

## II

### General Department

#### Introduction

The IMF's resources are held in the General Department, which consists of three separate accounts: the General Resources Account (GRA), the Special Disbursement Account (SDA), and the Investment Account.

#### General Resources Account

The GRA is the principal account of the IMF and handles by far the largest share of transactions between the IMF and its membership. The GRA can best be described as a pool of currencies and reserve assets built up from members' fully paid capital subscriptions in the form of quotas.<sup>1</sup> Quotas are the basic building blocks of the IMF. They broadly reflect each member's relative economic size, taking into account the quotas of similar countries. Quotas determine the maximum amount of financial resources that a member is obligated to provide to the IMF, voting power in IMF decision making, and a member's share of SDR allocations. The financial assistance a member may obtain from the IMF is also generally based on its quota.

The financial structure of the IMF rests on the principle that quota subscriptions are the basic source of financing for the GRA. A quarter of a member's quota subscription is normally paid in reserve assets, with the remainder paid in the member's own currency.<sup>2</sup> Currencies held by the IMF are of two types, usable and unusable. A currency is usable if the issuing member's external payments position is strong enough for it to be called upon to finance IMF credit to other members. Other currencies, that is, the

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<sup>1</sup>Reserve assets are those that are readily available and accepted for international payments, such as the four currencies currently recognized as "freely usable" by the IMF: the U.S. dollar, euro, Japanese yen, and pound sterling. A freely usable currency is one that the IMF determines is widely used to make payments for international transactions and is traded in the principal exchange markets.

<sup>2</sup>Prior to the Second Amendment of the IMF Articles on April 1, 1978, the reserve asset portion was paid in gold, and after that, in SDRs or "usable" currencies of other members as determined by the IMF.

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currencies of borrowers or financially weak members, are considered unusable. Thus, a portion of the GRA's pool of resources consists of currencies that cannot be used, leaving the IMF's effective lending capacity at about half of total quotas.<sup>3</sup>

The IMF may also supplement its quota resources by borrowing and through additions to its precautionary balances. These balances comprise reserves in the GRA as well as resources that have been set aside in the first Special Contingent Account (SCA-1) to protect against the risk of overdue payments. These resources are not segregated from other resources of the GRA and can therefore finance the extension of credit.

With its usable resources, the IMF provides financing to its member countries. Members "borrow" from the GRA under the IMF's "credit tranche" policies or under special policies or facilities.<sup>4</sup> The credit tranches provide financing for balance of payments need, arising from almost any cause, whereas credits under other facilities deal with needs arising from specified causes. Financial assistance is typically made available in installments that are linked to the borrowing country's observance of specific economic and financial policy conditions that must be met before the next installment is released. These conditions are agreed with the member under agreements called "arrangements." Members using IMF resources pay a market-based rate of interest on their outstanding use of credit from the IMF.

A member's financial position in the IMF is measured by the GRA's holdings of its currency relative to quota. Members draw on the IMF's pool of members' currencies and SDRs through a purchase-repurchase mechanism (Box II.1). A member obtaining resources from the IMF "purchases" either SDRs or the currency of another member in exchange for an equivalent amount (in SDR terms) of its own currency, and later reverses the transaction

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<sup>3</sup>A member with usable currency pays in a usable currency whereas other members pay only the reserve asset portion in usable currency. Any member may pay the reserve asset portion in SDRs. Currencies are held by the IMF in depository accounts at members' central banks. Payment of the nonreserve asset portion of quota subscriptions is normally in the form of promissory notes (nonnegotiable, non-interest-bearing securities) that are converted into currency on demand.

<sup>4</sup>GRA credit is normally governed by the IMF's general lending policies (also known as "credit tranche" policies), as opposed to the special policies that apply to other types of credit. Both sets of policies are discussed in the section "Credit Outstanding." IMF credit has traditionally been provided in "tranches" (segments), equivalent to 25 percent of quota, as explained in the section "Credit Tranche Policies." "Borrowing" is undertaken through the purchase-repurchase mechanism, which is discussed in Box II.1.

### BOX II.1. THE IMF'S MAJOR FINANCING MECHANISM

The IMF's lending is financed from the capital subscribed by member countries. Each country is assigned a quota that determines its maximum financial commitment to the IMF. A portion of the quota is provided in the form of reserve assets (foreign currencies acceptable to the IMF or SDRs) and the remainder in its own currency. The IMF extends financing by providing reserve assets to the borrower from the reserve asset subscriptions of members or by calling on countries that are considered financially strong to exchange their currency subscriptions for reserve assets.

The loan is disbursed or drawn by the borrower "purchasing" the reserve assets from the IMF with its own currency.<sup>1</sup> Repayment of the loan is achieved by the borrower "repurchasing" its currency from the IMF with reserve assets. The IMF levies a basic rate of interest (charges) on loans based on the SDR interest rate and imposes surcharges depending on the amount and maturity of the loan and the level of credit outstanding.

A country that provides reserve assets to the IMF as part of its quota subscription or through the use of its currency receives a liquid claim on the IMF (a reserve, or reserve tranche, position) which can be encashed on demand to obtain reserve assets to meet a balance of payments financing need.

