:dg

cc: Messrs. Nurick, Sella, Buhler, Uhrig

Record Removal Notice

The World Bank Group Archives & Records Management

File Title Valuation of the Bank's capital - US, Asian Development Bank, Inter-American Development Bank - 1977 to 1978	**Barcode No.** 1851279
Document Date March 22, 1978	**Document Type** Letter
Correspondents / Participants To: Lester Nurick, Associate General Counsel, IBRD From: Graeme F. Rea, General Counsel, Asian Development Bank	
Subject / Title Enclosed informal paper regarding "Denomination and Valuation of the Bank's Capital: Procedural Aspects"	
Exception(s) Information Provided by Member Countries or Third Parties in Confidence	
Additional Comments	The item(s) identified above has/have been removed in accordance with The World Bank Policy on Access to Information or other disclosure policies of the World Bank Group.

Withdrawn by	Date
Bertha F. Wilson	February 23, 2018

CONFIDENTIAL

Incoming Telex from Asian Development Bank, Manila

WASHINGTON DC
17 MARCH 1978
FOR NURICK

RE CAPITAL DENOMINATION

AA YESTERDAY AT CONCLUSION OF BOARD MEETING WE INFORMALLY DISCUSSED WITH BOARD MEMBERS HOW TO PROCEED ON THIS ISSUE. I OUTLINED DEVELOPMENTS TO DATE AND INDICATED THAT UNLESS BOARD PREPARED TO REACH DECISION (WHICH I SUGGESTED MIGHT BE PROVISIONAL ONE) AHEAD OF WORLD BANK THEN IT SEEMED QUITE LIKELY THAT SECOND AMENDMENT WOULD BECOME EFFECTIVE WITHOUT OUR HAVING AN AGREED BASIS FOR VALUING CAPITAL. PRESIDENT AND STAFF HAVE THEREFORE BEEN REVIEWING POSSIBLE COURSES OF ACTION OPEN TO BANK ADMINISTRATION. WE CONSIDERED THAT CONTINUATION OF PRESENT SYSTEM UNDER WHICH UNITED STATES DOLLAR AS REGARDED AS BEARING FIXED RELATIONSHIP TO CHARTER UNIT BY VIRTUE OF THEIR RESPECTIVE GOLD CONTENT, AND VALUE IN OTHER CURRENCIES IS ASCERTAINED THROUGH DOLLAR, WOULD BE UNTENABLE FROM MOMENT SECOND AMENDMENT BECOMES EFFECTIVE. LEGALLY A CASE COULD BE MADE THAT SDR MUST BE PRESUMED TO ACQUIRE STATUS AS UNIT OF VALUE BUT PRESIDENT DID NOT WISH TO ACT ON THIS PRESUMPTION WHEN WHOLE ISSUE WAS ALREADY UNDER REVIEW AND AWAITING DECISION BY BOARD.

BB I EXPLAINED THAT IN CIRCUMSTANCES, ONLY OPTION WHICH WE COULD SEE LEFT TO MANAGEMENT WOULD BE TO FIX SHARE VALUES IN TERMS OF ALL CURRENCIES AT EXCHANGE RATES APPLICABLE AS OF DATE SECOND AMENDMENT BECOMES EFFECTIVE AND FOR AN INTERIM PERIOD CONTINUE TO ATTRIBUTE THESE VALUES TO SHARES. THIS WOULD PROVIDE A BASIS FOR PROVISIONALLY CALCULATING AND ACCEPTING SUBSCRIPTION PAYMENTS IN EACH CURRENCY, SUBJECT TO RETROSPECTIVE ADJUSTMENT WHEN DEFINITIVE DECISION ON VALUATION HAS BEEN MADE. HOWEVER, IN ABSENCE OF COMMON DENOMINATOR WE COULD NOT CALCULATE MOV ADJUSTMENTS NOR COULD WE PREPARE

MEANINGFUL FINANCIAL STATEMENTS. PROVIDED SECOND AMENDMENT DOES NOT BECOME EFFECTIVE UNTIL AFTER 31 MARCH AND DECISION IS REACHED BEFORE 30 JUNE, WE DID NOT ANTICIPATE SERIOUS PROBLEMS IN RESPECT OF ABOVE MATTERS. WE WERE HOWEVER CONCERNED ABOUT POSSIBLE PROBLEMS IN PREPARING PROSPECTUSES AND MIGHT HAVE TO COME BACK TO BOARD ON THIS.

CC SEVERAL BOARD MEMBERS STRESSED THAT NOTWITHSTANDING THESE PROBLEMS WE SHOULD NOT PROCEED TO A DECISION QUOTE IN ADVANCE OF UNQUOTE WORLD BANK, AND MATTER WAS LEFT THAT STAFF WOULD CONTINUE TO MAINTAIN CLOSE CONTACT WITH DEVELOPMENTS IN IBRD. SUBSEQUENT DISCUSSION WAS DEVOTED TO CLARIFYING LIKELY NATURE O[F] INTERIM PROBLEMS AND HOW THESE MIGHT BE HANDLED. CONTROLLER AND I AGREED TO SEND MEMORANDUM TO BOARD MEMBERS SUMMARIZING THE POSITION AS PRESENTED AT MEETING. THIS IS BEING FINALIZED NOW. I WILL SEND YOU COPY ON MONDAY BUT MUST EMPHASIZE THAT IT IS HASTILY PREPARED AND EXPOSITION OF ISSUES LACKS FINESSE PARTLY BECAUSE PROPOSED INTERIM APPROACH WAS ONLY SETTLED WITH PRESIDENT AND CONTROLLER YESTERDAY MORNING IMMEDIATELY BEFORE BOARD MEETING. I HAD BEEN ADVOCATING A MORE POSITIVE PROPOSAL.

DD BALL NOW RETURNS TO YOUR COURT. I HAVE JUST RECEIVED AND AM DULY IMPRESSED WITH RONNIES OPINION BUT WONDER HOW FAR ISSUE CAN BE FORCED PARTICULARLY IN VIEW OF APPARENT INABILITY OF UNITED STATES ADMINISTRATION EITHER TO AGREE TO VALUATION IN TERMS OF SDR OR TO IMPLEMENT CONSEQUENT OBLIGATIONS WITHOUT LEGISLATIVE AUTHORIZATION. ONE APPROACH WHICH MIGHT BE CONSIDERED IS TO RECOMMEND LOW-KEY PROVISIONAL ADOPTION OF SDR VALUATION IN FIRST INSTANCE, WITH DEFINITIVE DECISION POSTPONED FOR TWELVE MONTHS DURING WHICH MEMBERS WOULD BE EXPECTED TO TAKE MEASURES NECESSARY TO IMPLEMENT THE DECISION. IN INTERVENING PERIOD, MOV ADJUSTMENTS WOULD BE PROVISIONALLY CALCULATED IN

TERMS OF SDR BUT NO MOV SETTLEMENTS WOULD OCCUR. CAPITAL PAYMENTS WOULD ALSO BE PROVISIONALLY CALCULATED IN TERMS OF SDR BUT MEMBERS WOULD HAVE OPTION TO PAY EITHER AT SDR RATE OR AT RATE FIXED AS OF DATE OF SECOND AMENDMENT.

EE WOULD APPRECIATE ANY INDICATION YOU CAN GIVE ON HOW YOU INTEND TO PROCEED SINCE I WOULD LIKE TO MAKE SIMILAR PRESENTATION TO MY OWN BOARD IF POSSIBLE. INCIDENTALLY AND CONFIDENTIALLY I HAVE JUST SEEN CABLE FROM GERMANY TO EXECUTIVE DIRECTOR HERE INDICATING THAT THEY ARE EXPECTING ADB MANAGEMENT TO PRESENT DRAFT RESOLUTION FOR CHANGEOVER TO SDR BY INTERPRETATION AND THAT THEY ARE PUZZLED AS TO WHY WORLD BANK IS NOT TAKING SOME ACTION. I INTEND TO SUGGEST THAT IF GERMANY HAS NOT YET DEPOSITED ACCEPTANCE OF SECOND AMENDMENT IT SHOULD DEFER MATTER UNTIL JUST AFTER 31 MARCH THUS MINIMIZING IMMEDIATE PROBLEMS FOR ADB.

REGARDS

REA

ASIANBANK

Mr Broches
Mr Nurick
Mr Sella
Mr Nurick

ASIAN DEVELOPMENT BANK

CONFIDENTIAL
(For Consideration by the Board
about mid April 1977)

Working Paper 2-77
24 March 1977

PROPOSALS CONCERNING THE DENOMINATION AND VALUATION OF THE BANK'S CAPITAL, MAINTENANCE OF VALUE AND RELATED MATTERS, IN THE CONTEXT OF THE NEW INTERNATIONAL MONETARY SYSTEM

Attached for the consideration of the Board is a working paper on the above subject.

For Enquiries on Financial Aspects: Mr. Alan L. Pan, Controller's Department (Ext. 410)

For Enquiries on Other Matters : Mr. John L. Taylor, Office of the General Counsel (Ext. 168)

ASIAN DEVELOPMENT BANK

WORKING PAPER

PROPOSALS CONCERNING THE DENOMINATION AND VALUATION OF THE BANK'S CAPITAL, MAINTENANCE OF VALUE AND RELATED MATTERS, IN THE CONTEXT OF THE NEW INTERNATIONAL MONETARY SYSTEM

Office of the General Counsel

March 1977

TABLE OF CONTENTS

PROPOSALS CONCERNING THE DENOMINATION AND VALUATION OF THE BANK'S CAPITAL, MAINTENANCE OF VALUE AND RELATED MATTERS, IN THE CONTEXT OF THE NEW INTERNATIONAL MONETARY SYSTEM

1. During the discussions last year on the proposed second general capital increase in the Bank's capital stock, the Board was informed that prospective changes in the international monetary system could have a significant effect on the method of denomination and valuation of the Bank's capital. It was indicated that, in due course, proposals on these and other relevant issues would be formulated and submitted for consideration of the Board.1/

2. The need for a reappraisal of the Bank's practice arises principally from the fact that the capital stock of the Bank is denominated and valued "in terms of United States dollars of the weight and fineness in effect on 31 January 1966" (the "1966 gold dollar"). The par (i.e., face) value of each share is ten thousand 1966 gold dollars. At all times, the Bank must be in a position to measure the value of the 1966 gold dollar in terms of relevant currencies, so that it can determine with precision:

(a) the size of the Bank's capital;

(b) the obligations of members to make payments in respect of subscriptions for paid-in and callable shares, and the liability of members on shares already subscribed;

(c) the value of the Bank's ordinary capital resources and the statutory limit on ordinary operations under Article 12 of the Articles of Agreement;

1/ For a list of earlier Board documents relevant to the present discussion, see Appendix 1.

(d) the amount of ordinary resources available to be set aside to Special Funds under Article 19.1;

(e) the maintenance of value (MOV) obligations of the Bank and its members under Article 25; and

(f) necessary data concerning the above for inclusion in the Bank's reports and financial statements.

3. A realistic measure of the value of the 1966 gold dollar in terms of currencies relevant to Bank operations is possible only so long as the value of the 1966 gold dollar and of such currencies are linked, either directly or indirectly, to a common denominator. Under the international monetary system established in 1944 at Bretton Woods, the common denominator was gold (direct gold link) or the United States dollar of fixed gold content (indirect gold link). Recent developments in the international monetary system mean that gold has lost in fact, and will shortly lose as a matter of law, its status as a common denominator for the purposes of currency equivalence. These developments are reflected in proposed amendments to the Charter of the International Monetary Fund (IMF), which are likely to become effective later this year. Hence, within the context of the modified international monetary system, the Bank must find a new method for denominating and valuing its share capital and for determining the specific issues referred to in the preceding paragraph, without reference to gold.

4. The purpose of this Paper is to consider this problem and to recommend how it could best be resolved. The Paper is divided into five Sections, as follows:

- Section I briefly outlines the principal features of the international monetary system as established at Bretton Woods and as they have evolved since, and indicates how these principles have been reflected in the Bank's financial arrangements up to the present time;

- Section II considers the possible alternative monetary units which the Bank could adopt as successor to 1966 gold dollars, and concludes that for the Bank's purposes the most appropriate successor is the Special Drawing Rights (SDR);

- Section III discusses the implications for the Bank's capital and for maintenance of value rights and obligations of adopting the SDR;

- Section IV examines the implications of such adoption for other issues relevant to the Bank; and

- Section V examines the procedure for changing the unit of denomination of the Bank's share capital.

