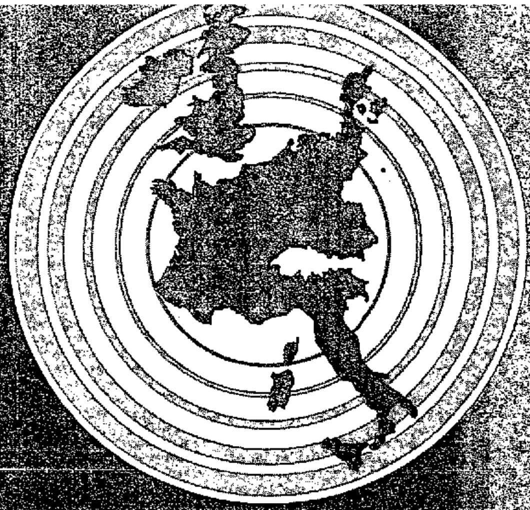
Report by the Commission on the monetary organisation of the Community (1973)

Caption: On 28 June 1973, the Commission of the European Communities submits a report to the Council on the adjustment of short-term monetary support arrangements and the conditions required for the progressive pooling of reserves.

Source: Bulletin of the European Communities. 1973, No Supplement 12/73. Luxembourg: Office for official publications of the European Communities. "Monetary organization of the Community".



Monetary organization of the Community

Commission
of the European Communities

Monetary organization of the Community

Economic and monetary union is to be established in the Community by 31 December 1980. This commitment was entered into by the Council in its Resolution of 22 March 1971 and reaffirmed by the Heads of State or Government at the meeting they held in Paris in October 1972.

Economic and monetary union means in particular that the Community must from a single monetary entity within the international system, characterized by the total and irreversible convertibility of its currencies, the abolition of margins of fluctuation for its exchange rates, the fixing of irrevocable parity relationships, which is essential to the creation of a single currency, and involving a Community-level organization of Central Banks which should assist in attaining the objectives of stability and growth in the Community.

A third of the time fixed for attaining the objectives of economic and monetary union has already passed and if the plan is to be seen through on time, measures must be taken to translate political declarations rapidly into concrete acts.

With the member countries' economies opening up to each other and becoming highly interdependent it is more and more urgent for an independent monetary system to be set up involving fixed but adjustable parities. In the enlarged Community, the main share of commercial and financial transactions is between Member States and this share is constantly growing. The cohesion and well-being of the Member States are very largely dependent on secure exchange rate relationships in these transactions. This is all the more important as, for a number of years, the international monetary system has been shaken by deep and repeated crises which seriously jeopardize the economic unification process between the member countries. Attempts are being made to reform the monetary system and the Community is using all its influence to help towards this reform, but it still cannot be said how much time will be needed and what shape the reform will take. The Community cannot go on enduring the uncertainty and the dangers this presents for further integration, as regards, in particular, the development of external trade or the establishment of a European capital market. The creation of a stable and lasting monetary system is just as important for making the necessary progress in other spheres of Community activities.

A Community system of Central Banks can only be arrived at progressively by increasing in successive stages the role played by the Monetary Cooperation Fund which is the embryonic form of this system. In fact the Commission feels that the objectives set for 1980 are such that a basic structure must be created immediately and be substantial enough to enable them to be achieved by the agreed date. This is the line taken by proposals that the Commission outlines in this report in accordance with the mandate it received: progressive pooling of foreign exchange, improvement of credit machinery with a stronger accent being laid on its Community nature, strengthening of the coordination of domestic monetary policies, Community watching brief on exchange rate policies, joint action on international monetary relations. In brief, the main proposals are as follows:

(i) Extension of the tasks of the Monetary Cooperation Fund with the gradual pooling of reserves beginning with an inital contribution of 20 % on 1 January 1974, to finish with all reserves pooled in 1980;

(ii) Improvement of credit machinery so that there are uninterrupted credit facilities ranging from automatic short-term loans to longer-term loans with specific economic policy conditions attached;

In the absence of effective coordination of economic policies this structure might seem fragile. The Commission already stressed this problem in its communication concerning the second stage, and proposed solutions concerning, *inter alia,* the adoption of additional measures concerning the coordination of monetary policies and concerning exchange rate policies.

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Based on a number of new measures and achievements extending throughout economic policy, the economic and monetary union must be the result of growing integration and solidarity between Member States and will clear the path for the European Union. Progress towards the creation of the Community's own monetary system is an expression of Community solidarity; it is a sign of the increasing unity of the Member States' economies, policies and objectives. This monetary system is at the same time a reflection of the need for the Community to ensure it acts as a single entity on the international economic scene and of its will to speak with one voice.

1. The Community's monetary organization is, at present, made up of various elements which do not fit together very well.