These claims earn interest (remuneration) based on the SDR interest rate and are considered by members as part of their international reserve assets. As IMF loans are repaid (repurchased) by the borrower with reserve assets, these funds are transferred to the creditor countries in exchange for their currencies and the creditor claim on the IMF is extinguished.

The purchase-repurchase approach to IMF lending affects the composition of the IMF's resources but not the overall size. An increase in loans outstanding will reduce the IMF's holdings of reserve assets and the currencies of members that are financially strong and increase the IMF's holdings of the currencies of countries that are borrowing from the IMF. The amount of the IMF's holdings of reserve assets and the currencies of financially strong countries determines the IMF's lending capacity (liquidity).

While the purchase-repurchase mechanism is not technically or legally a "loan," it is the functional equivalent of a loan. Similarly, IMF lending "arrangements" provide for drawings in installments upon the fulfillment of certain policy conditions. Thus, they are similar to conditional lines of credit. For ease of reference, these more commonly understood terms are often used in this pamphlet rather than the unique internal IMF terminology.

<sup>1</sup>In making a purchase, the member provides domestic currency to the IMF additional to currency previously paid to the IMF for the member's quota subscription.

by a “repurchase” of its currency held by the IMF with SDRs or the currency of another member.<sup>5</sup>

Members receive a liquid claim on the IMF (called a reserve, or reserve tranche, position) for the reserve assets they provide to the IMF. This claim earns a market-related rate of interest (called remuneration) and can be encashed on demand to obtain reserve assets from the IMF. Consequently, a member’s provision of reserve assets to the IMF changes the composition of the member’s reserve assets—from, for example, U.S. dollars to claims on the IMF—rather than the overall size of its international reserve assets. As the borrower repays the IMF loan (repurchases its currency with reserve assets), these funds are transferred to the creditor countries in exchange for their currencies, and the creditor’s claim on the IMF is extinguished.

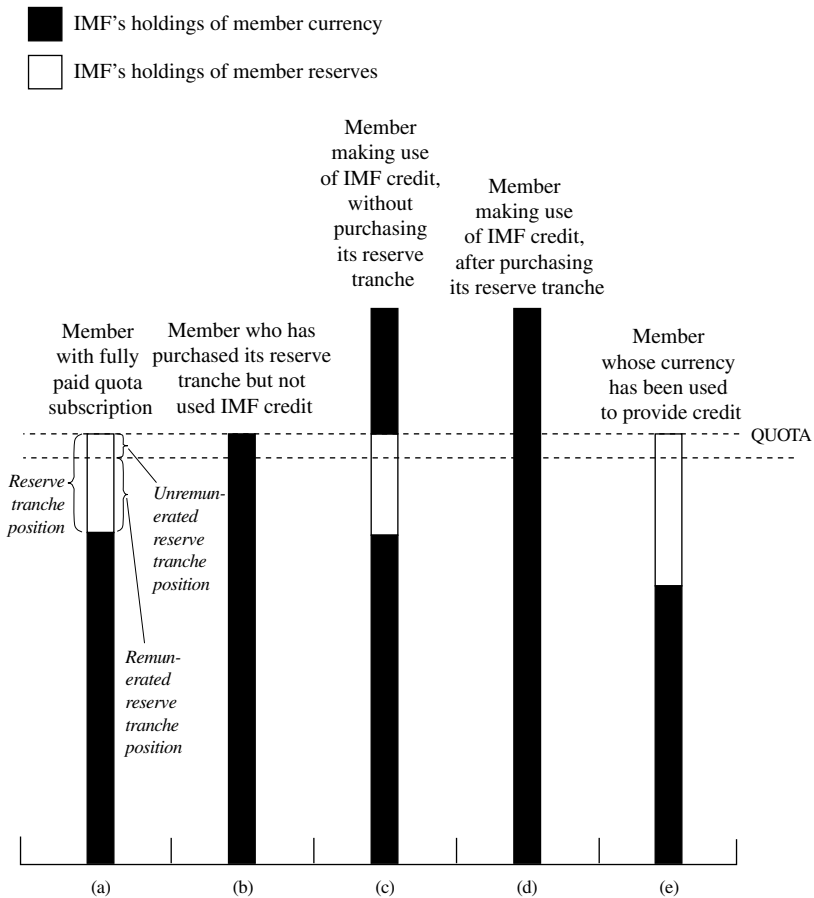
A member’s purchase of currency reduces the IMF’s holdings of the currency purchased, enlarges the reserve tranche position of the country whose currency is purchased, and increases the IMF’s holdings of the purchasing member’s currency. Charges (interest) are not levied on purchases within the reserve tranche, as these resources are the member’s own reserves. Interest is charged on the use of IMF credit, which is obtained through purchases outside of the reserve tranche. A member can choose whether or not to use its reserve tranche before utilizing IMF credit. Alternative financial positions of members in the IMF’s pool of resources in the GRA are illustrated in Figure II.1.