7. The Articles of Agreement also provide for the maintenance of value of payments made, in terms of 1966 gold dollars. Article 25 imposes on each member an obligation to maintain the value of the Bank's holdings of its currency by making additional payments, whenever the IMF par value of such currency is reduced in terms of the 1966 gold dollar or whenever the foreign exchange value of the currency has depreciated to a significant extent. The Article imposes a corresponding obligation on the Bank to refund an appropriate amount to a member when the par value of its currency is increased, or the foreign exchange value significantly appreciates. Soon after the establishment of the Bank, the Board of Directors by Resolution dated 21 March 1968[1/] (the "1968 Resolution") decided that the obligation of a member or of the Bank to make maintenance of value payments should be limited to such amount of the member's currency held by the Bank as is equivalent to the value, in terms of 1966 gold dollars, of the paid-in portion of that member's subscription to the paid-in capital stock of the Bank. (This amount is now commonly referred to as the MOV ceiling.) The Board also adopted the principle that each member with a convertible currency should pay the 6.2(a) portion of its paid-in capital subscription in its own currency. The 1968 Resolution has formed the basis for MOV actions ever since.

Changes in the Bretton Woods System and the Bank's Response

8. In the final years of the Bretton Woods monetary system, the supply of gold for monetary purposes had become increasingly unrelated to the needs of the rapidly expanding international economy and trade. In 1969, in an effort to reduce the monetary system's dependence on gold as the central reserve asset, the IMF established the facility of Special Drawing Rights, which were designed to act as a "supplement to existing reserve assets". Notwithstanding the creation of this facility, liquidity to finance international

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1/ DOC.M14-68 dated 21 March 1968. For the full text of the 1968 Resolution, see Appendix 2.

transactions was increasingly obtained by countries borrowing or purchasing U.S. dollars, until foreign official holdings of dollars, convertible into gold under the United States' par value obligation, amounted in mid-1971 to more than three times the value of total U.S. gold holdings.

9. Faced with this situation, and considering that the exchange rates of major currencies, including the U.S. dollar itself, did not reflect changes in the competitive realities of international trade, the United States in August 1971 announced that it would no longer convert U.S. dollars into gold. This action forced a multilateral reassessment of the international monetary system, and set in train a series of significant changes in the valuation of, and the relationship between, the U.S. dollar and other major currencies. The dollar was formally devalued in 1972 and again in 1973, through a reduction in its gold value. Although a number of other currencies continued to be expressed in terms of a "par value", an increasingly widespread acceptance of flexible exchange rates meant that eventually most IMF members no longer maintained effective par values or prescribed margins for their currencies, and no IMF member bought and sold gold freely for the settlement of international transactions. As a matter of practice, the fulfillment of the formal par value obligations of IMF members had ceased, and the IMF was obliged to suspend the application of par values in its operations and transactions.

10. Although the currency realignments of recent years have had a significant impact on the Bank's financial and other operations,1/ the Bank has maintained the formal status of the 1966 gold dollar as the unit of denomination and valuation of its capital. Each time the authorized capital stock of the Bank has been increased over the original $1 billion specified in the Articles, the additional stock has been denominated in terms

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1/ For details of currency realignments and their effect on Bank operations, see DOC.R2-72 dated 20 January 1972, DOC.R41-72 dated 7 July 1972, DOC.R20-73 dated 27 February 1973, DOC.IN.58-73 dated 21 September 1973, DOC.R93-73 dated 6 November 1973, and DOC.IN.145-75 dated 15 December 1975.

of United States dollars of the weight and fineness in effect on 31 January 1966.1/

11. This approach has been possible because, up to the present time, the United States continues to maintain a "par value" for its dollar in terms of gold, even though the value is purely a formal one. Since 18 October 1973, the formal gold content of the U.S. dollar has been 0.736662 gram of fine gold. The Bank currently values its capital and the rights and obligations of its members with respect thereto on the basis of the following principles:

(a) the value of the current U.S. dollar is deemed to be equal to its "par value" as fixed by U.S. legislation and communicated from time to time by the United States to the IMF; and

(b) the current U.S. dollar value of the 1966 dollar is determined by comparing the gold (par value) content of the current U.S. dollar (0.736662 gram of fine gold) with the gold (par value) content of the 1966 dollar (0.888671 gram of fine gold).

On this basis, the Bank regards one 1966 gold dollar as being equivalent to 1.20635 current (1977) United States dollars.2/ It then derives the value of all other currencies in terms of 1966 gold dollars by determining their value in terms of current U.S. dollars. In effect, under the Bank's practice, the current U.S. dollar is assumed to bear a fixed relationship to the 1966 gold dollar through their common denominator, gold, and all other currencies are regarded as appreciating or depreciating in relation to the current U.S. dollar.

12. In arriving at the value of these other currencies, the Bank applies the principles laid down by the Board of

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1/ See Board of Governors Resolutions No. 10, para. 1; No. 46, para. I(1); No. 55, para. 1(d); No. 79, para. 1(d); No. 80, para. 1(c); No. 89, para. 1(d); and No. 100, para. 1(d). See also Resolution No. 104, Section II(1), which is not yet effective.

2/ i.e., $\frac{0.888671}{0.636662} = 1.20635.$

Directors in its Resolution of 31 August 1972, entitled "Exchange Rates to be Used for Translation of Currencies and Maintenance of Value" (the "1972 Resolution").1/ This Resolution was adopted to provide guidance to the Bank in dealing with what was then believed to be a temporary situation, in which many important member currencies were no longer maintaining par values. The basic purpose was to enable the Bank to determine and apply a "realistic foreign exchange value" for such currencies in such a situation.

Evolution of the SDR

13. When created in 1969, the SDR was given a gold content identical to that of the 1944 (and 1966) U.S. dollar, i.e., its value was equivalent to 0.888671 gram of fine gold. This equivalence made it possible readily to determine the value of the SDR in terms of other relevant currencies. With the suspension of convertibility of the U.S. dollar into gold in 1971 and the events which followed that decision, the valuation of the gold-based SDR in terms of currencies became less realistic since it did not reflect actual changes in the value of currencies.

14. To overcome these difficulties, the IMF decided, with effect from 1 July 1974, to determine the value of the SDR not only in terms of gold, but also in terms of a "basket" of currencies. The basket was composed of 16 IMF member currencies2/ whose issuers had had an average share in total world exports of goods and services of more than one percent during the period 1968-1972. The decision to adopt the basket method of valuation did not effect an amendment to the IMF Articles so that, strictly as a matter of law, the SDR's value continued also to be identical in gold terms to the value of the 1944 dollar of fixed gold content.

1/ The text of the 1972 Resolution is reproduced in Appendix 3. A detailed description of its application appears in Appendix 4.

2/ Fourteen of which are issued by members of the Bank.

15. As indicated in Appendix 5, for each business day the IMF calculates and publishes the value of the SDR basket in terms of the U.S. dollar, and in terms of a large number of other currencies. The dollar/SDR rate is arrived at by adding together the U.S. dollar equivalents of the various currency amounts making up the basket, determined on the basis of the actual spot exchange rates in selected markets. The value of the SDR in terms of other currencies is determined by translating the dollar value into those currencies, on the basis generally of a "representative rate" between each currency and the dollar; so that if, for example, the representative rate of the currency is 10.00 units = US$1.00, and the dollar/SDR rate is US$1.20 = 1 SDR, then 12 units of the currency will be equivalent to 1 SDR. To preserve continuity of valuation, the amounts of the various currencies in the basket were determined in such a way that the value of the SDR in terms of the current U.S. dollar on the last business day of June 1974 (i.e., 28 June 1974) was identical to the value determined on the basis of the gold-based method of valuation (namely $1.20635 per SDR), thereby establishing the equivalence in terms of currencies of the gold value of the SDR. This continuity in value assumes particular importance for the Bank, as mentioned later in this Paper.

16. While the gold value of the SDR has formally remained the same as that of the 1944 gold-based dollar, the SDR's value under the "currency basket" method of valuation has been fluctuating daily in terms of current dollars and other currencies, since this method was introduced. This is in contrast to the current dollar value of the 1966 gold dollar, which has formally remained fixed at the par value last established by the United States in consultation with the IMF. Table 1 shows the values, in terms of current dollars, of both the 1944 gold-based dollar and the SDR since mid-1971. It will be seen that in 1972 and 1973 the current dollar value of both units increased, due to the devaluation of the dollar in those years. Since the introduction of the basket concept, the current dollar value of the SDR has at times been higher, and at other times lower, than that of the 1944 gold-based dollar. At present, it is approximately 4.2% lower in value than the latter unit.

Table 1
Comparison of Current U.S. Dollar Values

	1944$	SDR
30 June 1971	1.00000	1.00000
30 June 1972	1.08571	1.08571
30 June 1973	1.20635	1.20635
30 June 1974	1.20635	1.20635
30 September 1974	1.20635	1.18713
31 December 1974	1.20635	1.22435
30 June 1975	1.20635	1.23641
31 December 1975	1.20635	1.17066
30 June 1976	1.20635	1.14610
31 December 1976	1.20635	1.16183
28 February 1977	1.20635	1.15601

The Reformed International Monetary System and its Implications for the Bank

17. The period since 1971 has also seen determined efforts to reform the international monetary system established at Bretton Woods, so as to bring it into greater conformity with the needs of the modern world. These efforts culminated in the approval by the Board of Governors of the IMF, on 30 April 1976, of proposals for a Second Amendment to the IMF Articles (hereinafter called the "Second Amendment"). The Second Amendment will become effective upon acceptance of the Amendment by three-fifths of the members of the IMF having four-fifths of the total voting power. This is expected to occur in about mid-1977.

18. A fundamental feature of the Second Amendment is the *de jure* substitution of gold by the SDR as "numeraire" and central reserve asset in the new international monetary system. In particular, the Second Amendment, upon effectiveness:

(a) will abolish the official price of gold and eliminate its function as the "common denominator" of the par value system and as the unit of value of the SDR;

(b) will legalize the floating exchange rate system;

(c) will enable a par value based system to be introduced again in the future, but only by a decision by an eighty-five percent majority of total voting power of the IMF. If a par value based system is re-introduced, neither gold nor any individual currency can become the common denominator of that system;

(d) will confirm the current IMF practice of establishing IMF quotas, and valuing IMF assets in its accounts, in terms of the SDR; and

(e) will require the value of currency holdings of the IMF to be maintained in terms of the SDR.

The legal definition of the unit of value of the SDR (being "equivalent to 0.888671 gram of fine gold") is repealed by the Second Amendment. However, the method of valuing the SDR in terms of a basket of currencies will continue, unless changed in accordance with procedures provided for in the Second Amendment.

19. Since 1945, the United States by its internal law has maintained a formal par value of the dollar in terms of gold.1/ In October 1976, legislation was enacted2/ which,

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1/ For the most recent par value of 0.736662 gram of fine gold, see Section 2 of the Par Value Modification Act (86 Stat. 116, 31 U.S.C. 449 et seq. (1972)), which also established the value of the U.S. dollar in terms of the SDR.

2/ The Bretton Woods Agreement Act Amendment Act, Pub. L. No. 94-564, 94th Cong., 2d Sess. (19 October 1976).

upon the effectiveness of the Second Amendment, will abolish the par value of the dollar and the legal definition of the dollar in terms of gold or the SDR. This legislation will enable the United States to select an exchange rate arrangement of its choice for the dollar, within the framework of the new international monetary system.