The principal feature of that organization is known as the 'Community's band of fluctuation' within which the widest possible margin between two Community currencies is limited at any given moment to 2.25 %. Intervention must be effected by the issuing authorities of the currencies at either extreme of this margin. These transactions are financed on an 'interim' basis under a system of very short-term credit (30 days—end of month), with no limits on amounts. Observance of the fluctuation margins may require substantial intervention for which the means of financing must be automatically available. Upon expiry of the time limit, the debtor central bank may either arrange for short-term monetary support to take over from very short-term credit, by initiating the procedure under the Agreeement between Central Banks of 9 February 1970, or settle the debt by transferring assets in accordance with the composition of its reserves.

Organizing the system whereby one form of credit takes over from the other is made extremely complex because both work on a basically bilateral basis. Furthermore, the working of both systems has been strongly impeded by the following difficulties:

(a) The short-term monetary support mechanism was worked out at a time when the dollar was the only intervention currency on the exchange markets; the procedures for operating it are therefore no longer entirely appropriate to present circumstances in which the dollar is not convertible.

(b) The limits placed on the credits available under the system, as regards both the amounts[1] and the duration[2] reduce the clearing possibilities between credit and debit positions.

(c) Finally, these settlement operations have run into increasing difficulties. The debtor central banks have shown more and more reluctance to hand over gold reserves at an official price which diverges considerably from the market price; the opposite attitude has been adopted as regard settlements in dollars. To palliate these difficulties increasingly complicated techniques of keeping accounts separate have been worked out.

When first considering the development of the Community monetary system, it was thought that the Community credit system should be adjusted by merging the credit facilities described above within overhauled machinery, to be followed by the progressive pooling of reserves. But while an 'adjustment of credit arrangements', both in volume and duration, would help improve clearing, it would still fail

[1] The quotas are as follows: Germany, France, U.K.: 300 million u.a. each; Italy 200 million u.a.; BLEU and the Netherlands: 100 million u.a. each; Denmark: 45 million u.a.; Ireland: 17.5 million u.a. Subject to the approval of the Committee of Governors of the Central Banks, the borrowing facilities of each central bank, which would normally be limited to its quota, may be extended up to an amount corresponding to the total quotas, that is, 1 362.5 million u.a.

[2] Utilization of the facilities within a maximum of one month, duration of credit three months, renewable once.

to eliminate the drawbacks deriving both from the bilateral bias of the credit mechanisms and from the complex nature of the settlement methods, itself due to the heterogeneity of the assets transferred.

Furthermore, intervention in dollars has always been kept outside the system of interim financing, clearing and settlement. It would not be desirable to maintain this attitude. The possibility of action having to be taken on the exchange rates of Community currencies against the dollar cannot be ruled out completely, and in such a case the question of the distribution of risks would inevitably arise. Besides, the Community's objective in the field of international monetary relations still is to return to stable but adjustable parities, and this would require, when the time arrives, resorting again to systematic intervention vis-à-vis the dollar.

The existing credit mechanisms must thus be improved so as to enable the Fund to achieve full multilateralization of all transactions on the exchange markets. For this objective to be attained, two essential conditions must be met:

(i) the Fund must be provided with its own resources which would enable it to act as a genuine intermediary between creditors and debtors within the Community and to asume responsibility for risks arising from intervention in dollars;

(ii) a unit of account must be adopted which would be used as a means of settlement between the monetary authorities and as a reserve instrument.

In other words, the very technique of the pooling of reserves must be adopted.

Finally, the pooling of dollar reserves would make it easier to consolidate the dollar balances, generally considered to be one of the main problems in the reform of the international monetary system. If part of the dollar balances were thus in the hands of a single body, the decisions which the Member States of the Community are aiming at in this field would be easier to take. Meanwhile the Fund would administer these balances, thus giving concrete form to the general policy of the Community as regards the involvement of member countries in international affairs.

2. This new stage in the monetary organization of the EEC must not involve the same risks that other similar Community attempts have encountered in the past (the system being generally called into question, individual derogations being applied to interventions and settlements, certain currencies withdrawing from the Community band). This is why it is important for the machinery set up to be in a form which clearly reflects that it is intended to be permanent and to be imposing enough to make those involved believe in it.

First of all, it is therefore recommended that Member States subscribe from their budgets a capital of 500 million u.a., to be paid into the European Fund. This total would be apportioned between the Member States according to the scale fixed for short-term monetary support set up under the Agreement of 9 February 1970.[1] The capital of the European Fund would be subscribed exclusively in currencies of Community countries. It would translate the legal personality of the Fund at financial level and would enable operating expenditure to be financed from the revenue it earns.

Two separate formulae should be used for pooling reserves:

(a) the progressive transfer to the Fund of official reserves (gold, assets linked to gold and dollars) accumulated in the past. The initial contribution could be of the order of 20 % of the total reserves of the EEC countries, which would be equivalent to a total in the region of 11 000 million u.a. (on the basis of a total of Community reserves of 56 000 million u.a. at the end of March 1973).