The currency purchased from the IMF must be that of a member with a strong external position, whose subscribed currency is considered usable for IMF transactions. If the currency purchased is not freely usable, the member whose currency is purchased is obliged to exchange purchased amounts of its currency for freely usable currencies. If the purchased currency is freely usable, the borrower can undertake transactions in the private exchange markets or with the issuer of the freely usable currency to acquire a different currency. A member whose currency is being used is obligated, if necessary, to provide an amount of reserve assets of up to 100 percent of its quota. The amount of reserve assets provided to the IMF has in practice fallen well short of this maximum. In planning and executing members’ transactions, members’ currencies are used in the financing of IMF credit according to their relative quota shares. In turn, members’ currencies are used in effect-

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<sup>5</sup>This financing mechanism has its roots in the credit facilities that existed between central banks before the IMF was established.

**FIGURE II.1. MEMBER FINANCIAL POSITIONS IN THE GRA**



**Situation (a):** A member has paid its quota subscription in full and not drawn on its reserve tranche. The remunerated reserve tranche position excludes certain holdings (holdings acquired as a result of a member's use of IMF credit and holdings in the IMF No. 2 Account that are less than 1/10 of 1 percent of quota; see "IMF Accounts in Member Countries"). See text for an explanation of the unremunerated portion of the reserve tranche.

**Situation (b):** The member has drawn its reserve tranche in full. The reserve tranche purchase is not subject to charges (interest).

**Situation (c):** The member is using IMF resources but has not drawn its reserve tranche. The level of holdings in excess of the member's quota is subject to charges.

**Situation (d):** The member is using IMF resources, in addition to having drawn its reserve tranche. The level of holdings in excess of the member's quota is subject to charges.

**Situation (e):** The IMF has made use of the member's currency and pays the member remuneration on its enlarged reserve tranche position.

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ing receipts to the IMF in a manner that adjusts reserve tranche positions toward a uniform proportion of their quotas.<sup>6</sup>

The purchase-repurchase mechanism explains why, from an accounting perspective, the IMF's total resources do not vary as a result of the IMF's financial assistance—only the composition of its assets change. Moreover, the value of members' currencies held in the GRA's pool of resources is maintained in SDR terms over time through periodic additions to the amounts of currencies that are depreciating against the SDR and reductions from those that are appreciating against the SDR. This maintenance of value provision is an obligation of members under the Articles.<sup>7</sup>

### **Special Disbursement Account**

The Special Disbursement Account (SDA) is the vehicle for receiving and investing profits from the sale of the IMF's gold (i.e., the net proceeds in excess of the book value of SDR 35 a fine ounce), and for making transfers to other accounts for special purposes authorized in the Articles, in particular for financial assistance to low-income members of the IMF.

### **Investment Account**

The IMF is authorized to establish an Investment Account in the General Department; to date, however, no decision has been taken to this effect. Investments of amounts up to the level of accumulated reserves may be made only in income-generating marketable obligations of international financial organizations or of the member whose currency is used for the investment.<sup>8</sup> The income may be reinvested or used to meet the expenses of conducting the business of the IMF, including both operational and administrative expenses.

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<sup>6</sup>For an analysis of the key elements underlying the GRA's costs and revenues and past proposals for simplification or modification, see "Financing the Fund's Operations—Review of Issues," March 2000, on the IMF's website (<http://www.imf.org/external/np/tre/ffo/2001/fin.htm>).

<sup>7</sup>Article V, Section 11(a).

<sup>8</sup>The resources in the GRA are managed in such a way as to lower the IMF's costs or to increase the IMF's revenue. In order to be more profitable than GRA resources, resources in an Investment Account would need to be invested at a rate that exceeds the SDR interest rate after taking into account any exchange risk.

## The Balance Sheet

The relationships among the sources and uses of resources in the General Department, and their relative magnitudes, are summarized in its balance sheet (Table II.1).

On the asset side, the first major item is credit outstanding at the end of FY2001 of SDR 42.2 billion, which is the value of financing extended by the IMF to its members. Financing to debtor members is largely funded by the use of the currencies of creditor members and is reflected in the resulting reserve tranche positions of creditor members (see Box II.1). Members with outstanding credit pay a market-related rate of interest on these loans which fully covers the payment of interest to the creditors providing the resources to the IMF, as further explained below. The vast bulk of other assets held by the IMF in the GRA was usable and other currencies, equal to SDR 165.7 billion. Gold, valued at SDR 5.9 billion, represented a relatively small share of total assets.<sup>9</sup> The IMF receives no interest on its gold or currency holdings that do not result from the extension of IMF credit. The only interest-bearing asset held by the IMF other than its outstanding credit is its holdings of SDRs, which were SDR 2.4 billion. With the addition of some minor receivables and other assets, total assets of the GRA at end-April 2001 amounted to SDR 217.5 billion.