20. The principles which the Bank has applied since the first dollar devaluation in 1972 to establish the relationship of the 1966 gold dollar to the current U.S. dollar, and through the U.S. dollar to other currencies, will no longer be applicable when the Second Amendment comes into force. Since neither the U.S. dollar nor any other currency will have a par value in terms of gold, it will be impossible to determine an equivalence between the 1966 gold dollar and any currency. As a result, the Bank will be unable to measure its capital, or the amounts payable for the paid-in and callable portions of members' subscriptions to such capital; it will be unable to implement MOV arrangements; it will be unable to determine the statutory limit on its ordinary operations or its borrowing limit; and it will be unable to prepare the necessary data concerning capital, and the obligations of members with respect thereto, for the purposes of its financial statements and reports.

21. It is clear that action must be taken by the Bank to avoid this situation, by denominating its share capital in a unit other than the 1966 gold dollar. The next Section of this Paper reviews various possibilities open to the Bank in this regard.

II. DENOMINATION OF CAPITAL IN NEW INTERNATIONAL MONETARY SYSTEM

22. When the Bank's founders were considering in 1965 what unit should be selected to denominate the Bank's share capital, they had three possible choices:

(a) a unit expressed directly or indirectly in terms of gold;

(b) a unit expressed in terms of a single currency; or

(c) a unit expressed in terms of a "basket" of currencies.

They chose the first alternative. This was consistent with the practice of comparable institutions at that time,1/ and enabled the value of the Bank's capital and subscriptions thereto to be determined by a constant unit of value meaningful in the context of the then existing monetary system.

23. Several reasons may be advanced why the gold-based dollar was selected for the Bank, and for other comparable institutions, as the most appropriate unit for denomination of capital:

(a) Constancy in Value: A unit was needed which was as constant in value as possible. The 1966 gold dollar fulfilled this requirement through its fixed relationship to gold.

(b) Translatability: A unit was needed which was readily translatable in terms of the currencies of actual and potential members. The gold-based dollar was so

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1/ The gold-based dollar was used by the IBRD and the Inter-American Development Bank, a gold-based unit was used by the European Investment Bank and the gold-based franc was used by the Bank for International Settlements. Although baskets of currencies were in limited use at that time, no international institution denominated its capital in such terms.

translatable, since gold was the central point of the prevailing monetary system, and the gold dollar provided in practice the medium through which the values of other currencies could be determined in relation to gold and to each other.

(c) Understandability: It was necessary that the unit be acceptable to, and readily understandable by, the governments which would be subscribing shares, and by the financial community which would be providing, through capital markets, a substantial portion of funds needed by the institution against the backing of the share capital.

(d) Mutuality: It was desirable that the unit enable reciprocity in the MOV rights and obligations of all the shareholders. The 1966 gold dollar fulfilled this qualification because it linked the rights and obligations of all members, directly or indirectly, to gold.

24. In selecting a successor to the 1966 gold dollar as the unit for denominating the Bank's capital, it is believed that the considerations expressed above are still critical. Clearly, however, it would now be inappropriate and absurd to consider gold, or any unit based on gold, as a possible denominator. With its demonetization, gold has become merely another commodity, the monetary value of which is determinable only by reference to its price in the commodity market.1/ Effectively, therefore

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1/ Recent wide fluctuations in the price of gold in the world market (from a high of almost $200 per ounce in 1974 to a low of approximately $100 per ounce in 1976) are unlikely to lessen. One objective of the Second Amendment is to avoid the management of the price, or the establishment of a fixed price, in the gold market. Whilst the Second Amendment envisages the possibility of dealings in gold between the IMF and its members, it is expressly provided that the price of gold shall be as agreed on the basis of prices in the market: see IMF Article V, Section 12 and Article VIII, Section 7 as amended by the Second Amendment.

the Bank must redenominate its capital either in terms of a single currency, or in terms of a basket of currencies. Each possibility will be briefly considered.

Selection of a Currency

25. It is clear that no single currency fulfills all of the criteria set out in paragraph 23 above. Any currency selected, therefore, would need to be one which fulfills as many as possible of these criteria and which, in addition, is of major significance to the Bank's operations. The U. S. dollar seems the most obvious choice. Indeed, it is difficult to see how a judgment could reasonably be made that a single currency other than the U.S. dollar would fulfill a more adequate role as a unit of denomination of the Bank's capital.

26. The U.S. dollar also has a special claim, since the capital of the Bank is already expressed in "dollars ... in terms of United States dollars of the weight and fineness in effect on 31 January 1966." It would be possible to proceed by eliminating all reference to the gold value of the dollar. Following this approach, the Bank could either:

(a) directly substitute current U.S. dollars for 1966 gold dollars, with the result that each share in the Bank's capital would have a value of current dollars 10,000; or

(b) substitute the current U.S. dollar value of the 1966 gold dollar on the basis of the latest par (gold) value of the current dollar, with the result that each share would have a value of current dollars 12,063.50.

27. However, selection of the U.S. dollar as the unit of denomination of the Bank's capital has two particular disadvantages:

(a) It would result in an unequal application of the maintenance of value obligations expressed in Article 25 of the Bank's Articles. This is because, in effect, maintenance of value obligations would cease to be applicable between the Bank and the United States, while variations in the value of the U.S. dollar in relation to other member currencies would result in maintenance of value adjustments between the Bank and the issuers of those other currencies. It is assumed that members of the Bank would not wish the mutuality of rights and obligations contemplated by Article 25 of the Charter to be so disturbed.1/

(b) Recent variations in the relative values of individual currencies, including the U.S. dollar itself, suggest that the use

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1/ If the U.S. dollar were selected as the denominator of the Bank's capital, it might be suggested that the mutuality of rights and obligations could be secured by elimination of the maintenance of value provisions from the Articles. However, Article 25 not only ensures that the Bank's holdings of currencies within the MOV ceiling retain their relative purchasing power despite changes in relative exchange rates, but also that each member pays the same amount as all other members in the same category for voting rights. In the absence of Article 25, a member whose currency weakens in international trade would contribute less for its shares and its share capital would be commensurately less valuable to the Bank. Accordingly, the Bank should vigorously resist any suggestion to eliminate MOV arrangements.

> of an individual currency unit would subject the Bank's capital to undesirably wide fluctuations in value in terms of other major currencies.

These disadvantages apply equally to any other currency which might seriously be considered as a unit of capital for the Bank.

Selection of a Basket of Currencies

28. The disadvantages associated with the use of an individual currency as the capital unit may be minimized by the use of a unit comprising more than one currency. In the new international monetary system, no unit will provide complete constancy in value, but a unit made up of a basket of currencies is likely to fluctuate less than a single currency and would certainly be more constant than any of its composite currencies: fluctuations in the value of any of these currencies will have a lesser effect upon the value of the unit, since the currency undergoing fluctuation forms a part only of the unit and since a depreciation in the value of one currency in the unit would tend to be offset by an appreciation in the value of other currencies in the unit. This feature has led to an increasing use of the "basket" concept in circumstances where a relatively stable unit of value is desired. In addition, the Bank's use of a capital unit comprising a basket of currencies would enable the continued application of Article 25 in respect of all members of the Bank.

29. To benefit from these advantages, the Bank could select one of the various units in use in financial circles, or could even create its own particular unit. Any unit which is reasonably representative of the currencies relevant to the Bank's operations would confer reasonable capital stability and enable reciprocity of MOV obligations. However, only one unit which displays these characteristics is also readily translatable in terms of the currencies of actual or potential members of the Bank and is accepted by, and readily understandable to, member governments and the financial community. That unit is the SDR.

30. In addition to these general considerations, it is suggested that the following specific reasons lead to the conclusion that the Bank should select the SDR for the purposes of denominating its capital:

(a) When the SDR was first established in 1969, its value was identical to that of the 1966 gold dollar, both units being equivalent to the same quantity of gold. When subsequently the IMF defined the SDR in terms of a basket of currencies, the composition of the basket was determined in such a way that the current dollar value of the 1966 gold dollar was equal to the sum of the values of the currencies which constituted the basket. In effect, during the last two years through which the Bretton Woods system functioned the SDR was equivalent to the 1966 gold dollar. In the reformed monetary system, the SDR has become the successor to the 1966 gold dollar.

(b) Just as gold was the common denominator for currency valuation under the Bretton Woods sytem, the SDR has become the common denominator under the new international monetary system. Through the SDR, the value of all IMF member currencies may directly or indirectly be determined. Hence, the SDR provides a functional substitute for the 1966 gold dollar for the purposes of the Bank's Articles.

(c) The selection of the SDR in lieu of the 1966 gold dollar will ensure that the capital of the Bank and subscriptions thereto will continue to be determined by reference to an independent unit of value and not by reference to the current value of any single currency unit. Thus (i) maintenance of value obligations expressed in Article 25 of the Bank's Articles will continue to operate between the Bank and all of its members; and (ii) the value of the SDR, though no longer constant in the same sense as the 1966 gold dollar (the value of which, through the gold denominator, was rigid) is expected to exhibit a greater measure of constancy of value than any single currency unit is likely to maintain.

31. For the reasons given above, it is recommended that the unit selected for redenomination of the Bank's capital be the SDR, as defined from time to time by the IMF. Subsequent sections of this paper discuss the implications of this recommendation and the procedures and timing to implement it.

III. IMPLICATIONS FOR VALUATION OF BANK'S CAPITAL AND RIGHTS AND OBLIGATIONS OF MEMBERS WITH RESPECT THERETO

32. If, as is proposed, the capital of the Bank were denominated in SDR's in lieu of 1966 gold dollars, each share would have a value of SDR 10,000. This would have important implications

(a) for the valuation of the SDR-denominated capital in terms of the Bank's unit of account, namely, current U.S. dollars;

(b) for the determination of the maintenance of value obligations of the Bank and its members under Article 25 of the Bank's Articles; and

(c) for the determination of outstanding amounts to be paid for the paid-in portions of member's subscriptions to the paid-in capital stock of the Bank issued under the First and Second General Capital Increases and special capital increases, as well as amounts payable in respect of callable shares.

A. VALUATION OF SDR-DENOMINATED CAPITAL IN TERMS OF UNIT OF ACCOUNT

33. The Bank's unit of account is the current U.S. dollar. When expressing the value of share capital denominated in SDR's in terms of this unit of account, the Bank would logically apply the published IMF dollar/SDR rate. As this rate varies, there will be corresponding daily fluctuations in the value of the Bank's capital in terms of its unit of account.

34. As indicated in paragraph 16 of this Paper, since the end of June 1974 the value of the SDR, expressed in terms of current U.S. dollars, has differed from the value of the 1966 gold dollar, expressed in similar terms. During the latter part of 1974 and the early part of 1975, the SDR's value was greater than that of the 1966 gold dollar. More recently, the SDR's value has been lower. Table 2 compares at six-monthly intervals since 30 June 1974 the current dollar value of the Bank's capital in terms of the 1966 gold dollar, with the corresponding value if at the relevant time the capital had been denominated in SDR's. As Table 2 shows, denomination of the share capital in SDR's would have meant a writing down in the value of the Bank's paid-in and callable capital, in terms of its unit of account, by about $136 million as of 31 December 1976. The effect on the Bank's balance sheet as of 31 December 1976 of a substitution of the 1966 gold dollar by the SDR is shown in Appendix 6.

Table 2

Subscribed Capital Stock

(Expressed in Millions of Current US Dollars)

	Paid-In Capital			Callable Capital		
	In 1966 Dollar a/	In SDR b/	Difference	In 1966 Dollar a/	In SDR b/	Difference
30 June 1974	930.30	930.30	-	1,830.93	1,830.93	-
31 Dec. 1974	932.11	946.02	13.91	1,838.16	1,865.59	27.43
30 June 1975	1,009.32	1,034.47	25.15	2,047.47	2,098.48	51.01
31 Dec. 1975	1,055.64	1,024.41	-31.23	2,145.90	2,082.42	-63.48
30 June 1976	1,055.68	1,002.95	-52.73	2,145.99	2,038.81	-107.18
31 Dec. 1976	1,182.48	1,138.84	-43.64	2,505.91	2,413.43	-92.48

a/ At current par value.
b/ At IMF rates.

