

## Ministry Paper No. 50

# **LIBERALIZATION OF EXCHANGE CONTROL REGIME**

### **A. INTRODUCTION**

**T**HE Government has repeatedly stated its intention to remove exchange controls on a phased basis so as to remove the distortions created in the economy by the existence of these regulations. Measures towards this end have been implemented over the past fifteen months. These include the introduction of the Inter-bank Foreign Exchange System, the development of the Foreign Currency "A" and "B" Accounts, and the expansion of the Retained Accounts for foreign exchange earners.

The operation of the Foreign Exchange Market in recent months has led to a situation whereby Government is now of the view that the time is opportune for moving to full liberalization of the Exchange Control Regime and the decision has been taken to implement such a regime with effect from September 25, 1991.

### **B. MACRO-ECONOMIC POLICY**

The successful implementation of a fully liberalized regime requires that during the transitional period the Government will be obliged to pursue very tight demand-management policies with the aim of stabilizing the exchange rate.

Fiscal policy will have to be operated in such a manner in relation to both Central Government and the Public Enterprises that the targeted overall Public Sector Deficit is not exceeded. With regard to the Central Government, the unanticipated increases in expenditure arising for example, from flood damage, and the increase in debt service payments brought about by the devaluation of the Jamaica dollar, will have to be compensated for by revenue increases or by expenditure cuts or a combination of both.

As far as the Public Enterprises are concerned, cost increases will have to be passed on in the form of higher prices where the enterprise sells its services to the public or by expenditure cuts, where the pricing route is not available.

As part of the macro-economic policy mix, the Bank of Jamaica will, in the short run, have to pursue a very aggressive open market policy which is likely to lead to increases in interest rates so as to cut domestic credit demand and correct the existing situation where interest rates are substantially negative.

To the extent that Government can increase its intake of funds from divestment above the programmed level, this will help to absorb liquidity from the system and reduce the need for open-market operations by the Bank of Jamaica. The Government will, therefore, make every effort to speed up the divestment process.

### C. THE LIBERALIZED REGIME

The movement from the present system to the new Liberalized Regime will involve the following:

- (1) Exporters and all other earners of foreign exchange will be free to hold these earnings in foreign currency accounts locally or abroad and to utilize same for meeting their foreign obligations. To the extent that they need to convert foreign exchange into domestic currency, they will be required to do so through an authorised dealer.
- (2) A corollary of (1) above is that all current account payments will now be free of any restrictions. Capital account payments will also be free with the following exceptions:
  - (i) *Financial institutions such as Life Insurance Companies, Commercial Banks, Merchant Banks, Trust Companies, Finance Houses, Building Societies, Unit Trusts, Pension Funds, Credit Unions, and any other organizations which are repositories for the financial savings of the society, will be required to match their Jamaica dollar liabilities to their clients with Jamaica dollar assets and will not therefore be free to diversify their investments into other currencies.*
  - (ii) *Where individuals and companies have Jamaica dollar accounts which were blocked by previous Exchange Control decisions, these funds will be released in line*

*with a time-table to be agreed with each concerned person after a stock-taking and assessment has been carried out.*

- (3) As at present, capital inflows including portfolio investment, will be free of any exchange control restrictions. The Government is developing an Investment Code dealing with the rights and obligations of investors.
  - (4) A further corollary of freeing exporters and other earners of foreign exchange from the requirement to repatriate is that all Retained Accounts including those for Exporters, Hotels, Villas and Apartments, U-Drive Operators, In-Bond Operators, and other tourism interests, will be abolished. Compulsory sales to the Jamaica National Retained Account (JNRA) by the tourism sector will no longer be required. However, on a voluntary basis, the tourism industry may wish to continue a similar centralised collection system if they find this convenient.
- The originally proposed scheme whereby 2.5 per cent of export proceeds was being collected by the Bank of Jamaica to assist in the financing of Linkage Companies will be abolished. Funds collected to date will be sold to the Linkage Companies on the basis of the agreed formula at the prevailing market rate.
- (5) The existing mechanism for settlement of CARICOM transactions will no longer continue and exporters to and importers from CARICOM will need to make their own arrangements for settling their transactions. Any CARICOM currency balances held by Jamaican banks as at Friday, September 20, 1991, can be applied by these institutions towards settlement of obligations in the respective countries.
  - (6) The Bank of Jamaica will eventually restrict its provision of foreign exchange to the servicing of the Public External Debt, making payments in respect of Government Diplomatic Missions, and any other essential requirements of the Government. The Bank will move as quickly as possible to divest responsibility for purchasing foreign exchange for Government entities including Petrojam.
  - (7) Any Company or person having payments to make to Government which by agreement or law (such as the Bauxite Levy), are payable in foreign exchange, will

continue to make such payments directly to the Bank of Jamaica. The foreign exchange proceeds of loans to Government or to Government Agencies will also continue to be paid to the Bank of Jamaica. In order to acquire any additional amounts of foreign exchange required to service the Public Debt and to meet other Governmental obligations indicated above, the Bank of Jamaica will be free to enter the market and buy foreign exchange from any persons and companies at rates to be published each day by the Bank. Where the Bank of Jamaica needs more foreign exchange than is obtained from its purchases from the sources mentioned above, it will purchase from the commercial banks and other authorised dealers on the same basis as the private sector, i.e. at the selling rate of the commercial banks.