On the resources and liabilities side, total quota resources were SDR 212.4 billion on April 30, 2001. As noted above, some of these subscription resources were usable and some were not. Usable currencies amounted to SDR 109.7 billion and unusable currencies SDR 56.0 billion. In addition, there were SDR 46.7 billion in reserve tranche positions of members. The reserve tranche positions of IMF members result from initial quota payments and the increase due to the extension of IMF credit to other members. These reserve positions earn a market-related rate of return, as explained below. Precautionary balances, which include reserves and the balance in the Special Contingent Account (SCA), amounted to an additional SDR 4.5 billion. Adding a small amount of interest (remuneration) payable and some other minor liabilities gives a total of SDR 217.5 billion of GRA resources and liabilities.

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<sup>9</sup>The IMF's holdings of gold are valued at historical cost. For most of the gold holdings, this is SDR 35 a fine ounce. Market prices for gold are much higher, which imparts a fundamental strength to the IMF's financial position. See the discussion below in the section on "Gold Holdings."

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TABLE II.1. BALANCE SHEET OF THE GENERAL DEPARTMENT,  
AS OF APRIL 30, 2001  
(In billions of SDRs)

Assets		Resources and Liabilities	
<i>General Resources Account:</i>		<i>General Resources Account:</i>	
		Members' resources:	
		Quota subscriptions, represented by:	
Credit outstanding	42.2	Reserve tranche positions	46.7
Usable currencies	109.7	Usable currencies	109.7
Other currencies	<u>56.0</u>	Other currencies	<u>56.0</u>
Total currencies	207.9	Total quotas	212.4
		Precautionary balances:	
		Reserves of the GRA	3.3
		SCA-1	<u>1.2</u>
			4.5
SDR holdings	2.4	Liabilities:	
Gold holdings	5.9	Remuneration payable	0.4
Receivables	0.6	Other liabilities	<u>0.2</u>
Other assets	0.7	Total liabilities	0.6
Total GRA	217.5	Total GRA	217.5
<i>Special Disbursement Account:</i>		<i>Special Disbursement Account:</i>	
Investments of the SDA	2.4	Accumulated resources of the SDA	2.8
SAF loans	<u>0.4</u>		
Total SDA	2.8		
Total assets	220.3	Total resources and liabilities	220.3

Note: Numbers may not add to totals due to rounding.

At end-April 2001, the IMF did not have any outstanding borrowing, but if it had, the amount of borrowing outstanding would have been shown on the liabilities side, with additional offsetting credit extended by the IMF to its members on the asset side. A comparison of the relative size of these resources and liabilities demonstrates that the IMF is overwhelmingly a quota-based institution.



The rest of the General Department consists solely of the relatively small amount of assets and liabilities of the SDA, SDR 2.8 billion at end-April 2001. These represent the accumulated resources of the account, which reflect the profits and investment returns realized on past gold sales on the resources side, and the investment of these resources on the asset side. The income from these investments is transferred to the PRGF and PRGF-HIPC Trusts to provide concessional financial assistance to low-income members. There was also a small amount (SDR 0.4 billion) of loans still outstanding from the Structural Adjustment Facility (SAF) at end-April 2001.<sup>10</sup> These loans were financed with SDA resources.

The remainder of this chapter expands upon the above discussion. It first discusses each item on the asset side of the GRA — namely, credit outstanding, which includes a description of the various terms and conditions of IMF lending, followed by relatively short sections on currency, SDR, and gold holdings. It then describes each item on the resources and liabilities side of the GRA — namely, quotas, including reserve tranche positions, and precautionary balances. Next, the chapter explains how the supply of and demand for GRA resources is managed through the quarterly financial transactions plan, and how the IMF monitors its overall level of liquidity in the GRA. Finally, it shows how IMF transactions are reflected in the accounts and balance sheets of member countries.

The management and investment strategy for the resources in the SDA is covered in Chapter IV.

## **The Asset Side**

### **Credit Outstanding**

Credit outstanding, as the caption suggests, represents loans already provided to members under the various IMF facilities. This section first describes the general terms and conditions of IMF lending, followed by a discussion of the IMF's financial policies and lending facilities.

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<sup>10</sup>The SAF is discussed in Chapter IV.

## *General Terms and Conditions*

### *Balance of Payments Need*

Members using IMF resources must have a balance of payments need. A borrowing member cannot use IMF resources in the absence of a representation of balance of payments need, and the extent of their use cannot exceed that need. Borrowing usually takes place under an IMF arrangement, which is similar to a conditional line of credit and is associated with the implementation of an economic reform program in a member country. The most common type of arrangement is a Stand-By Arrangement in the credit tranches or an arrangement under the Extended Fund Facility (EFF).<sup>11</sup> Such arrangements can be approved on the basis of a prospective balance of payments need, although the existence of a balance of payments need does not, in itself, entitle a member to draw on the IMF.

The concept of balance of payments need has evolved over time. The concept includes three distinct elements: the balance of payments position of the member, its foreign reserve position, and developments in its reserve position.<sup>12</sup> These three elements are regarded as separate, and a representation of need can be based on any one of them. An operational framework has been developed over the years to serve as the basis for judgments on the magnitude of balance of payments deficits and the adequacy of foreign reserves. In the implementation of this framework, the circumstances of members are taken into account.