[1] The scale used in this agreement is the following (in %): Germany, France, UK: 22.02 each; Italy: 14.68; BLEU and Netherlands: 7.34 each; Denmark: 3.3; Ireland: 1.28.

(*b*) The surrender to the Fund of reserves newly acquired or transferred as a result of interventions in exchange markets.

The process of pooling should be completed in 1980 by the transfer to the Fund of Member Sates' total reserves. A fixed time-table could be laid down for the contributions to be made in the intervening period; at intervals of 18 months, for instance, calls could be made for additional contributions, raising the overall contribution successively to 40 %, 60 %, etc. of the total reserves held by the central bank at the time of pooling. Depending on the circumstances and on the extent to which economic policies have been harmonized, the Commission could propose to speed up or slow down the progressive pooling of reserves.

It is necessary to avoid any formula for the pooling of reserves which would result in this operation starting out half-heartedly and depending merely on the trend which the payments relationships between Member States happened to show. This would result if the method used consisted of pooling only reserves arising from intervention either in Community currencies or in dollars. In addition to being slow to take effect, such an operation could come up with results which were distinctly unequal as between the countries contributing to the pooling of reserves or between the assets built up in this way.

At present, and as long as the problem of the price of gold has not been settled, the contribution of this reserve asset poses a problem of evaluation. But it is not advisable to pool reserves without including gold, for the operation would then lose most of its credibility. In view of the uncertainty currently surrounding the price of gold it would be understood that once a new official price was fixed or a price was agreed between central banks, the Council would have to take a decision to make allowance for this new fact.

The balances which the monetary authorities would be credited with in the accounts of the Fund would be denominated in 'European monetary units of account', which would become a settlement and reserve instrument. These units would be available for the settlement of positions arising from intervention in Community currencies, and exchangeable, in the Fund, for foreign exchange to finance intervention vis-à-vis third currencies. This unit of account, since it would become a settlement and reserve instrument, would be guaranteed by the Fund, which constitutes a weighty argument in favour of contributions in gold.

3. Settlement and credit operations in the Community would be operated through the Fund, which would be the centre of exchange relations between Member States.

(*a*) As regards settlements, arrangements for credit to finance intervention would be maintained as they stand (no limit on amounts, 30 days-end of month). Upon expiry of these credit arrangements, the debtor central bank could settle either by a transfer of units of account in the Fund's books or by transfer of reserve assets to the Fund;

(*b*) In the case of credits, a Bank which did not wish to made an immediate settlement as above could make use of the Fund's credit facilities. In this second case, the Fund would grant the credit in accordance with the following rules:

(i) part of these credits would be used to create possibilities of clearing within the Fund and would be granted automatically; they would be for six months and renewable once; whenever they were renewed, an examination would automatically be carried out of the situation of the debtor country; ceilings on debts would be fixed at six times the quotas currently laid down for short-term support[1]; in concrete terms, a credit would be granted to a country by paying units of account into its account with the Fund;

[1] The basic quotas are as follows: Germany, France, UK: 300 million u.a. each; Italy: 200 million u.a.; BLEU and Netherlands: 100 million u.a. each; Denmark: 45 million u.a.; Ireland: 17.5 million u.a.

(ii) any credit needs beyond the limits on amount (six times the quotas currently laid down for short-term support) or duration (six months, renewable once) would require recourse to a procedure which would reflect the purely conditional character of the facilities granted; this procedure would, to begin with, involve an examination of the economic situation of the debtor country by the Commission, together with the Monetary Committee, followed by a decision by the Council. This decision could lead to the granting of an additional credit by the Fund or the granting of a medium-term credit; in both cases the Council would attach economic policy conditions.

(iii) the rules relating to the utilization of credit facilities and the ceilings on debts should be subject to review at a later date, for instance when the Member States make their successive contributions to the Fund.

The Commission will make proposals before the end of the year as regards profits and losses made by the Fund as a result of changes in the value of its assets.

If all the proposed measures are to be successfully put into effect, the economic policies of the Member States must be effectively brought closer together. If full use is made of all the various types of coordinating machinery available to the Community, it should be possible to maintain sufficient cohesion between the economies of the Member States for the proposed monetary organization to operate harmoniously. In connection with this joint Community-level application of economic policy instruments, it would also be necessary, and, at the same time, easier, to reinforce measures for the development of a European capital market. Community cohesion would also be strengthened if all the Member States were equipped with sufficiently effective instruments to ward off inflows of capital from abroad.