- (8) Payments due to persons who exercised Option C in respect of Commercial Arrears outstanding at September, 1990, will continue to be paid out in foreign exchange by the Bank of Jamaica on the basis of the agreed schedule, and at the guaranteed rate of exchange. Any creditor who wishes to withdraw from the scheme will be refunded his Jamaica dollar deposit and be free to purchase foreign exchange from the market at the prevailing market rate.
- (9) Persons who exercised Option A in respect of the Commercial Arrears indicated above, i.e. those who opted for bonds denominated in United States dollars but payable in the Jamaica dollar equivalent, will continue to receive these payments in line with the agreed schedule.
- (10) "A" Accounts
  - (i) *Non-residents will be able to continue to hold tax-free "A" Accounts on the existing terms.*
  - (ii) *Residents will be free to maintain Foreign Currency Accounts locally or abroad but these will be subject to the ordinary tax laws of Jamaica and the foreign country. All balances held in "A" Accounts by residents as at Friday, September 20, 1991, will continue to enjoy up to the time of their withdrawal or use whatever privileges they now enjoy such as tax-free interest and freedom to use the funds for whatever purpose. Residents will not be able to open new "A" Accounts or to add to existing balances held in such accounts.*

- (11) "B" Accounts
  - (i) *Non-residents will continue to be able to hold "B" Accounts on the existing terms.*
  - (ii) *Residents will be allowed to have tax-free "B" Accounts provided that they are restricted to Certificates of Deposit with a minimum duration of one year. Withdrawal before the end of the one-year period will nullify the tax-free status.*
- (12) The stipulation that tourists should pay their hotel bills and certain other expenses in Jamaica dollars will no longer be applicable. Under the new foreign exchange system, tourists will be able to settle all bills and make other payments in any currency acceptable to the provider of the service.
- (13) It will still be necessary for anyone carrying on the business of trading in foreign exchange to hold a license. Commercial banks and other licensed foreign exchange dealers will be free to buy and sell foreign exchange at market rates, spot and forward, as perceived by themselves. Net retention of foreign exchange by dealers will be subject to guidelines laid down by the Bank of Jamaica.
- (14) The Bank of Jamaica will continue to undertake arrangements for collecting information on foreign exchange trading and rates from banks and other authorized dealers and publishing this information.
- (15) There will be a continuing need for authorized dealers to collect the necessary information to satisfy themselves from the point of view of prudent banking that they are not parties to illegal transactions such as money laundering or the transfer out of the country of criminal gains from theft or extortion.
- (16) In order to facilitate the detection of money laundering and other similar illegal activities, there will be regulations prescribing reporting requirements in respect of the importation into and the export from Jamaica of both foreign and domestic currency notes exceeding US\$10,000 and J\$150,000 respectively. As regards the deposit of cash (i.e. currency notes) into bank accounts in Jamaica, the Basle Agreement provides guidelines which commercial banks in Jamaica will be required to observe.



#### D. LEGAL ASPECTS OF LIBERALIZATION

Exchange Control in Jamaica is imposed by the Exchange Control Act, Law 50 of 1954. The Act almost totally consists of prohibitions, but each prohibition exists only in so far as the permission of the Minister has not been given. To this extent the Act is restrictive or liberal according to the mode of operation by whatever administering agency is responsible.

The intention is to repeal the Act. This is however, not immediately possible, as a number of provisions need to be retained. These concern restrictions that normally would be found in other laws but have traditionally been dealt with under Exchange Control. As soon as the relevant other laws can be passed or amended, the Exchange Control Act will be repealed, and in this respect the current steps being taken represent the final stage in the process of liberalization.

To achieve the current exercise, use is being made of section 45 of the Act which enables the Minister, by order, to amend the Act, and to suspend the operation of all or any part of the Act. This is similar to what was effected in the United Kingdom in 1979 when exchange control was almost totally suspended under a similar order.

The Order, the Exchange Control (Removal of Restrictions) Order, 1991, accordingly, indicates the Parts and Sections of the Act which are being suspended. Among the major innovations are the following:

- ( i ) persons who earn or receive foreign currency are now free to retain it, both here and overseas;
- ( ii ) all dealings in securities by residents and non-residents are now permissible;
- (iii) payments of all kinds for imports or other obligations are now permitted.

As indicated above, certain items have to be retained until they can be accommodated under other legislation, and these consist of the following:

- ( i ) It is normally required the world over, for persons dealing in foreign exchange as a business to have a license to do so. The system of and the current list of authorised dealers is therefore, being preserved, and in time, other institutions, primarily those which are under a regime of supervision, will be authorised. No person will be per-

mitted to carry on this business without a license, and any person who buys foreign currency with Jamaica dollars, MUST buy from an authorised dealer and any person who sells foreign currency for Jamaica dollars, must sell to an authorised dealer.

- ( ii ) In order to allow banks to pay out blocked accounts in accordance with a time-table agreed between each holder of such account and the Bank of Jamaica, the relevant portions of the existing provisions are being retained for the time being. No new blocked accounts can be established.
- (iii) Financial institutions which attract and hold the savings of the public, will be subject to directions from the Minister or Bank of Jamaica as to the amount of foreign currency holdings or instruments they may hold at any given moment. This is a prudential requirement, not an exchange control restriction, and is applied in most countries.

As early as the relevant legislation can be implemented, the above will be transferred elsewhere. Provision will be made for the licensing of dealers, the payment out of blocked accounts can be dealt with administratively between each bank and the Bank of Jamaica, and the prudential provisions in respect of foreign currency holdings can be dealt with both in the Bank of Jamaica Act, and in the relevant Act under which the Financial institution exists. In addition, investment legislation both for incentives and appropriate monitoring will be introduced.

Finally, it is necessary to retain, for the time being, sanctions against non-compliance with the above requirements, and accordingly, the provisions for enforcement contained in the Fifth Schedule to the Act, continue to apply.

The relevant Order, the Exchange Control (Removal of Restrictions) Order, 1991, to come into effect on the 25th September, 1991, has been tabled, and a copy is attached to this Ministry Paper for the benefit of the House.