B. MAINTENANCE OF VALUE ARRANGEMENTS

35. Article 25 Obligations. Subject to certain exceptions, Article 25 of the Bank's Articles requires a member to pay to the Bank (or the Bank to pay to a member) an amount of the member's currency necessary to maintain the value, in terms of 1966 gold dollars, of all such currency held by the Bank. As interpreted by the 1968 Resolution, this obligation applies only to the Bank's holdings of currency up to the MOV ceiling; the portion of a currency held in excess of this ceiling is not subject to maintenance of value. The obligation to make payment under Article 25 arises in two circumstances, namely,

(a) whenever the par value in the IMF of the currency of the member is reduced (increased); or

(b) whenever, in the opinion of the Bank after consultation with the IMF, the foreign exchange value of the member's currency has depreciated (appreciated) "to a significant extent".

Each payment is to be made within a reasonable time after the change in value of the currency occurs.

36. Present MOV Practice. The present practice of the Bank in implementing Article 25 is described in Appendix 4. MOV actions are taken on the basis of exchange rates determined in accordance with the 1972 Resolution, the purpose of which was to enable the Bank to determine a realistic foreign exchange value for each member currency, and to apply this value for MOV purposes. For member currencies having a par value, provisional or "other" rate, or central rate, on the basis of which foreign exchange transactions in the member's territory are generally conducted, an MOV adjustment is made in the Bank's books as at the date any change in the applicable rate occurs. Within a reasonable time thereafter, the outstanding MOV obligation is settled by a payment from the member to the Bank, or from the Bank to the member, as the case may be. For all other currencies, MOV adjustments are made in the Bank's books on the basis

of prevailing market rates as at the end of each calendar quarter. In the case of rates which are floating, however, such adjustments occur only if the new rate differs by more than 2.25%[1] from the rate previously used, the objective being to avoid unduly frequent adjustments as a result of relatively small changes in value. For all of these other currencies, MOV settlements are effected on the basis of amounts due as at the end of the second and fourth quarters in each year.

37. Future Application of Article 25. The abolition of par values means that, in the context of the new international monetary system, those portions of Article 25 which refer to a reduction or an increase in the par value of a member's currency will cease to have any effective application. Henceforth, the Article 25 obligations will apply only where the foreign exchange value of a member's currency has depreciated or appreciated to a significant extent. Moreover, assuming that the Bank decides to redenominate its share capital in SDR's, such depreciation or appreciation will have to be measured not in terms of the 1966 gold dollar as specified in the Article, but in terms of the SDR.

38. Proposed MOV Practice: Determination of Applicable Rates. The practice of the IMF in determining from day to day the value of the SDR in terms of current U.S. dollars and, through the U.S. dollar, in terms of a large number of other currencies, was referred to in paragraph 15. Clearly, it would be both appropriate and convenient for the Bank to utilize the relevant IMF published rates for purposes of maintaining the value of its currency holdings in terms of the SDR, so long as a rate to the SDR is available for the currency in question and so long as the IMF "representative" or other rate on which such SDR rate is based adequately reflects the realistic foreign exchange value of the currency. Where no rate to the SDR is published by the IMF for the currency, the Bank would

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1/ This percentage corresponds to the expanded permissible margins around parity accepted under the Smithsonian Agreement.

need to determine a rate for itself, using a suitable market rate between the currency and the U.S. dollar. Similarly, if in the Bank's opinion the currency/dollar rate used by the IMF does not seem adequately to reflect a realistic foreign exchange value for the currency, then it would be necessary for the Bank to determine and apply a suitable market rate, in order to ensure the proper application of Article 25. It is not clear at this stage whether, in fact, this latter situation is likely to arise very often. Where it does arise, it will probably be in cases of non-convertible currencies of some developing member countries. In such cases, the Bank need not concern itself with very minor divergences from market rates; it would act if, for example, a divergence of more than 2.25% appeared between the rate used by the IMF and the market rate preferred by the Bank.

39. In summary, it is proposed that for purposes of implementing Article 25 in relation to a share capital denominated in SDR's, the Bank would normally apply the rate for each relevant currency to the SDR as published by the IMF from time to time. Where there is no published rate, or where the IMF rate is based on an exchange rate between the currency in question and the U.S. dollar which differs by more than 2.25% from the market rate which the Bank considers most appropriate, then the Bank would determine for itself an applicable rate for such currency to the SDR, based on the market rate. If, in the example given in paragraph 15 above, the IMF representative rate is 10.00 units of the currency to US$1.00, while the preferred market rate is 15.00 units to US$1.00, then the rate which the Bank would apply for MOV purposes would be 15.00 (not 10.00) x 1.20 units = 1 SDR.

40. Proposed MOV Practice: Adjustments and Settlements. As to the actual implementation of Article 25, this will in future take place in a context where the value of each individual currency, in terms of the common denominator and measure of value, will be undergoing minor fluctuations from day to day. A very similar situation occurs at present in the case of floating currencies, and it seems reasonable to adopt a similar approach to that which is currently being successfully applied to such currencies under the 1972 Resolution.

Specifically, it is proposed that MOV adjustments for all currency holdings would be made in the Bank's books only at the end of each calendar quarter, and only if as of that date there has been a change of more than 2.25% in the rate previously applied for MOV purposes.[1/] MOV settlements would be made only once a year, based on the adjustment at the end of every fourth quarter, with payment being effected within (say) six months after the date as of which the amount of the settlement is determined. While it would be convenient from the Bank's point of view for all settlements to be made as of 31 December in each year, some flexibility could be given for the Bank to agree with a member, in special cases, on a different settlement date which is more closely related to the timing of the member's internal budgetary procedures.

41. Proposed MOV Practice: Base Rate. In the initial implementation of the arrangements outlined above, it would be necessary to maintain continuity between the valuation of the Bank's currency holdings in terms of 1966 gold dollars, on the one hand, and in terms of SDR's on the other. This requires the Bank to go back to 28 June 1974, being the last date on which the value of the two units was identical, and to use the IMF rates prevailing on that date as its base for calculating the first MOV adjustment consequent upon the redenomination of share capital. Thus, for MOV purposes the "base rate" of the U.S. dollar itself would be 1 SDR = US$1.20635. The first adjustment in this rate, for purposes of maintenance of value of the Bank's holdings of U.S. dollars within the applicable MOV ceiling, would be made if the dollar/SDR rate as at the end of the calendar quarter in which the present proposals become effective differs by more than 2.25% from this base rate. Subsequent MOV adjustments would occur if the dollar/SDR rate as at the end of any subsequent quarter differs by more than 2.25% from the rate previously adopted for MOV purposes. If these proposals had been in effect on 31 December 1976, the value of the U.S. dollar in terms of the SDR at that date (namely 1 SDR = US$1.16183) represents an appreciation of the dollar

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1/ In adopting the 1972 Resolution, the Board of Directors recognized that a change in value of more than 2.25% could be regarded as "significant" for purposes of Article 25.

above the base rate by more than 2.25%. Hence, an adjustment in the MOV rate from US$1.20635 to US$1.16183 would have been made, and a settlement of MOV obligations as of 31 December 1976 would have resulted in the Bank making a payment to the United States. A currency-by-currency estimation of the MOV adjustments which would have been applicable had the proposed method of valuation been adopted as at 31 December 1976, compared with the adjustments under the present MOV practice, is set out in Appendix 7. The net overall effect is that the Bank would have been required to pay to members a total amount equivalent to approximately US$32.7 million.

42. Deferment of Application of Realistic Rates. As indicated in Appendix 4, the 1972 Resolution enables developing member countries whose currencies are not convertible to seek a deferment of the application of realistic exchange rates for MOV purposes, on certain conditions. This arrangement will lapse with the 1972 Resolution itself. In making the initial transition to the proposed new basis for calculating MOV rights and obligations, it seems very desirable (if not essential) that all the Bank's currency holdings be properly valued at realistic market rates, and that requisite MOV adjustments be made. Whether subsequently a situation should be allowed to arise in which an MOV rate which is not realistic might be applied, with a deferment of the application of a more realistic rate, is a question which may need to be discussed further. However, given the fact that under the proposed new arrangements no member would be required to make an MOV payment more than once a year, the justification for allowing deferment arrangements may not be particularly strong.1/

1/ It should also be kept in mind that under the principles proposed in paragraph 38, a margin of up to 2.25% may exist between the rate for the currency which is applied for MOV purposes, and the rate which would be arrived at on the basis of a suitable market rate between the currency in question and the U.S. dollar: this is in addition to the margin allowed before a change in the MOV rate itself will occur.

C. PAYMENTS OF CAPITAL SUBSCRIPTIONS

43. Two issues need to be considered in connection with payments of capital subscriptions in the context of the new monetary system. One relates to the medium of payment, the other to the valuation of payments received.

(1) Medium of Payment

44. Provisions of Articles. The Bank's Articles require, in the case of subscriptions to the original authorized capital, that payment

(a) of the 6.2(a) portion of paid-in capital be made in gold or convertible currency;

(b) of the 6.2(b) portion of paid-in capital be made in the currency of the member concerned, whether that currency is convertible or not; and

(c) of callable capital be made in gold, convertible currency or the currency required to discharge the obligations of the Bank for the purpose for which the call is made.

The 1968 Resolution, which established a ceiling on the amount of each member's currency to which MOV obligations applied, called upon each member having a convertible currency to pay the 6.2(a) portion of its subscription in its own currency. This was designed to reduce the Bank's exposure to losses in respect of "unprotected" amounts of currency, i.e., amounts held in excess of the applicable MOV ceilings. The effect of the 1968 Resolution is that MOV protection is not available for amounts of convertible currency paid in under Article 6.2(a) by members whose own currencies are not convertible.

45. Provisions of Governors' Resolutions. With one exception, all subsequent Governors' Resolutions authorizing additional capital and providing for subscriptions thereto have applied to such new capital the provisions of the Articles

referred to above. The exception is Resolution No. 104, which authorized the second general capital increase. Under this Resolution, the 6.2(a) portion is payable only in convertible currency, with no option to pay in gold. This change in practice occurred because of the effective demonetization of gold.

46. <u>Position after Effectiveness of Second Amendment.</u> After the Second Amendment to the IMF Articles becomes effective, it will continue to be possible to apply the requirement that payment of the 6.2(a) portion of paid-in subscriptions be made in a convertible currency, since the basic concept of convertibility will not be modified.[1/] It will also still be necessary for each member having a convertible currency to pay its 6.2(a) portion in that currency. However, since the Second Amendment will formalize the demonetization of gold, it would be as inappropriate for the Bank to accept payment in gold - even in the remote eventuality that a member were to offer such payment - as it would be to accept payment in diamonds, platinum or any other valuable commodity. In referring to "gold" in the Articles, the draftsmen quite clearly meant this in the sense of the monetary denominator in terms of which all currencies were valued under the Bretton Woods system. Accordingly, it would seem proper for the Bank to regard all references in the Articles to "gold" as being no longer operative in the context of the new international monetary system.

1/ Article 23 of the Bank's Articles provides that the determination of whether any currency is convertible "shall be made by the Bank after consultation with the International Monetary Fund." The basic concept of convertibility is reflected in Article VIII, Sections 2, 3 and 4 of the IMF Articles which are not changed by the Second Amendment. A currency is convertible under Article VIII if the issuer of the currency accepts the obligations of that Article to avoid restrictions of a currency nature on the making of payments and transfers for current international transactions, multiple currency practices, and discriminatory currency arrangements. After the Second Amendment becomes effective, it will continue to be possible for the Bank to determine, after consultation with the IMF, whether a currency is convertible.