In the Commission's view, for the ideas outlined in this document to be given shape, there will be no need for new institutional measures to be adopted at the same time. However, there will have to be a firm political will to apply strictly the existing coordinating mechanisms and new means will be required in connection with exchange rate policy. The Commission stressed in its Communication to the Council of 19 April 1973 on the change-over to the second stage that it is not possible to do without parity adjustment in a monetary area in the process of being established, but any adjustments must be made under Community control by giving the Community a watching brief regarding changes in exchange relationships.

Article 107 of the Treaty of Rome provides that the Member States must treat their policies with regard to rates of exchange as a matter of common concern. It is now a question of giving concrete form to the application of this principle.

The utilization of reserves, changes in the emphasis on the various economic policy instruments and amendments to exchange rates are largely interchangeable. Exchange rate policies governing national currencies, under the pressure of increasingly heavier constraints as a result of the growing unity of the economies and the existence of a Community exchange rate system, must henceforth allow for the Community dimensions and not be the sole responsibility of the Member States.

It should also be stressed that no durable progress towards Economic and Monetary Union can be made, and that that Union cannot be viable, unless the Member States are all bound by the same principles as regards exchange policy.

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The main technical aspects of the guidelines set out in this report are discussed in the Annex. The Commission proposes to put forward a series of formal proposals to implement these guidelines.

The Commissions would like the Council, on the basis of the proposals which it will make following this report, to take the necessary measures to establish the European monetary system outlined above.

Technical Annex

Monetary organization of the Community

1. The present Community exchange rate system consists of elements which were placed side by side as required by circumstances and altogether is rather disjointed.

The rules of the Basle Agreement of April 1972 on the practical organization of the Community exchange rate system were drawn up and implemented in a period of major upheavals in international monetary relations: in less than three years the relatively narrow (1.5 %) spread ('tunnel') within which the currencies may fluctuate against the dollar grew wider (4.50 %), then disappeared completely after 19 March 1973. The rules of the Agreement on the narrowing of margins have had to be frequently adjusted, with respect in particular to settlements in gold and dollars, and there is still no sign that this process has come to an end.

The short-term monetary support mechanism set up by the Agreement between Central Banks of 9 February 1970, is based on notions belonging to the time when the dollar was the only intervention currency and no concrete plans existed for the Community to have its own monetary exchange rate system.

The introduction of the European Monetary Cooperation Fund in relations that have continued on a fundamentally bilateral basis, has not made the very complex system any simpler.

2. In this respect, the following points should be made:

(i) Banks accounts are kept according to category of maturity corresponding to the settlement date for a given operation, so that a Central Bank can be in credit with the Fund at the same time but with different maturity dates.

(ii) Clearing, the frequency of which reduces the size of settlements, is the exception rather than the rule, for the length of 'interim financing' is very short and the procedure for providing short-term monetary support was not designed with this in mind.

(iii) The arrangement for monetary support to take over from very short-term facilities is not well suited to present exchange rate circumstances.

(iv) Intervention in dollars, which was compulsory under the arrangements applying prior to 19 March and which today is possible only after a joint decision, is formally excluded from the Fund's accounts, although it is of a Community nature.

(v) Depending on the nature of the operations, the Fund has had to resort to accounting techniques involving various types of units of account in view of the fact that settlements must be made in proportion to the composition of the reserves of the debtor country and that the attraction of these elements varies greatly according to whether gold, SDRs or dollars are involved.

3. In calling on the Commission to report on adjustments to credit arrangements and on the progressive pooling of reserves, the Council provided an opportunity to seek means of reforming the entire system.

It had originally been thought that in the first stage, arrangements merely had to be made for one type of credit machinery to take over from another—very short-term credit facilities being followed by short-term monetary support —without modifying their essential characteristics. It had been intended to merge these two formulas in the second stage and fit them into one piece of 'overhauled machinery'. Finally, in a later stage, reserves were to be progressively pooled.

In Part I of this Annex, the problems raised by the 'adjustment of credit arrangements' will be examined. It will be seen that some of the difficulties encountered in organizing the process whereby one credit facility takes over from another cannot be solved simply by adjusting credit arrangements. In Part II, the technical details of a progressive pooling of reserves will be looked at.

Part I

Adjusting credit arrangements

4. The action to be taken would have to relate mainly to improving the details of the arrangement under which short-term monetary support takes over from very short-term credit. It would be based on the following principles:

(a) The provisions of the Basle Agreement permitting the running up of unlimited debt for a very short period would be retained.

(b) When these financing facilities matured, the debtor would have a right to have the credit extended up to a specific amount and duration[1] but would have to settle in reserve assets the portion of his debt above this amount.

(c) The credit obtained to this end through the Fund would in practice be granted by the initial creditor. In other words, this creditor would continue to have a claim on the Fund in u.a. equivalent to the amount of the credit.