Once an arrangement has been approved by the IMF, a member's representation of balance of payments need to make a purchase is not subject to challenge, under a long-standing policy intended to assure the member of the availability of IMF resources committed to it, subject only to its meeting conditions specified in the arrangement. However, the IMF may take remedial action after a purchase under an arrangement or a reserve tranche purchase if it finds that the conditions for the purchase were not met, including that of balance of payments need.

Other conditions may also be required. The IMF's policies under particular facilities may also stipulate requirements concerning the origins and nature of the underlying balance of payments disequilibrium. For instance,

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<sup>11</sup>See discussion below under "Financial Policies and Facilities."

<sup>12</sup>Article V, Section 3(b)(ii).

the use of the Compensatory Financing Facility (CFF) is restricted to temporary balance of payments deficits arising from overall export shortfalls or increased costs of specified cereal imports.

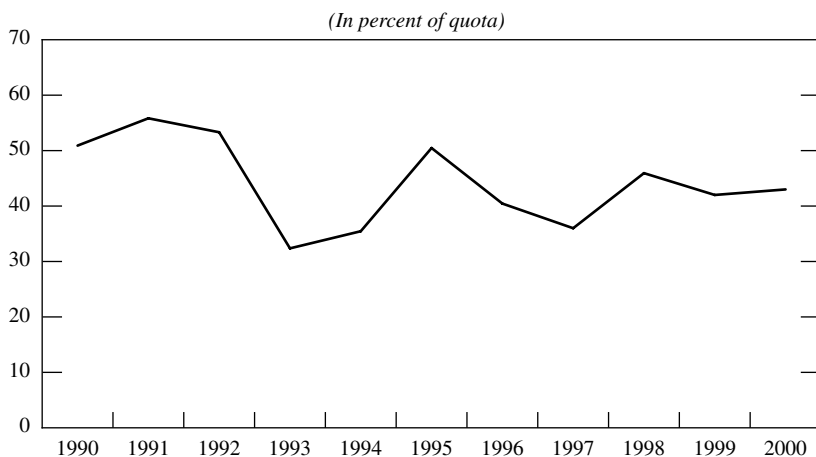
### *Access Policy*

The policy of the IMF is to encourage members to approach it for assistance at an early stage of their balance of payments difficulties. Members experiencing balance of payments problems can approach the IMF, but are under no obligation to do so at any time. Over the years, it has come to be recognized that the efficacy of the mixture of adjustment policies and financing depends largely on the early adoption of corrective policy measures. Early resort to an adjustment program supported by IMF resources can help to avoid more drastic policy actions that may otherwise be required, thereby limiting the impact of the adjustment on other members.

Quantitative limits on access are used to ensure equal treatment of members. Access limits are set in terms of quota, the basic measure of members' financial rights and obligations in the IMF. For the credit tranches and the EFF, which account for the lion's share of IMF lending, the current limits take the form of an annual limit of 100 percent of quota on purchases over any 12-month period and a cumulative limit of 300 percent of quota on the level of IMF credit outstanding. Average annual access under these lending arrangements in recent years has been 40–50 percent of quota (Figure II.2). Other IMF facilities are subject to separate access limits or, in some cases, no explicit limits (Box II.2). In exceptional circumstances, these limits can be waived, as they were for members most immediately affected by the severe financial crises of the late 1990s.

The level of access to GRA resources under Stand-By Arrangements and the EFF—that is, the amount that can be borrowed—is based on criteria that are applied uniformly to all members. These criteria seek to balance the needs of members against the overarching responsibility of the institution to safeguard and ensure the temporary use of its resources. The criteria are:

- actual or potential need for resources from the IMF, taking into account other sources of financing and the desirability of maintaining a reasonable level of reserves;
- ability to service indebtedness to the IMF, thereby protecting the revolving character of IMF resources;
- amount of the outstanding use of IMF credit and record in using IMF resources in the past.

**FIGURE II.2. AVERAGE ANNUAL ACCESS UNDER STAND-BY AND EXTENDED ARRANGEMENTS<sup>1</sup>**

<sup>1</sup>Excluding the cases with exceptional access (i.e., exceeding the access limits). Excluded arrangements are Mexico's 1995 Stand-By Arrangement; Indonesia's, Korea's and Thailand's 1997 Stand-By Arrangements; Brazil's 1998 Stand-By Arrangement; Indonesia's 1998 Extended Arrangement; Turkey's 1999 Stand-By Arrangement; and Indonesia's 2000 Extended Arrangement.

### *Phasing of Purchases*

An important feature of IMF lending is the phasing of disbursements. All arrangements above 25 percent of quota in the credit tranches—the upper credit tranches—and under the EFF are subject to conditionality and the phasing of purchases (see Chapter V). Purchases in the first credit tranche (up to 25 percent of quota) are not phased, but do incorporate some policy conditionality.

Phasing refers to the practice of making IMF resources available in installments over the period of an arrangement, typically quarterly, subject to the observance of performance criteria, the completion of a program review, or both.<sup>13</sup> This is intended to ensure that IMF financing goes hand in hand with

<sup>13</sup>An “arrangement” is an assurance by the IMF that it stands ready to provide foreign exchange or SDRs under certain conditions during a specified period of time. The arrangement is in support of a detailed economic “adjustment program” of the member. See the Glossary for definitions of these terms.