(2) Valuation of Subscription Payments

47. Present Practice. Article 6.4 of the Bank's Articles requires, with respect to the 6.2(b) portion of initial capital subscriptions, that payment be made at exchange rates which the Bank determines to be equivalent to the "full value", in terms of 1966 gold dollars, of each member's subscription. Each member is to make an initial payment in such amount as it thinks appropriate; but such payment is subject to adjustment within 90 days, as necessary to make up the full dollar equivalent of the amount due, as determined by the Bank. Since adoption of the 1972 Resolution, the Bank has been using the principles laid down in that Resolution to determine the exchange rates at which payments for both the 6.2(a) and the 6.2(b) portions of all capital subscriptions should be made.1/

48. Proposed Future Practice. The principle that the Bank should receive "full value" for each payment in respect of capital subscriptions, as of the date payment is received, will still apply whatever unit for denomination of share capital is adopted in the future. The difficulty in implementing this principle where the unit is the SDR will be that the rate between each currency of payment and the SDR will vary from day to day, and the member making the payment may not be able readily to ascertain the precise rate at which payment should have been made, until the day after the date such payment actually occurred. One solution to this problem, corresponding to that specified in Article 6.4 with respect to initial 6.2(b) subscriptions of members, would be for each member to make its payment at the rate which it thinks is appropriate, with an adjustment to the correct rate occurring within a short time thereafter. A simpler and (it is believed) more broadly acceptable solution would be for payment generally to be made

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1/ For example, the policies relating to translation of currencies were made applicable to payment of subscriptions to the First General Capital Increase (see DOC.M30-72 dated 21 September 1972 and DOC.R82-72 dated 1 November 1972) and to the Second General Capital Increase (Section III, paragraph 2 of Board of Governors' Resolution No. 104 adopted 29 October 1976).

at the rate applied by the Bank for MOV purposes as at the end of the previous quarter, with any subsequent adjustments taking the form of MOV action in due course. This approach would be subject to two exceptions:

(a) where on the date of payment the applicable rate to the SDR has already moved beyond a 2.25% margin from the last MOV rate;

(b) where the payment is made in a convertible currency which is not that of the member making the payment, so that the paying member has no MOV obligation in respect of that currency. (This would apply to all 6.2(a) payments by members with non-convertible currencies.)

In each of these situations, it is recommended that payment be initially made at the rate of the concerned currency to the SDR prevailing just before the date of payment, subject to adjustment to the actual rate of the day through an additional payment to the Bank, or a reimbursement by the Bank, to be effected within 30 days after the payment date.

IV. OTHER RELEVANT ISSUES

49. There are four other issues which require consideration in the context of the proposals to denominate the Bank's capital in terms of the SDR, namely, the effect upon:

(a) the unit of account;

(b) the method of valuation to be used for purposes of accounting;

(c) the limitation on the Bank's ordinary operations; and

(d) the Bank's borrowing limit.

A. UNIT OF ACCOUNT

50. As used by the Bank, the term "unit of account" means the currency unit which the Bank uses to record its transactions in various currencies in its books of account and financial statements. As a matter of law, the Bank is free to select whatever unit of account it considers appropriate, and the entry into force of the Second Amendment will not change this position. From the Bank's inception, it was decided that the unit of account would be the current U.S. dollar, which was then also the unit of value of the share capital. On occasions since, especially when the U.S. dollar was devalued, the Board has given consideration to the issue[1] and has decided that the unit of account should continue to be the current U.S. dollar.

51. Selection of the current U.S. dollar as the appropriate unit of account has been made primarily for accounting and administrative convenience; to ensure easily understandable accounts; to facilitate comparison of the Bank's

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1/ See the Board documents referred to in Appendix 1.

operations with the financial data of other institutions; and to maintain consistency with the practice of various international financial institutions which are most closely related to the Bank in terms of function and nature of operations, namely, the World Bank group and the Inter-American Development Bank.[1/] These reasons will hold good whatever decision is now made concerning the denomination of the Bank's capital. It is, therefore, assumed that the current U.S. dollar will continue to be the Bank's unit of account after the Second Amendment comes into force.[2/] The calculations in this Paper have been prepared on this assumption.

B. VALUATION OF CURRENCIES FOR ACCOUNTING PURPOSES

52. In addition to prescribing the method of valuing currencies for MOV purposes, the 1972 Resolution specifies the method of valuing currencies for accounting purposes (referred to in the 1972 Resolution as "translation of currencies"). Pursuant to the Resolution, translation is effected at the same rates of exchange as those utilized for MOV purposes. Thus changes in the exchange rates of currencies having a par value, provisional, other rate or central rate may be recorded in the Bank's books as at the date of such changes, but changes in the value of all other currencies, including floating currencies, (referred to in paragraph 3 in the 1972 Resolution and known generally as "paragraph 3 currencies") may be recorded only as at the end of each calendar quarter. The rates for paragraph 3 currencies as so determined are fixed, and under the Resolution are required to be applied for accounting purposes during the succeeding calendar quarter without variation during that quarter.

1/ The reasons supporting the use of the current U.S. dollar as the Bank's unit of account are fully discussed in DOC. IN.22-73 dated 3 April 1973.

2/ The unit of account will of course no longer be formally described, as it is at present, as "the current United States dollar with a gold content of 0.736662 gram of fine gold", but simply as "the current United States dollar".

53. Difficulties have been experienced in the application of the 1972 Resolution for accounting purposes. Increasingly, members of the Bank have adopted fluctuating exchange rates for their currencies; thus the Bank has categorized an increasing number of currencies as paragraph 3 currencies. Day-to-day transactions (for example, disbursements for loan operations and for administrative expenses) involving paragraph 3 currencies during a quarter having generally been recorded at the rates of exchange prevailing as at the end of the previous quarter, despite the fact that these rates differed from the actual or market rates at which those transactions took place. In addition, delays have at times been experienced in determining the rate to be adopted as at the end of each quarter for the purposes of preparing the Bank's financial statements: these delays often resulted from the consultation procedures required by the 1972 Resolution in the case of paragraph 3 currencies.

54. Similar difficulties are likely to occur in the future if valuation for accounting purposes is to continue on the same basis as valuation for MOV purposes. MOV adjustments will continue to be made only at the end of each calendar quarter and, in some cases, delays may still be caused in determining an appropriate rate for MOV purposes if consultation with members becomes necessary. Hence it is proposed that the method of valuation of currencies for accounting purposes should be separated from the method used for MOV purposes.

55. Proposed Practice: The Controller's Department proposes to value currencies for accounting purposes in accordance with generally accepted accounting principles. In general, assets and liabilities in currencies other than U.S. dollars will be valued at market rates of exchange as of the relevant dates and income and expenses will be translated at an average of the market rates of exchange in effect during the period. Since market rates will vary frequently in the context of the new international monetary system, it is most desirable to avoid frequent adjustments affecting numerous accounts in the Bank's books for small

variations. Accordingly, it is proposed that a new rate will be adopted and adjustments will be made only when such new market rates differ by more than 2.25% from the rates previously adopted for accounting purposes.

C. LIMITATION ON ORDINARY OPERATIONS

56. Article 12, paragraph 1 of the Bank's Articles provides that the Bank's operational limit is not to exceed "the total amount of its unimpaired subscribed capital, reserves and surplus included in its ordinary capital resources exclusive of [specified reserves] ...." Substitution of the 1966 dollar by the SDR will produce changes in this statutory operational limit, corresponding to the changes in the current dollar value of the Bank's capital. Depreciation of the current dollar against the SDR will raise the statutory operational limit, and appreciation will lower the limit, in terms of the unit of account.

57. An indication of the fluctuations in the operational limit during the past three years may be seen by the comparison shown in Table 3. As of 31 December 1976, the statutory lending limit would have been 3.7 per cent less if the SDR had been adopted by the Bank as the unit for valuing its capital. The corresponding limit would have been 1.5 per cent higher as of 31 December 1974.

Table 3
Statutory Operational Limit[a/]
(Expressed in Millions of Current US Dollars)

Date	Expressed in 1966 Dollars[b/]	Expressed in SDR[c/]	Difference
30 June 1974	2,768.39	2,768.39	-
31 December 1974	2,789.89	2,831.52	41.63
30 June 1975	3,094.32	3,171.43	77.11
31 December 1975	3,245.70	3,149.68	-96.02
30 June 1976	3,262.17	3,099.25	-162.92
31 December 1976	3,773.11	3,633.87	-139.24

a/ Excludes Special Reserve and Capital Set-Aside for Special Operations.
b/ At current par value.
c/ At IMF rates.

These variations are unavoidable in the context of a system of fluctuating exchange rates. The variations would have significance only at those times when the operational limit is being approached, which would normally occur just before a general capital increase. At these times, regard will need to be given to the potential variations in the limit caused through exchange rate fluctuations and, to avoid the limit being exceeded, consideration could be given to the establishment of margins beyond which operations will not be permitted.

D. LIMITATION ON TOTAL BORROWINGS

58. The effect on the Bank's borrowing limit will be similar. Bank policy (reflected in covenants with bondholders) has been to restrict outstanding borrowings and guarantees chargeable to ordinary capital resources to the amount of the callable capital stock then subscribed by members whose currencies are convertible.[1/] Hence, whilst the borrowing limit will remain constant in terms of SDR, the limit will fluctuate in terms of the Bank's unit of account, as indicated in Table 4.

Table 4
Effective Borrowing Limits[a/]
(Expressed in Millions of Current US Dollars)

Date	In 1966 Dollars[b/]		In SDR[c/]		Difference	
	100%	75%	100%	75%	100%	75%
30 June 1974	1,065.93	799.45	1,065.93	799.45	-	-
31 Dec. 1974	1,073.17	804.88	1,089.18	816.89	16.01	21.01
30 June 1975	1,169.68	877.26	1,198.82	899.12	29.14	21.86
31 Dec. 1975	1,210.69	908.02	1,174.87	881.16	-35.82	-26.86
30 June 1976	1,210.69	908.02	1,150.23	862.67	-60.46	-45.35
31 Dec. 1976	1,570.62	1,177.96	1,512.70	1,134.49	-57.92	-43.47

a/ Based on callable capital of those members specified in covenant in Bank's first bond issue maturing in 1984.
b/ At current par values.
c/ At IMF rates.

1/ To date, the Bank has further restricted its borrowings to 75% of this amount as an internal measure of prudent financial management.

59. Since the Bank's borrowings are denominated in a number of currencies, the U.S. dollar value of such borrowings varies depending upon variations in the exchange rates between the currency of borrowing and the U.S. dollar. The denomination of the Bank's capital in terms of the SDR means that the limit on borrowings will also vary corresponding to the variations in the U.S. dollar value in the SDR. The variations in the U.S. dollar value of the Bank's borrowings and of its callable capital will require careful observation to ensure that the level of permissible borrowings is not exceeded.

V. PROCEDURE FOR GIVING EFFECT TO PROPOSALS

60. It is expected that the Second Amendment will become effective some time during the second half of this year - probably not earlier than the end of June, but possibly not much later. As soon as it becomes effective, all references in the Bank's Articles of Agreement and in relevant Governors' Resolutions to share capital denominated in terms of 1966 gold dollars will cease to have any operative meaning. Before this happens, the Bank must have adopted a new method of denominating and valuing its share capital, in terms which are meaningful in the context of the reformed international monetary system and appropriate to the character and functions of the Bank as an inter-governmental financial institution. The new denominator recommended in this paper is the SDR, as defined from time to time by the International Monetary Fund.

61. There are two possible ways in which the necessary redenomination of the share capital could occur:

(a) through a formal amendment of the Articles and of the relevant Resolutions; or

(b) through the exercise of the Bank's powers of interpretation.

Amendment

62. A procedure for amendment of the Articles is laid down in Article 59. Following a decision by the Board of Directors to recommend an amendment for consideration by the Governors, the text of the proposed amendment would be submitted to the Board of Governors, through its Chairman, for a vote. Since the matter at issue does not fall within the "vested right" provisions specified in Article 59.2, the Governors' Resolution adopting the amendment could be passed by a positive vote of two-thirds of the total number of Governors, representing not less than three-fourths of the total voting power of the members. Between the date the Resolution is adopted and

the date the amendment comes into effect, a certain time period may elapse as specified by the Governors, such period in the absence of any directions to the contrary by the Governors being three months.

63. The special majority required to amend the Articles is the same as the majority required for initial adoption of each of the Governors' Resolutions which have increased the authorized capital stock of the Bank, denominated the new stock in 1966 gold dollars, and specified the applicability of the Articles (including Article 25) thereto. It follows that a similar majority would be required to amend these Resolutions.