(d) This claim would rank as a reserve asset,[2] for it would be guaranteed by all participating central banks and could be mobilized if needed. This would be done in the following way:

(i) if the currency of the initial creditor had in its turn to be supported through intervention in a Community currency, the resulting indebtedness would be set off against the original claim. A new creditor would take the place of the initial creditor; he would have the same rights and obligations as the former.

(ii) in the case of intervention in dollars (selling), the initial debtor would be free to mobilize his claim on the Fund against dollars; to this end, the Fund would be able to draw on

[1] The limits on amount and duration could be those outlined in Part II, Section B II.
[2] The credit position in European monetary units of account (u.a.) with the Fund would form an integral part of the official reserves of each central bank.

credit lines in dollars with the participating central banks. Use of these credit lines would give rise to a claim in u.a. on the Fund[1].

(e) At fixed dates, for instance on 30 June and 30 December of each year, the accounts would be cleared. This lumping together of maturities, while encouraging clearing, would put the debtor at a disadvantage where the period of the credit obtained was not fixed but varied with the date on which the credit was taken up.

(f) To prevent the credit period being shortened in this way, the Fund would ask central banks able to do so to grant ad hoc credits (i.e. credits with specifically tailored amounts and periods) permitting settlement with the creditor on the appointed day and enabling the credit to the debtor to be maintained until the normal maturity date.

5. This adjustment would improve the current system appreciably: the process of one of the two types of financing taking over from the other would be more effective, particularly because it would be automatic up to the ceilings fixed; there would be increased possibilities of clearing, which would reduce the size of settlements.

6. However, there would still be some deficiencies:

(i) Adjustment of the credit arrangements would not eliminate the fundamentally bilateral character of the credit mechanisms. Though transactions in Community currencies would have to pass through it, the Fund would not be a genuine intermediary capable of ensuring conversion designed to put the relationships between central banks on a fully multilateral basis. In the circumstances, the accounting and settlement methods would remain complex, and the Fund could not avoid keeping accounts separate and using a variety of units of account because of the heterogeneity of the assets transferred between central banks.

(ii) As the granting of ad hoc credits would require the assistance of the central banks, the debtor would have no guarantee of obtaining the credit for the whole period which he would normally be entitled to.

(iii) Any intervention in dollars would remain outside the scope of interim financing, clearing and settlements, which would be abnormal in a system under which such intervention must necessarily be based on concerted action. Given the Community character of the decision to which this procedure leads, it would be equitable to share out the relevant risks among all participants.

To get round these difficulties, consideration could be given to setting up a continuous clearing system under which the Fund, drawing on a 'buffer' formed by its own reserves, would finance the period between the date for settlement with the creditor and repayment by the debtors on normal maturity of the credit. But this technique would be precisely that of pooling reserves.

It can therefore be seen that from a technical point of view the pooling of reserves is indispensable. The only question is whether for non-technical reasons this pooling should involve successive contributions leading to the complete pooling of reserves. The main part of this document sets out reasons which, from a Community angle, argue for this approach.

[1] Action on the dollar in the form of buying would continue to be for the party's own account.

Part II

Progressive pooling of reserves

Three questions will be examined: the choice of the method for pooling reserves, the advantages of pooling from the point of view of settlement and credit arrangements and certain important points connected with this pooling.

A. *Methods of pooling reserves*

Reserve assets and holdings of Community currencies

7. The first question is whether it is not only reserve assets that are to be pooled, but also holdings of currencies of the Community countries. At first sight, it could be felt that handing over to the European Fund large amounts in currencies of the Member States was quite natural in a Community enterprise. Then the Central Bank whose currency required support would no longer turn directly to the Central Bank whose currency had appreciated to obtain the resources necessary to finance intervention, but to the Fund instead.

Under closer examination, however, this argument proves to be weak: it should be recalled here that the financing of interventions can, under certain circumstances, involve extremely large sums (in the case of speculative attacks on a currency, for instance) which exceed the amounts of national currency which might have been handed over to the Fund; the Fund would then have to make a special call on the creditor central bank. It can then be asked what would be gained by setting up such cumbersome financing mechanisms, when use could be made of those which already exist and which require each central bank to grant, through the Fund, unlimited credits in its currency to the partner central banks for a very short period. Retaining direct financing operations between central banks in no way detracts from the Community nature of an undertaking which would be based on a unit of account acting as a means of settlement and a reserve instrument within the Fund.

The idea of supplying the Fund with amounts in national currencies had also been put forward to make the overhaul of Community credit arrangements easier. It will be shown below that a credit system can operate very well without contributions in national currencies having to be made to the Fund.

Methods of contributing reserve assets

8. Two separate formulae exist for pooling reserve assets alone:

(*a*) the transfer to the Fund of reserves newly acquired

(i) from intervention in dollars,

(ii) from intervention in Community currencies.