## BOX II.2. THE FRAMEWORK FOR ACCESS TO IMF RESOURCES

### Quota-based access limits

- The *credit tranches* (mainly accessed through Stand-By Arrangements) and the *Extended Fund Facility* (EFF) are subject to the same access limits. These consist of an annual limit of 100 percent of quota and a cumulative limit of 300 percent of quota. The annual limit applies to gross purchases in any 12-month period. The cumulative limit applies to credit outstanding, less scheduled repurchases, plus scheduled purchases, over the period of commitment of resources. These limits may be exceeded in exceptional circumstances. Average annual access has been fairly stable at around half of the annual limit in recent years (see Figure II.2).

- Access under the *Compensatory Financing Facility* (CFF) is subject to its own limits. These limits are cumulative, and include limits of 45 percent of quota each for access under the export shortfalls and excess cereal imports elements, and a combined limit of 55 percent of quota. These limits cannot be exceeded.

- The amount of *emergency assistance* for natural disasters and for post-conflict cases is limited, in any one instance, to 25 percent of quota. Larger amounts can be made available on an exceptional basis in post-conflict cases. Emergency assistance was until recently subject to the access limits under the credit tranches but was converted into a facility and excluded from these access limits, pending further review.

### Access to other facilities

- The *Supplemental Reserve Facility* (SRF) is not subject to explicit access limits. SRF resources are provided under Stand-By or Extended Arrangements in addition to credit tranche or EFF resources, which are subject to annual and cumulative limits. The IMF uses the same criteria for access to its resources under all policies and facilities (see section on “General Terms and Conditions”) but in the case of the SRF also takes into account the liquidity position of the IMF, given the magnitude of the balance of payments need in cases qualifying for this facility.

- The *Contingent Credit Lines* (CCLs) are not subject to access limits but commitments under the CCL are expected to be in the range of 300–500 percent of quota. CCL resources are provided under Stand-By Arrangements, in combination with credit tranche resources up to the annual or the cumulative limit. As with the SRF, the liquidity position of the IMF is taken into account when determining access under the CCL.

policy measures that are considered necessary to resolve underlying balance of payments problems and enable members to repay the IMF within the established repurchase period. Phasing also enables the purchasing member to demonstrate to other members that its adjustment program is being implemented and warrants their continued support.

The choice between even phasing and uneven phasing depends on the balance of payments need and the path of adjustment. These choices are made on a case-by-case basis: resources are normally fairly evenly spread over the arrangement period but a concentration of adjustment at the beginning of an arrangement could justify front-loading of purchases. The frequency of purchases may also be affected by the length of lags in the reporting of data relating to performance criteria.<sup>14</sup>

### *Repurchase Policies*

The repurchase policies of the IMF are intended to ensure the revolving character of its resources. All purchases made from the IMF are subject to predetermined repurchase schedules (Table II.2). The length of the repurchase period and the number of repurchase installments differ according to the policy or facility under which the credit was extended.

In the case of most purchases, a borrower is expected to repurchase earlier than the schedule of repurchase obligations. Such time-based repurchase expectations are aimed at securing early repayment from members in a position to do so, in keeping with a long-standing principle of the IMF that its resources should be used only as long as there is a balance of payments need (Box II.3). A waiver of early repurchase expectations can be provided by the Executive Board upon the request of a member, if the member's external position is not strong enough for the member to pay early without undue hardship or risk. In case of a waiver, repurchases would fall due according to the original obligation schedule.

Time-based repurchase expectations apply to purchases made after November 28, 2000 in the credit tranches and under the CFF and EFF. For purchases in the credit tranches and under the CFF, the expectation schedule is 1 year in advance of the obligation schedule, beginning 2¼ years after each purchase and ending after 4 years. For the EFF, the expectation schedule

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<sup>14</sup>Specific guidelines on phasing are set out in *Selected Decisions and Selected Documents of the International Monetary Fund* (Washington). This volume is updated annually on June 30. See, for example, the Twenty-Fifth Issue, June 30, 2000.

Table II.2. Financial Terms of IMF Credit

Instrument	Charges				Repurchases		
	Base	Surcharge	Service	Commitment	Expectation	Obligation	Installments
First credit tranche	Basic rate	None	50 basis points	None	2¼-4 years	3¼-5 years	8 quarterly
Stand-By Arrangement	Basic rate	100 basis points for credit over 200 percent of quota; 200 basis points for credit over 300 percent of quota	50 basis points	25 basis points plus 10 basis points for amounts in excess of 100% of quota	2¼-4 years	3¼-5 years	8 quarterly
Extended Fund Facility (EFF)	Basic rate		50 basis points		4½-7 years		6 semiannual
Supplemental Reserve Facility (SRF)	Basic rate	300-500 basis points	50 basis points	25 basis points plus 10 basis points for amounts in excess of 100% of quota	1-1½ years	4½-10 years	12 semiannual
		Initial surcharge rises by 50 basis points after one year and each subsequent six months			2-2½ years	2 semiannual	
Contingent Credit Line (CCL)	Basic rate	150-350 basis points	50 basis points		1-1½ years	2-2½ years	2 semiannual
Compensatory Financing Facility (CFF)	Basic rate	None	50 basis points	None	2¼-4 years	3¼-5 years	8 quarterly
Emergency assistance	Basic rate	None	50 basis points	None	None	3¼-5 years	8 quarterly