64. The major advantage of formally amending the Articles and Resolutions is that these would then expressly record the correct position regarding denomination of the Bank's share capital, thus removing all possibility of confusion. In principle, this seems desirable and appropriate, especially since the Bank has never issued any share certificates which would serve as an independent record of members' holdings. In practice, however, adoption of an amendment procedure may not meet the Bank's requirements, for it may well prove impossible to complete this procedure prior to the date the Second Amendment becomes effective. Since the Bank has had no previous experience of amending its Articles, it is not known what internal steps members may consider themselves obliged to take before voting on a formal amendment; but experience of other organizations suggests that at least some members may wish to change their internal legislation, either before an amendment is put to the vote or before it becomes effective, in order to facilitate the performance of their obligations under the amended arrangements.1/ It may also perhaps be thought premature to

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1/ Presumably this is the reason for the time-lapse before effectiveness contemplated by Article 59. It may be noted that, in fact, the terms applicable to most of the Bank's outstanding capital stock are specified in various Governors' Resolutions rather than in the Articles themselves, and the Board of Governors has frequently amended its own earlier Resolutions. However, in the particular circumstances it is considered necessary for the amendment of the Articles and of the Resolutions to proceed in tandem, so that one type of amendment does not become effective before the other.

take the formal step of amending the Articles to refer explicitly to the SDR, until some experience has been gained in the practical application of the reformed monetary system and of a possible further evolution of the SDR in this context.

Interpretation

65. In these circumstances, it may be preferable, and even essential, for the redenomination to occur through the exercise by the decision-making organs of the Bank of the broad powers of interpretation which are vested in the Bank pursuant to its Charter.1/ The legal basis for such an approach is briefly stated in the following paragraphs.

66. It is a generally-accepted principle of treaty interpretation that the provisions of a treaty should, if possible, be given a practical effect and not be allowed to fail. The provisions in the Bank's constituent treaty relating to the denomination and valuation of its share capital are critical to the financial viability of the Bank and to its ability to carry out its functions. The issue before the Bank is how these provisions can continue to be given practical meaning and effect in the context of an international monetary system different from that contemplated when the Articles were initially framed. A mechanism for resolving this type of issue exists in the Articles, since the decision-making organs of the Bank are empowered to make definitive decisions regarding the interpretation and application of the provisions of the Articles. It seems clear that it would be appropriate for these organs to exercise their powers in the present case. Indeed, it would be mandatory for them to do so, if this is necessary to avoid a situation in which the Bank is left with no effective basis for valuing its share capital.

67. There are a number of precedents for an exercise of broad interpretative powers by the Board of Directors. The 1968 Resolution itself, which imposed a ceiling on the maintenance of value obligations specified in Article 25, is one such

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1/ See in particular Articles 21(vii), 28 and 60.

precedent. Another is the interpretation of the voting provisions of Article 33, under which a member which did not vote at an election may subsequently invest a Director with its voting rights. Another is the authorization to use and commit resources of the Technical Assistance Special Fund together with the Bank's ordinary income to finance technical assistance operations, notwithstanding the provisions of Article 10. These, and many other examples, demonstrate that in applying the Articles the Board of Directors has been willing to look behind the surface wording to the underlying intention, where this has seemed justifiable and in the general interests of the Bank. There have been few if any instances where the need for this has been more compelling than in the present case.

68. A specific rationale for the interpretation now proposed can be found in the fact that the expression "United States dollars of the weight and fineness in effect on 31 December 1966" appearing in Article 4.1 reflects the intention of the draftsmen that the Bank's share capital should be denominated in the unit which, under the Bretton Woods system, served as the common denominator and measure of value of all currencies. The significance of the expression lies in its reference to a specific and defined amount of gold. Since in the context of the new monetary system the expression has lost its intended significance, the Bank would be justified in regarding it as referring to the unit whose function in the new system most closely approximates to that previously performed by the 1966 gold dollar. This unit is the SDR. In effect, the Bank would be recognizing the SDR as successor to the 1966 gold dollar for purposes of applying its Articles in the future. Such recognition is, in principle, not substantially different from a recognition of the fact that references in the Articles to "the Economic Commission for Asia and the Far East" must now be read as referring to "the Economic and Social Commission for Asia and the Pacific."1/

1/ See Articles 1, 2(v) and 3.3. A precise analogy would occur if, for example, the IMF were to be wound up and a new institution created which performs essentially the same functions. In such circumstances, it would seem reasonable and proper to regard the many references in the Articles to the IMF as applying, mutatis mutandis, to the successor institution.

69. It is a matter for decision whether, in the circumstances, an interpretation as proposed should be made by the Board of Directors or by the Board of Governors. Article 60 lays down a specific procedure to be followed for resolving questions of interpretation or application of a provision of the Articles "arising between any member and the Bank, or between two or more members of the Bank." In such a case, it is mandatory for the Board of Directors to reach a decision in the first instance, but any member may then require the matter to be referred to the Board of Governors, whose decision shall be final. In fact, none of the interpretative decisions made in the past in the Bank have been explicitly made in response to a "question ... arising" between the Bank and a member, and many could not have been so characterized. Accordingly, it would in principle have been possible for the decisions to have been taken either by the Board of Governors, or by the Board of Directors in the exercise of the powers delegated to it by the Board of Governors. In practice, all such decisions were taken by the Board of Directors, partly no doubt by analogy with the Article 60 procedure and partly because this seemed the more convenient and appropriate course of action.

70. For the reasons summarized above, the General Counsel is of the opinion that the Board of Directors or Board of Governors could properly exercise their powers of interpretation to give effect to the recommendation that the Bank's share capital be redenominated in terms of SDR's. Such interpretation could be in lieu of, or in advance of, a formal amendment of the Articles. Given the consequences for the Bank if appropriate action has not been taken by the time the IMF Second Amendment becomes effective, however, it seems incumbent on the Board of Directors or Governors, as the case may be, to have taken such action by that date.

71. Any decision on the unit of denomination of the share capital would necessarily have to be accompanied by a series of decisions on revised procedures for payment of subscriptions and for maintenance of value, as outlined in Section III of this paper. The specific procedures can be more usefully discussed once the preliminary views of the Board of Directors are known on the major issue of redenomination of the share capital, and on the preferred procedure and forum for resolving this issue.

APPENDICES

Appendix 1

List of Relevant Board Documents

The following are documents relevant to the decisions and recommendations of the Board concerning the indicated subjects:

(1) Resolution and Recommendation dated 21 March 1968 Concerning Maintenance of Value and Use of Currencies

(a) DOC.R15-68 dated 16 February 1968 entitled "Maintenance of Value of the Currency Holdings of the Bank"

(b) DOC.M14-68 dated 21 March 1968

(2) Board Decisions Concerning the Finalization of Financial Statements for 1971 and Use of U.S. Dollar with Newly-Established Par Value for Accounting Purposes

(a) DOC.R2-72 dated 20 January 1972 entitled "Currency Realignment and its Effects on Bank's Assets, Capital and Operations"

(b) DOC.M3-72 dated 8 February 1972

(c) DOC.M13-72 dated 6 April 1972

(d) DOC.M14-72 dated 18 May 1972

(e) DOC.R41-72 dated 7 July 1972 entitled "Unit of Account"

(f) DOC.M25-72 dated 8 August 1972

(3) Resolution dated 31 August 1972 Concerning Translation of Currencies and Maintenance of Value

(a) DOC.R42-72 dated 31 August 1972 (Corrigenda 1 and 2, Addenda 1, 2 and 3) entitled "Exchange Rates to be Used for Translation of Currencies and Maintenance of Value"

(b) Supplementary Papers No. 1-5 issued from the Secretary dated 14 August 1972 (and Corrigendum 1) entitled "No. 1 - Observations on Scope and Application of Article 25; No. 2 - Definition of Terms; No. 3 - Maintenance of Value Practice of Other International Financial Institutions; No. 4 - Comparative Exchange Rates; and No. 5 - Bank Holdings, Expenses and Disbursements, by Currency

(b) DOC. M29-72 dated 5 September 1972

(4) Information Paper dated February 1973

IN12-73 dated 21 February 1973 entitled "Summary of Maintenance of Value and Related Actions Taken by the Bank in 1972"

(5) Board Decision dated 5 April 1973 to Continue Application of 31 August 1972 Resolution

(a) DOC. R20-73 dated 27 February 1973 (and Corrigendum 1) entitled "Currency Realignment: (i) Translation of Currencies and Maintenance of Value, and (ii) Unit of Account"

(b) DOC. M15-73 dated 10 April 1973

(6) Board Decisions to Continue Use of 1972 U.S. Dollar as Unit of Account

(a) IN22-73 dated 3 April 1973 entitled "Memorandum on the Implications of Adopting the SDR as the Bank's Unit of Account"

(b) IN28-73 dated 16 April 1973 entitled "Statements Showing Effects of Adoption of Different Units of Account"

(c) DOC. M17-73 dated 3 May 1973

(d) DOC. M35-73 dated 27 September 1973

(e) DOC. R93-73 dated 6 November 1973 entitled "Unit of Account".

(f) DOC. M45-73 dated 29 November 1973

(7) Information Paper dated September 1973

IN58-73 dated 21 September 1973 entitled "Report on Action Taken Pursuant to Board Paper R2-72 'Currency Realignment and Its Effects on Bank's Assets, Capital and Operations' as of 31 August 1973." This paper includes sections on maintenance of value, financial statements, unit of account and other matters.

(8) Information Paper dated December 1975

IN145-75 dated 15 December 1975 entitled "Losses Arising from Changes in Value of Currencies." This paper includes sections on unit of account, maintenance of value, translation, switching of currencies and other matters.

Appendix 2

Resolution Dated 21 March 1968 Concerning Maintenance of Value and Use of Currencies

"The Board of Directors, having been apprised of the observations in paragraph 23 of the Report of the Fourth Session of the Committee on Preparatory Arrangements for the Establishment of the Asian Development Bank (29 August - 1 September 1966), and having reviewed the maintenance of value and related provisions in the Articles of Agreement of the Bank,

RESOLVES

1. Maintenance of Value of the Currency Holdings of the Bank: Application of the Articles of Agreement

Pursuant to Article 60, paragraph 1 of the Articles of Agreement of the Bank, that the indicated provisions of the Articles be applied as follows:

a) Article 25, paragraphs 1 and 2:

The term 'currency held by the Bank' shall include holdings in the form of cash, bank balances or accounts, notes or other obligations accepted by the Bank under Article 6, paragraph 3, time deposits, bonds, notes and other authorized investments of the Bank and accrued income thereon, and all amounts outstanding under any loan made by the Bank and not yet paid together with interest payable thereon.

b) Article 25, paragraph 1:

The obligation of a member to make a payment to the Bank of an additional amount of its currency for the purpose of maintenance of value of the Bank's holdings of its currency does not apply to any amount of such currency in excess of such amount as is equivalent to the value in terms of dollars of the paid-in portion of that member's subscription to the paid-in capital stock of the Bank.

c) Article 25, paragraph 2:

The obligation of the Bank to make a payment to a member of an amount of its currency to adjust the value of the Bank's holdings of that member's currency does not apply to any amount of such currency in excess of such amount as is equivalent to the value in terms of dollars of the paid-in portion of that member's subscription to the paid-in capital stock of the Bank.

d) In accordance with Article 4, paragraph 1, the term 'dollars' herein shall be understood as being United States dollars of the weight and fineness in effect on 31 January 1966;

AND

2. <u>Use of Currencies: Adoption of Decision Pursuant to Article 24, Paragraph 4(ii)</u>

Pursuant to Article 24, paragraph 4(ii) of the Articles of Agreement, that:

a) Gold or the currency of a non-member held by the Bank, or

b) the convertible currency of a member held by the Bank, in excess of the amount to which the obligation of that member under Article 25, paragraph 1 applies,

may be used by the Bank to purchase the convertible currency of any member of the Bank.

AND, in order to facilitate the implementation of the above decisions,

<u>RECOMMENDS</u> as desirable that members whose currencies are convertible should make the payment provided for in Article 6, paragraph 2(a), in their own respective currencies."