(*b*) the transfer to the Fund, as an initial contribution, and afterwards at a fixed pace, of official reserves accumulated in the past in the form of gold, assets linked to gold and foreign exchange, mainly dollars.

If the first method alone was chosen, the decision to pool reserves would, at the beginning, appear half-hearted, whereas the Fund needs to be given massive resources if the credit system it is administering is to operate satisfactorily. It is probable that, as regards intervention in dollars, in a system where such intervention is no longer systematic, this method would be slow to take effect and would create inequalities; for example, only countries buying dollars (non-guaranteed) would transfer these to the Fund in exchange for units of account (with a guaranteed value). As regards intervention in Community currencies, the pace of contributions would, in the present circumstances, be less slow and the inequality less marked, for it can be assumed that there would be a certain rotation between debtor countries which would, in settling up, contribute to the Fund a range of different reserve assets (gold, assets linked to gold, dollars) in proportion to the composition of their reserves.

It can then be seen that even if this method is necessary for risks that would be involved in any intervention in dollars to be underwritten on a Community basis, it would still have some deficiencies that would have to be made up by contributing reserves built up previously. It would be essential to make use of this second method, for it alone would offer the possibility of fixing the exact initial contributions, of making detailed arrangements for subsequent contributions and of distributing evenly transfers of reserves to the Fund. It would also make it possible to set up truly Community credit machinery. Finally, as it is being assumed that all reserves will have to be pooled in the present decade, only with this method is it possible to do it progressively.

The two methods set out above must therefore be used together. The following paragraphs describe how they would be implemented.

Description of the process for pooling reserves

9. *(a) Settlement of intervention in Community currencies*

Intervention in Community currencies already involves entries, in units of account, in the Fund's books. The central bank which has lent the currency for this operation has its account credited and the central bank borrowing the currency has its account debited. These positions must be settled—by transfer of reserve assets to the creditor—within short periods.

Following pooling, the operations would be effected as follows:

(i) the central bank would receive from the Fund a credit in monetary units of account as a final settlement;

(ii) the debtor bank would clear its position by transferring reserve assets to the Fund.[1] This settlement would be made:

- on the date when the very short-term facility falls due, or

- at a later date if the facility has been extended by a credit from the Fund, the terms of which are discussed in section B below.

(b) Financing interventions vis-à-vis the dollar

Normally, any interventions vis-à-vis the dollar would have a Community character because they would influence the position of the 'snake'. Financing and bearing the exchange risks connected with these interventions would therefore have to be regarded as Community operations:

(i) the dollars purchased would be handed back to the Fund against a credit entry in u.a.,

(ii) the dollars sold would be obtained from the Fund against a debit entry in u.a.

However, the Board of Governors of the Fund should remain free to vary application of this principle in accordance with circumstances.

In the present situation, a country may for instance wish to restrict the appreciation of its currency against the dollar while its partners would be prepared to let this movement continue. In this case, the dollars which the country concerned purchased with the authorization of the Fund, would be purchased on that country's own account; they would not be handed over to the Fund but would remain with the central bank making the intervention.

According to the same principle it could be conceived that a country whose currency tended to be used as a reserve instrument could, with the authorization of the Fund, use its dollar holdings when the balances in its own currency had been run down.

[1] The credit position in European monetary units of account (u.a.) with the Fund is an integral part of each central bank's official reserves.

(c) Feeding the Fund through pooling official reserve holdings

This type of pooling would cover all components of official reserves: gold, SDRs, reserve position in the IMF, foreign exchange holdings.[1]

However, certain legal difficulties over the transfer to the European Fund of reserve positions in the IMF and of SDRs would have to be solved beforehand. For the reserve positions no solution seems in sight at the moment. As regards the transfer of SDRs, however, one could envisage applying to the IMF for the European Fund to be given the status of 'other holder'.

Ways of calculating the contributions

10. The contributions of reserve assets can be made according to two methods: either as a uniform percentage of the reserves of each central bank, or by reference to quotas.

Under the percentage method each central bank would transfer to the Fund an identical proportion of its reserves, in successive tranches. The composition of the contribution would reflect the share of the individual reserve assets in the country's total reserves. The table below shows how this method would be applied, assuming that reserves worth 11 300 million u.a., or about 20 % of all official reserves of the Community countries at the end of March 1973, would be pooled.

Under the quota method each central bank would pay into the Fund reserve amounts fixed by reference to its share in the capital of the Fund. As under the previous method, the contribution made by each central bank would be such as to reflect the share of the individual reserve assets in total national reserves.

A comparaison of the two methods shows that:

(i) the 'identical percentage' method enables pooling to be staggered without difficulty up to the end period envisaged for the operation There would be a timetable for the contributions: they would have to be made at intervals of 18 months so that each country's total contribution would rise successively to 40 %, 60 %, etc. of its total reserves at the time when the contributions were due. The other method, however, would cause the total reserves of a given country to be exhausted before the end of the period, which means that it could be used for a few years only.