The *basic rate of charge* is linked directly to the SDR interest rate by a coefficient that is fixed each financial year. The basic rate of charge therefore fluctuates with the market rate for the SDR, which is calculated on a weekly basis. The basic rate of charge is adjusted upward for burden sharing to compensate for the overdue charges of other members (see Box II.9). The *Surcharge* on high levels of credit outstanding under the credit tranches and the EFF is designed to discourage large use of IMF resources. The *SRF and CCL surcharges* increase with the time elapsed since the first SRF or CCL purchase, which sharpens the incentive for repurchases ahead of the obligation schedule. The annual *commitment fee* applies to amounts available under an arrangement during the year. The fee is refunded to the extent that available amounts are purchased.

*Repurchases* are made in equal installments at regular intervals over a fixed period. A member is free to repurchase in advance of maturity and to attribute repurchases to any outstanding obligation to the IMF. The repurchase obligation schedule for each type of credit is generally associated with an accelerated schedule, which members are expected to follow. A member not in a position to meet the expectations schedule can request an extension up to the corresponding period in the obligation schedule.

**BOX II.3. EVOLUTION OF IMF POLICIES ON REPURCHASES**

Under the original Articles of Agreement, there were no fixed repurchase periods for the use of IMF resources: repurchases were calculated annually for each member according to a formula based on their international reserves. This reflected the principle that the IMF's resources are made available only to members with a balance of payments and reserve need, and was designed to ensure their revolving character.

This approach became unworkable over time, however, and was increasingly supplemented by policies on repurchase periods. The coexistence of these two approaches—one based on explicit schedules and another on reserve strength—was codified under the Second Amendment of the Articles in 1978 with the establishment of fixed repurchase periods (Article V, Section 7(c)) and provision for early repurchase by members as their balance of payments and reserve position improves (Article V, Section 7(b)).

A major change in the repurchase policies was introduced in 1997 with the establishment of the SRF to help members experiencing exceptional balance of payments difficulties owing to a large short-term financing need resulting from a sudden and disruptive loss of market confidence. In line with the short-term nature of this type of balance of payments need, the SRF incorporates much shorter repurchase periods and features repurchase expectations that are legally outside of the framework of Article V, Section 7(b). Repurchases under the SRF are expected to be made in two installments after 1 and 1½ years from the date of the purchase. In order to provide flexibility for cases where the member's return to capital markets takes longer than anticipated, each repurchase can be extended by up to 1 year, upon request by the member and approval of the request by the Executive Board. The same repurchase profile was adopted for the CCL in 1999.

Repurchase expectations were introduced for purchases in the credit tranches and under the EFF and the CFF in November 2000. These time-based repurchase expectations (see Table II.2) can be extended upon request by the member, in which case repurchases would fall due according to the original obligation schedule. Waivers are considered by the Executive Board if the member's external position is not strong enough for the member to pay early without undue hardship or risk. Adjustment programs supported by credit tranche or EFF resources are generally designed on the basis of the obligation schedule for repurchases, so that in most cases members will be in a position to meet repurchase expectations only if their external position is stronger than projected at the outset of the program. In contrast, adjustment programs supported by SRF and CCL resources are designed on the basis of the expectation schedule from repurchases.



begins after 4½ years, as with the obligation schedule, but repurchases are doubled, so that the expectation schedule ends after 7 years rather than 10 years under the obligation schedule. Figure II.3 illustrates the mapping of repurchase expectations and the corresponding repurchase obligations.

A member can request an extension of time-based repurchase expectations if its external position is not sufficiently strong. If the IMF agrees to an extension, all repurchase expectations during the period covered by the extension would revert back to the corresponding repurchase obligations. There is a presumption that this period would be one year, although a longer or shorter period could be set. If the IMF does not agree to an extension, the member would be expected to make repurchases according to the expectation schedule. Failure to do so would result in a suspension of the right to make further purchases, including prospective purchases under an existing arrangement. However, the member would not be in arrears until it failed to meet a repurchase obligation.

IMF-supported programs are guided by the requirement that the member should be able to meet repurchase obligations. In most cases, therefore, members will be considered to be in a position to meet repurchase expectations only if their external position is stronger than had been projected at the time of approval of the associated IMF arrangement. Similarly, the evaluation of members' capacity to repay the IMF is based on the obligation schedule.