Appendix 3

Resolution Dated 31 August 1972 Concerning Exchange Rates to be Used for Translation of Currencies and Maintenance of Value

"The Board resolved:

That in view of the current temporary regime in the international monetary system and pending further decision by the Board of Directors, the policy set forth in paragraphs 1 through 5 of this Resolution be adopted by the Bank with respect to the translation of currencies into United States dollars in the books of account and financial statements of the Bank, and for maintenance of value under Article 25 of the Articles of Agreement of the holdings of the Bank of member currencies:

1. For each member currency having a par value or provisional rate or other rate heretofore used by the Bank for translation and maintenance of value purposes, on the basis of which foreign exchange transactions in the territory of the concerned member are generally conducted, the Bank will use such par value or provisional rate or other rate for translation purposes. A maintenance of value adjustment will be made whenever there is a change in the applicable par value or provisional rate or other rate. Settlement of maintenance of value obligations will be effected within a reasonable time after each adjustment.

2. For each member currency having a central rate, on the basis of which foreign exchange transactions in the territory of the concerned member are generally conducted, the Bank will adopt such central rate for translation purposes as of 30 June 1972, or as of such later date as a central rate for such currency is established. A maintenance of value adjustment will be made as of the date first used by the Bank for translation purposes, and a further adjustment will be made whenever there is a change in the applicable central rate. Settlement of maintenance of value obligations will be effected within a reasonable time after each adjustment.

3. For each member currency which does not fall within paragraphs 1 or 2 of this Resolution, and subject to paragraph 4 of this Resolution, the Bank will use for translation and maintenance of value purposes an exchange rate which, in the opinion of the Bank, after consultation with the International Monetary

Fund, represents from time to time a realistic foreign exchange value of such currency. To this end:

(a) In the case of a currency which is floating, the Bank will, at the end of each calendar quarter, determine a current market rate for the currency, by utilization of (i) the rate prevailing in a principal exchange market in the member's territory on the last business day of the calendar quarter, or (ii) the average of the daily rates prevailing in a principal exchange market in the member's territory during the ten business days preceding the end of the calendar quarter, or (iii) such other method as the Bank, after consultation with the member concerned, may consider most appropriate for purposes of this Resolution. As of 30 June 1972, or as of the end of the calendar quarter in which the currency shall have commenced to float, whichever is the later, the Bank will adopt for translation purposes the current market rate; and during each succeeding calendar quarter thereafter, translation will be made at the current market rate determined as of the end of the preceding calendar quarter. A maintenance of value adjustment will be made at the end of each calendar quarter at the current market rate. Settlement of maintenance of value obligations will be effected on the basis of amounts due at the end of the second and fourth calendar quarters of each calendar year, and within a reasonable time thereafter, with effect from 31 December 1972. Notwithstanding anything heretofore provided, the Bank will in any calendar quarter adopt a current market rate for translation and maintenance of value purposes only if such rate differs from the rate previously used by the Bank for such purposes by more than 2.25 per cent of such previous rate.

(b) For all other currencies falling within this paragraph 3, the applicable rate will be determined by the Bank on a case-by-case basis. The rate so determined for each such currency will be adopted by the Bank for translation purposes as of 30 June 1972, or as of such later date as the currency shall first be deemed by the Bank to fall within this sub-paragraph (b). At the end of each calendar quarter thereafter, the Bank will review the rate so adopted and, if necessary, adopt a new rate for the next succeeding calendar quarter. A maintenance of value adjustment will be made as of the date on which a rate is first adopted for translation purposes pursuant to this sub-paragraph (b), and as of each subsequent date on which a new rate shall have been so adopted. Settlement of maintenance of value obligations will be effected on the basis of amounts due at the end of the second and fourth calendar quarters of each calendar year, and within a reasonable time thereafter: Provided that the first settlement will be effected as of 31 December 1972.

4. Where a currency falling within paragraph 3 of this Resolution is that of a developing member of the Bank and such currency is not convertible, the Bank, if so requested by the member, will agree to defer action pursuant to paragraph 3 of this Resolution, so long as arrangements satisfactory to the Bank are made in respect of those portions of the Bank's holdings of such currency which may be required to be used by the Bank for administrative expenses and for purposes of loan operations, to avoid any adverse effects which would otherwise be sustained by the Bank by reason of such deferment. Pending the outcome of consultation with each member which would be entitled to seek a deferment under this paragraph 4, and during the period of any such deferment as may be agreed by the Bank and the member concerned, translation and maintenance of value actions in respect of a currency to which this paragraph 4 applies will continue to be undertaken in accordance with the policies set out in paragraphs 1 or 2 of this Resolution, as appropriate.

5. In the event that a change in circumstances makes it appropriate to regard a member currency as falling within a category established in paragraphs 1, 2 or 3 of this Resolution different from that in which it was formerly placed, the policies concerning translation and maintenance of value actions applicable to the new category will be applied as from the date of the change,

and any necessary maintenance of value adjustments and settlements with respect thereto will be made as of such date: Provided that where a currency commences to float, the provisions of subparagraph (a) of paragraph 3 of this Resolution shall come into effect only as of the last day of the calendar quarter in which such floating shall have commenced.

6. The President is authorized to make appropriate arrangements to carry into effect the policies set forth in this Resolution."

Appendix 4

Practice of Bank Concerning Maintenance of Value and its Applicability After Second Amendment Becomes Effective

Article 25

1. Subject to certain exceptions, Article 25 of the Bank's Articles requires a member to pay to the Bank (or the Bank to pay to the member) an amount of the member's currency required to maintain the value of all such currency held by the Bank, in two alternative circumstances, namely, whenever:

(a) the par value in the IMF of the currency of the member is reduced (increased) in terms of the 1966 dollar; or

(b) in the opinion of the Bank, after consultation with the IMF, the foreign exchange value of the member's currency has depreciated (appreciated) to a significant extent.

1968 Resolution

2. Currencies and MOV Ceiling: By Resolution dated 21 March 1968 relating to implementation of Article 25 (the 1968 Resolution[1/]), the Board of Directors took the following two important decisions which are still in force, inter alia:

(a) the Board provided an interpretation of the meaning of the term "currency held by the Bank" for the purposes of Article 25; and

(b) the Board decided that the obligation of a member of the Bank to make payment in

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1/ For full text, see Appendix 2.

> respect of maintenance of value ("MOV") shall be limited to the amount of the member's currency held by the Bank equivalent to the value in terms of 1966 dollars of the paid-in portion of that member's subscription to the paid-in capital stock of the Bank (the so-called MOV ceiling).

In order to facilitate the implementation of these decisions, the Board recommended that members whose currencies were convertible should make payment of the 6.2(a) portion of capital subscriptions (namely, payment of the gold or convertible currency portion) in their own respective currencies.

1972 Resolution

3. Valuation for MOV Purposes: The method currently used by the Bank to value currencies for purposes of MOV is specified in the 1972 Resolution.1/ That Resolution divides member currencies into three categories, as follows:

> paragraph 1 currencies are currencies having a par value, provisional or other rate, on the basis of which foreign exchange transactions are generally conducted. Changes in these rates result in immediate MOV adjustments, MOV settlements are made within a reasonable time thereafter;
>
> paragraph 2 currencies are currencies having a central rate, on the basis of which foreign exchange transactions are generally conducted. MOV adjustments and settlements are effected as in the case of paragraph 1 currencies; and
>
> paragraph 3 currencies are all other currencies including floating currencies. MOV adjustments are effected on the basis of realistic foreign

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1/ For full text, see Appendix 3.

exchange rates determined by the Bank in consultation with the IMF and the member concerned at the end of each calendar quarter.[1/]

4. Deferment Arrangements: The 1972 Resolution provides that in respect of the currency of a developing member which is not convertible, the Bank, if so requested by the member concerned, will agree to defer utilizing realistic rates for MOV purposes, so long as arrangements satisfactory to the Bank are made to make available to the Bank, at realistic rates of exchange, portions of such currency which may be required to be used by the Bank. Hence, during the period of such deferment, MOV of the portions not required by the Bank for its use is made on the basis of the par value, provisional or other rate, or central rate, even though these may be ineffective or unrealistic.

5. Increasingly since the adoption of the 1972 Resolution, most member currencies, particularly the convertible currencies, have adopted fluctuating exchange rates. As a result, the Bank has increasingly categorized member currencies as paragraph 3 currencies for purposes of the 1972 Resolution and has determined the value of such currencies for MOV purposes on a quarterly basis, according to one of the various methods of valuation of fluctuating currencies permitted by the Resolution.

Continued Applicability of Article 25 in the Context of the New International Monetary System

6. After the Second Amendment becomes effective, Article 25 will continue to be applicable but only in the circumstances indicated in paragraph 1(b) of this Appendix. Under paragraph 1(b), MOV action is required in the event of an appreciation or depreciation in the foreign exchange value of a member's currency. Paragraph 1(a) will be rendered inapplicable (unless and until the IMF should decide to reintroduce a new par value system), because par values in existence under the present IMF Articles will cease to be in effect.

1/ In the case of floating currencies, new rates are adopted only if they differ by more than 2.25 per cent at the end of any one quarter from the rates previously adopted.

Continued Applicability of 1968 and 1972 Resolutions in the Context of the New International Monetary Situation

7. Recent developments in the exchange arrangements utilized by members have rendered the 1972 Resolution increasingly difficult to apply. After the Second Amendment becomes effective, the 1972 Resolution will be largely inappropriate because the categorization of currencies referred to in the Resolution will become outdated. If the proposed MOV practice described in paragraphs 38 to 42 of the Paper are adopted, the principles embodied in the 1968 and 1972 Resolutions would be affected in the following manner:

(a) 1968 Resolution: The definition of the term "currency held by the Bank" appearing in this Resolution would not be affected. Similarly, the decision concerning use of currencies (authorizing switching of currencies held in excess of the MOV ceiling) as well as the recommendation that convertible currency members make payment of the Article 6.2(a) portion of their subscriptions to capital in their own respective currencies, would remain unaffected. However, expression of the MOV ceiling will undergo change since the 1968 Resolution expresses the ceiling in terms of 1966 dollars. Since it is proposed to interpret the 1966 dollar, wherever appearing in the Bank's Articles, as the SDR, consistency demands that the same interpretation be applied in the case of references to the 1966 dollar in resolutions, decisions and records of all organs of the Bank. In this event, the MOV ceiling will be interpreted as follows: that the Bank and each member is required to maintain in terms of the SDR the Bank's holdings of the member's currency up to, but not exceeding, the value in terms of the SDR of the paid-in portion of that member's subscription to the paid-in capital stock of the Bank.

(b) 1972 Resolution: The 1972 Resolution will become incapable of application after the Second Amendment becomes effective. Paragraphs 1 to 3 of that Resolution categorize currencies according to the exchange rate categories discussed in paragraph 3 of this Appendix. Paragraph 1 (par value, provisional or other rate) currencies will no longer be meaningful upon the adoption of the Second Amendment to the IMF Articles. The valuation of paragraph 2 (central rate) and paragraph 3 (other) currencies will be superseded by the method of valuation discussed in paragraphs 38 and 39 of the Paper. It will not be possible to apply paragraph 4 (deferment arrangements) and paragraph 5 (consequences of a recategorization of currencies) of the Resolution, since the relevant categories of currencies will no longer be meaningful. Paragraph 6 of the Resolution authorizes the President to make appropriate arrangements to carry into effect the policies set forth in the Resolution. The practice of the Bank has revealed that such an authorization is a particularly useful administrative mechanism, especially in circumstances like the present where it is difficult to foresee the likely course of events in respect of the exchange rates of relevant currencies. Accordingly, it would appear appropriate to include a similar provision in any new resolution on this subject.

the old method of valuation was used, the old and the new methods yielded the same values for currencies in terms of the SDR, namely US$1.20635. The amounts of each currency so determined were as follows:

Currency	Currency Amount Component
U.S. dollar	0.40
Deutsche mark	0.38
Pound sterling	0.045
French franc	0.44
Japanese yen	26.00
Canadian dollar	0.071
Italian lira	47.00
Netherlands guilder	0.14
Belgian franc	1.60
Swedish krona	0.13
Australian dollar	0.012
Danish krone	0.11
Norwegian krone	0.099
Spanish peseta	1.10
Austrian schilling	0.22
South African rand	0.0082

The amounts of the currencies are fixed under Rule O-3 of the Rules and Regulations of the IMF and will remain unchanged unless otherwise determined by the IMF.