(ii) the quota method provides an automatic solution to the allocation of risks and gains on reserves built up previously which have been pooled; as this allocation would be made in proportion to the contributions, the consequence of such 'losses' or 'gains' for a country would be the same, regardless of whether its reserves had been pooled or not. This neutral effect would, however, be lessened when reserves were contributed in connection with intervention on the foreign exchange markets.

In the light of this comparison, the identical percentage formula seems to be the most satisfactory solution.

At present, and as long as the problem of the price of gold has not been settled, the contribution of this reserve asset poses a problem of evaluation. But it is not advisable to pool reserves without including gold, for the exercise would then lose most of its credibility. Consequently, in view of the uncertainty currently surrounding the price of gold, it would be understood that once an agreement was reached at international level or between the Community Central Banks on the price of gold, the Council would have to take a decision to make allowance for this new fact.

Furthermore, a solution would also need to be found to the matter of allocating the revenue

[1] Excluding the small amounts of various currencies held by the central banks with their correspondents, amounts which in most cases relate to the role of Treasury accountant played by the central bank concerned.
See annexed table on the total level and composition of Member States' official reserves as at the end of March 1973.

Breakdown, by country and reserve asset, of a contribution of 11 300 million u.a. made to the Fund in accordance with the 'identical percentage' method (20 %)

Country	Total contribution (in mill. u. a.)	As a percentage of the country's total reserves	Contribution in gold or in assets linked to gold (in mill. u. a.)	As a percentage of the country's relevant holdings	Contribution in foreign exchange (in mill. u. a).	As a percentage of the country's relevant holdings
Belgium/Luxembourg	807	20	502	20	305	20
Denmark	178	20	40	20	138	20
Germany (FR)	5 251	20	1 207	20	4 044	20
France	1 854	20	912	20	942	20
Ireland	173	20	18	20	155	20
Italy	1 037	20	711	20	326	20
Netherlands	999	20	619	20	380	20
United Kingdom	1 001	20	294	20	707	20
Composition of Fund's holdings	11 300	100	4 303	38.1	6 997	61.9

Breakdown, by country and reserve asset, of a contribution of 11 300 million u.a. made to the Fund in accordance with the quota method[1]

Country	Total contribution (in mill. u. a.)	As a percentage of the country's total reserves	Contribution in gold or in assets linked to gold (in mill. u. a.)	As a percentage of the country's relevant holdings	Contribution in foreign exchange (iu mill. u. a.)	As a percentage of the country's relevant holdings
Belgium/Luxembourg	829	20.5	516	20.5	313	20.5
Denmark	373	41.8	84	41.8	289	41.8
Germany (FR)	2 488	9.5	572	9.5	1 916	9.5
France	2 488	26.8	1 223	26.8	1 265	26.8
Ireland	145	16.7	15	16.7	130	16.7
Italy	1 659	32.0	1 138	32.0	521	32.0
Netherlands	829	16.6	513	16.6	316	16.6
United Kingdom	2 488	49.7	730	49.7	1 758	49.7
Composition of Fund's holdings	11 299	100	4 791	42.4	6 508	57.6

(1) Rounded figures.

Credit ceiling for each country

(u.a. millions)

Belgium/ Luxembourg	Denmark	Germany (FR)	France	Ireland	Italy	Netherlands	United Kingdom
600	270	1 800	1 800	105	1 200	600	1 800

earned by the Fund from the investment of the transferred reserve assets. This problem bears no resemblance to that of possible exchange rates gains. It is proposed that this revenue should be allocated to the central banks in proportion to the participation of each Member State in the capital of the Fund.

B. *Community settlement and credit arrangements following the progressive pooling of reserves*

General principles

11. By pooling reserves it would be possible to strip the settlement and intra-Community credit machinery of the bilateral characteristics that remain attached to it—even after the overhaul—and the shortcomings of which were mentioned above.

After pooling, the Fund would no longer be an 'intermediary' institution through which settlement and credit operations between the Member States pass, but would become the organ which itself settled up with the creditor and lent to the debtor.

The following machinery is envisaged here:

(i) Very short-term financing (30 days from the end of the month in which the credit is granted) would continue as at present;

(ii) Far-reaching changes would be made in short-term credit arrangements, as regards the amounts involved, the duration of the credit and the conditions under which it was granted. There should be no link between the amount of reserves contributed and the ceiling fixed. If the percentage method was used for the pooling, such a link would have undesirable results, for countries of comparable economic size would end with vastly differing credit possibilities.

Taking into account firstly the amounts and the duration of credits likely to improve possibilities of using clearing in the Community exchange rate system, and, secondly, 'reasonable' levels of indebtedness, ceilings could be fixed at six times the quotas granted the Member States under the short-term monetary support mechanism.[1] These ceilings could be adjusted later. The table above gives the amounts proposed.

Credit up to the above ceilings would be granted automatically for a period of six months with the possibility of being renewed once. Any renewal would result automatically in the situation of the debtor country being examined. Where credit needs exceed the limits on amount or duration, a procedure would have to be used which reflected the strictly conditional character of the facilities granted.

Method of implementation

12. The Fund's accounting procedure would need to distinguish between the u.a. obtained

[1] The short-term monetary support quotas are as follows: Germany, France, United Kingdom: 300 million u.a. each; Italy: 200 million u.a.; BLEU and Netherlands: 100 million u.a. each; Denmark 45 million u.a. and Ireland: 17.5 million u.a.

against reserves handed over and the u.a. representing credits obtained. A country should be able to obtain credit even before it has begun to draw on its reserves, including its holdings in u.a. For operational reasons it would be advisable to record separately the various types of credits a country had received.

Each central bank would thus have three separate accounts with the Fund:

(i) a 'reserve' account with an initial credit entry corresponding to the reserves contributed;

(ii) a 'very short-term financing' account on which the amounts necessary for support intervention would be debited;

(iii) a 'short-term credit account' recording the short-term credits received from the Fund.

Thus, when intervention is made in Community currencies, the Fund would record the operations in the various accounts as follows:

(*a*) The Fund would settle up immediately with the central bank providing the hard currency by crediting its reserve account with the equivalent, in u.a., of the amount of its currency sold when intervening.

(*b*) The Fund would debit the same amount to the 'very short-term financing' account of the central bank whose currency was supported. At the present time there is no ceiling on this type of finance, but the position must be cleared by the debtor central bank at the end of the period agreed (end of month, 30 days). This would be done by the following methods, used separately or jointly:

(i) debiting the reserve account with the Fund;

(ii) handing over reserve assets not yet transferred to the Fund, in proportion to their relative share in the debtor's total reserves;

(iii) having short-term credit take over from very short-term finance up to the amounts available under this head.

C. *Points connected with the pooling of reserves*

13. Two major points deserve to be mentioned in connection with the new stage in the monetary organization of the EEC.

Capital of the Fund

Under the proposals set out in this document, the Fund, a legal personality, takes on a major monetary role. The Fund should be provided with its own capital to mark this stage.

This capital, amounting to 500 million u.a., would be subscribed in Community currencies from the Member States' budgets. This capital would be apportioned between the Member States in accordance wih the scale fixed for 'short-term monetary support' and could be paid up in successive tranches, for insistance at the same pace as reserves are pooled.

Giving the Fund its own capital could enable it to finance its operating expenditure from revenue obtained from the investment of its resources. Futhermore, this capital could be used as the scale for allocating the revenue earned from the joint management of the reserve assets.

Larger role for the European monetary unit of account

The instrument used for the pooling of reserves would be the European monetary unit of account (EMUA), a definition of which was given in Article 5 of the Statutes of the European Fund. This unit would not only serve for keeping the accounts on the Fund's operations but would also become a payment and reserve instrument.

Against this background it must be asked whether or not the present definition of this unit of account should be reviewed. Here, the idea is sometimes floated that the value of this instrument should be defined on the basis of the currencies of the participating countries. This would mean linking the value and adjustments in the value of this unit mainly to the value of the component currencies rather than to monetary events outside the Community.

Level and composition of the official reserves of the countries of the European Community

(situation as at the end of March 1973)

Country	Total reserves		Holdings in gold or in assets linked to gold			Holdings in foreign exchange		
	Amount (in mill. u. a.)[1]	As a percentage of EC reserves	Amount (in mill. u. a.)[1]	As a percentage of the reserves of: The country	As a percentage of the reserves of: The EC	Amount (in mill. u. a.)[1]	As a percentage of the reserves of: The country	As a percentage of the reserves of: The EC
Belgium/Luxembourg	4 034	7.1	2 512	62.3	11.7	1 522	37.7	4.4
Denmark	892	1.6	200	22.5	0.9	692	77.5	2.0
Germany (FR)	26 255	46.5	6 034	23.0	28.1	20 221	77.0	57.8
France	9 269	16.4	4 558	49.2	21.2	4 711	50.8	13.5
Ireland	867	1.5	91	10.5	0.4	776	89.5	2.2
Italy	5 182	9.2	3 554	68.6	16.5	1 628	31.4	4.7
Netherlands	4 995	8.8	3 093	61.9	14.4	1 902	38.1	5.4
United Kingdom	5 003	8.9	1 467	29.3	6.8	3 536	70.7	10.1
Community	56 497	100	21 509	38.1	100	34 988	61.9	100

([1]) 1 u.a. = 0.888671 g of fine gold = 1.20635 US $.