Valuation of Currencies in Terms of SDR

3. To determine the exchange rate for a currency in terms of the SDR, a calculation is made of the equivalent of all the currency components of the SDR in terms of that currency on the basis of exchange rates in the market. For the sake of convenience, the IMF makes this calculation in accordance with the following procedures (embodied in Rule O-3):

a) the rate for the SDR is calculated in terms of the U.S. dollar. This rate is the sum of the U.S. dollar equivalents of the 16 currency components at market rates for these currencies, with the exception of the yen, from the London (or if not available, New York or Frankfurt) exchange markets. For the yen, the rate is received from Tokyo;

b) having obtained the U.S. dollar rate in the manner set out in (a), rates for the SDR against other currencies (including currencies not in the SDR basket) are calculated on the basis of representative market rates, which are exchange rates for a member's currency determined by a procedure or criterion agreed between the member and IMF, and are often rates reported to the IMF individually by the central banks of the members concerned. For example, if one SDR = US$1.14610 and a representative market rate for the French franc is F4.74025 per U.S. dollar, the rate for the SDR in terms of the French franc is 4.74025 multiplied by 1.14610, that is, one SDR = F5.4328.

4. It may be noted that utilizing the above procedures, the U.S. dollar is no longer at par in relation to the SDR: the rate for the U.S. dollar fluctuates in terms of the SDR from day to day in the same way as the rates for other currencies fluctuate. Moreover, changes in the exchange rate for any one currency in the SDR basket affect the value of the SDR according to the proportion of the currency in the basket. Thus the value of the SDR itself fluctuates daily.

Appendix 5

"Currency Basket" Technique of Valuation of SDR and Currencies in Relation to the SDR

Valuation of SDR

1. Effective 1 July 1974, the value of the SDR ceased in fact to be determined by the IMF in terms of a fixed value of gold (equal to the gold value of the 1966 dollar) and started to be determined on the basis of the composite value of 16 currencies whose issuers had had a share in total exports of goods and services in excess of 1% on average over the period 1968-1972. Percentage weights were assigned to each of the 16 currencies in broad proportion to the share in international transactions of the issuers of such currencies. The 16 currencies selected and the percentages ascribed to each currency were as follows:

Currency	Weight (in per cent)
U.S. dollar	33
Deutsche mark	12.5
Pound sterling	9
French franc	7.5
Japanese yen	7.5
Canadian dollar	6
Italian lira	6
Netherlands guilder	4.5
Belgian franc	3.5
Swedish krona	2.5
Australian dollar	1.5
Danish krone	1.5
Norwegian krone	1.5
Spanish peseta	1.5
Austrian schilling	1
South African rand	1
	100

2. The percentage weights of the various currencies were then converted into amounts of each currency. The currency amounts were determined in such a way that, on 28 June 1974, the last day on which

ASIAN DEVELOPMENT BANK
ORDINARY CAPITAL RESOURCES
ILLUSTRATION OF IMPACT OF SUBSTITUTION OF 1966 DOLLAR WITH SDR[1/]
31 DECEMBER 1976
(Expressed in US$1,000)

	Before	Substitution: Restatement of Capital	Substitution: Increase (Decrease)	After
ASSETS				
Receivable from Special Funds		2,120	2,120)	
			)	
Total Assets	3,489,672		)	3,491,792
LIABILITIES	2,316,406		)	
			)	
Maintenance of Value Payable		32,711	32,711)	2,349,117
CAPITAL AND RESERVES				
Capital Subscribed	3,688,391	3,552,272	(136,119)	3,552,272
"Callable" Shares Subscribed	2,505,914	2,413,435	92,479	2,413,435
"Paid-In" Shares Subscribed	1,182,477	1,138,837	(43,640)	1,138,837
Subscription Instalments Not Yet Due	112,595	108,439	4,156	108,439
Instalments Matured	1,069,882	1,030,398	(39,484)	1,030,398
Capital Set-Aside for Special Operations	57,434	55,314	2,120	55,314

	Before	Substitution: Restatement of Capital	Substitution: Increase (Decrease)	After
Capital for Ordinary Operation	1,012,448	975,084	(37,364)	975,084
Reserves and Net Income	160,818		)	
Credit Arising from Restatement of Capital		6,773	6,773)	167,591
Total Liabilities, Capital and Reserves	3,489,672			3,491,792

1/ One SDR = $1,16183 at 31 December 1976.

Appendix 7

ASIAN DEVELOPMENT BANK
Maintenance of Value Due to Members if SDR Were Substituted for the 1966 US Dollar as the Unit of Value for the Bank's Capital

31 December 1976
(Expressed in US$1,000)

	Maintenance of Value Ceilings If Unit of Value Is		Amount Due to Members (Difference) 2/
	1966$	SDR	
Regional Members:			
Afghanistan	2,477	$ 2,386	91
Australia	82,032	79,005	3,027
Bangladesh	6,872	6,618	254
Burma	3,309	3,187	122
Cambodia	1,562	1,504	58
China, Republic of	7,970	7,676	294
Cook Islands	3	3	- 3/
Fiji	517	498	19
Gilbert Islands	32	31	1
Hong Kong	7,721	7,436	285
India	48,186	46,408	1,778
Indonesia	27,017	26,020	997
Japan	193,016	185,893	7,123
Korea, Republic of	31,054	29,908	1,146
Laos	217	209	8
Malaysia	27,497	26,482	1,015
Nepal	1,059	1,020	39
New Zealand	11,950	11,509	441
Pakistan	16,498	15,889	609
Papua New Guinea	700	674	26
Philippines	9,597	9,243	354
Singapore	4,211	4,055	156
Solomon Islands	49	47	2
Sri Lanka	4,370	4,209	161
Thailand	10,260	9,881	379
Tonga	31	30	1
Viet Nam	6,221	5,991	230
Western Samoa	7	7	- 3/
Total Regional	504,435	485,819	18,616

	Maintenance of Value Ceilings If Unit of Value Is 1966$	SDR	Amount Due to Members 2/ (Difference)
Non-Regional Members:			
Austria	4,825	4,647	178
Belgium	4,825	4,647	178
Canada	36,634	35,282	1,352
Denmark	4,825	4,647	178
Finland	2,807	2,703	104
France	24,127	23,237	890
Germany, Federal Republic of	39,942	38,468	1,474
Italy	19,302	18,590	712
Netherlands	10,616	10,224	392
Norway	4,222	4,066	156
Sweden	3,016	2,905	111
Switzerland	4,825	4,647	178
United Kingdom	28,953	27,884	1,069
United States	193,016	185,893	7,123
Total Non-Regional	381,935	367,840	14,095
Grand Total	886,370	853,659	32,711

1/ Paid-in capital or net currency holdings whichever is lesser.

2/ Assuming maintenance of value settlement has already been made in terms of the 1966 US Dollar or 1.20635 current US dollar.

3/ Too small.

Appendix 8

Response of Other International Institutions to New International Monetary System

A. IBRD and Inter-American Development Bank (IDB)

1. The Second Amendment to the IMF Articles and the changed international monetary system have presented issues, similar to those discussed in the Paper, to the IBRD and the IDB. The IDB has not yet decided what course of action to take to solve these issues. The IBRD Board of Directors is currently considering a proposal that an interpretation (not a formal amendment) of the IBRD Articles of Agreement be made along the lines proposed in the Paper, namely:

(a) that the 1944 dollar (the equivalent in the Articles of Agreement of IBRD to the 1966 dollar in the Bank's Articles) be interpreted as the SDR in the context of the new international monetary system. The interpretation method has been proposed mainly because of the severe time limitations for necessary action;

(b) that valuation of capital and maintenance of value be effected in terms of capital expressed in units of SDR. Specific details for application of the MOV provisions have not yet been formally proposed to the IBRD Board; and

(c) that the current U.S. dollar continue to be used as the unit of account or "reporting unit".

B. European Investment Bank (EIB)

2. Articles 4 and 7 of the Statute of the EIB define the capital of EIB in terms of a unit equal to 0.88867088 gram of fine gold (i.e. equal to the gold content of the 1966 dollar and

the SDR) and require MOV adjustments in the event of a change in the parity of a currency in relation to that unit. Since the validity of these provisions has been overtaken by developments in the world monetary system, steps were taken in July 1975 to formally amend the statute of EIB. As an interim measure, pending the effectiveness of the amendments (which are not yet effective), the Board of Governors authorized EIB to use a new system of capital valuation and conversion of currencies by reference to a special basket of European currencies determined in such a way that, as at 28 June 1974, the sum of the component currencies in the basket equalled the SDR through the common gold content of the EIB unit and the SDR.

3. Since the equivalent of the EIB unit of account expressed in member currencies varies on a daily basis, EIB, like the Bank, uses more stable conversion rates for internal accounting and statistical purposes. Thus the value of the EIB unit at the end of each quarter is used to prepare quarterly balance sheets at such dates and to record all operations during the following quarter.

Record Removal Notice

The World Bank Group Archives & Records Management

File Title	Barcode No.
Valuation of the Bank's capital - US, Asian Development Bank, Inter-American Development Bank - 1977 to 1978	1851279

Document Date	Document Type
December 14, 1977	Letter

Correspondents / Participants
To: Aron Broches, VP and General Counsel, IBRD
From: Graeme F. Rea, General Counsel, Asian Development Bank

Subject / Title
Proposed redenomination of the share capital of respective institutions in SDR, as a consequence of the second amendment to the IMF Charter.

Exception(s)
Information Provided by Member Countries or Third Parties in Confidence

Additional Comments

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Withdrawn by	Date
Bertha F. Wilson	February 23, 2018

Record Removal Notice

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File Title	Barcode No.
Valuation of the Bank's capital - US, Asian Development Bank, Inter-American Development Bank - 1977 to 1978	1851279

Document Date	Document Type
N/A	Note

Correspondents / Participants
Lester Nurick

Subject / Title
Inter-American Development Bank - steps being taken to increase the IDB's capital

Exception(s)
Attorney-Client Privilege

Additional Comments

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Withdrawn by	Date
Shiri Alon	April 20, 2017

LNurick:ldb
May 17, 1978

IDB - Valuation

Levinson told me that at the Board Meeting to consider the SDR matter held today, the following statements were made.

Japan: Anyone who proposes an amendment has the burden of approving the necessity for it. Levinson's legal opinion is okay.

Germany: Pressed very hard for both the interpretation and the SDR, saying the SDR was the only possible interpretation (with an exception that I did not get). They want a quick answer, within weeks, a short interim period and the decision to be retroactive to April 1.

U.S.: An amendment is "necessary". (This is different than the position they have, so far, been taking with us.) There is no other way to go; cautious about the SDR and wants a consideration of the practical effect of the SDR.

Some Latins (Uruguay and Colombia) also doubt whether an interpretation is legal for them because it involves a change in the literal language of the Articles. Brazil, however, agreed with the legal opinion. Mexico reserves on the question but do not want a decision quickly.

There should be complete coordination with the IBRD.

There will be a further Executive Directors meeting tomorrow, followed by informal consultations. No decision was reached.

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The World Bank Group Archives & Records Management

File Title	Barcode No.
Valuation of the Bank's capital - US, Asian Development Bank, Inter-American Development Bank - 1977 to 1978	1851279

Document Date	Document Type
April 24, 1978	Memorandum

Correspondents / Participants
To: Robert A. McNamara
From: A. Broches

Subject / Title
Standard of Value Inter-American Development Bank

Exception(s)
Information Provided by Member Countries or Third Parties in Confidence

Additional Comments

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Withdrawn by	Date
Bertha F. Wilson	February 5, 2018

Record Removal Notice

The World Bank Group Archives & Records Management

File Title	Barcode No.
Valuation of the Bank's capital - US, Asian Development Bank, Inter-American Development Bank - 1977 to 1978	1851279

Document Date	Document Type
April 10, 1978	Memorandum

Correspondents / Participants
To: The Board of Executive Directors, Inter-American Development Bank
From: The President, Inter-American Development Bank

Subject / Title
Standard of Value Under the Agreement Establishing the Inter-American Development Bank

Exception(s)
Information Provided by Member Countries or Third Parties in Confidence

Additional Comments

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Withdrawn by	Date
Shiri Alon	April 20, 2017