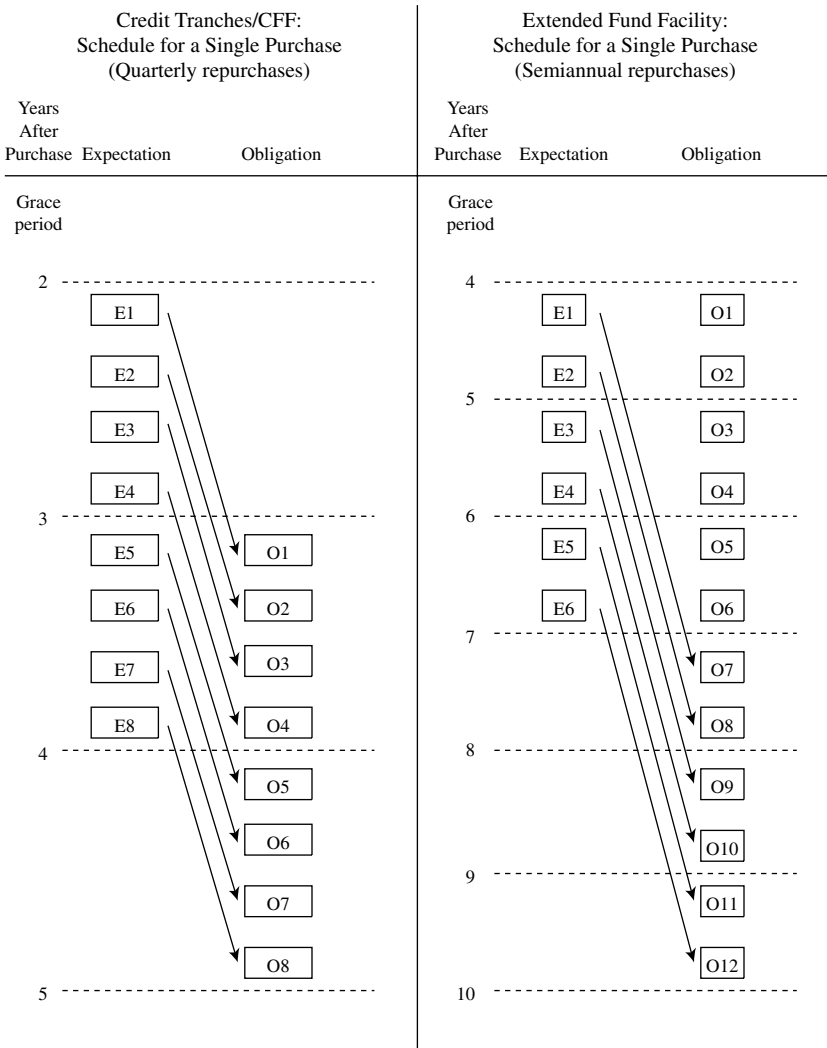
An early repurchase policy serves as a backstop to the standard repurchase provisions. Members with IMF credit outstanding are normally expected to make repurchases as their balance of payments and reserve position improves.<sup>15</sup> A member could experience an especially rapid and strong turnaround in its balance of payments and reserve position, and may be in a position to make repurchases earlier than under the fixed schedules for time-based repurchase expectations. In addition, there are some purchases for which time-based repurchase expectations are not applicable.<sup>16</sup> Judgments on the appropriateness of early repurchases in individual cases are made by the Executive Board. The amount of such repurchases expected during a given quarter is determined on the basis of a formula that relies heavily on gross reserves (Box II.4).

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<sup>15</sup>Article V, Section 7(b).

<sup>16</sup>Time-based repurchase expectations do not apply to purchases made prior to November 2000 or to purchases under emergency assistance; separate repurchase expectations apply to purchases under the CCL and SRF.

FIGURE II.3. EARLY REPURCHASE EXPECTATIONS



A member meeting the expectations schedule would meet expectations E1 through E8, which would extinguish obligations O1 through O8.

A member meeting the expectations schedule must repurchase obligations O1 through O6, and would meet the contemporaneous expectations E1 through E6, extinguishing obligations O7 through O12.

**BOX II.4. EARLY REPURCHASE POLICY: MINIMUM  
REPURCHASE AMOUNTS****Formula**

Under the guidelines for early repurchase, the minimum amount that a member is expected to repurchase each quarter is determined by a formula based on the member's gross international reserves:

- 1.5 percent of latest reserves plus (minus)
- 5.0 percent of the increase (decrease) in reserves over the previous six months.

For this purpose, the IMF uses the latest data on the member's gross reserves as reported in the IMF's *International Financial Statistics*, with gold valued at SDR 35 an ounce, available when the associated financial transactions plan is prepared for Executive Board consideration. The formula thus ensures a tight link between reserves and repayments to the IMF, with any increase in reserves resulting in larger repurchases and vice versa. The formula is applied anew for every quarter the member is included in the transactions plan for early repurchases.

**Limits**

The minimum repurchase amount is subject to quantitative limits. This amount cannot

- exceed 4 percent of latest reserves in a quarter,
- exceed 10 percent of latest reserves in a year, or
- reduce latest reserves below 250 percent of quota.

These limits are a means to protect members from having to draw too heavily on their owned reserves to meet IMF repayments. In the two decades since the policy was established, early repurchase amounts generated by the formula have always fallen below these limits.

**Credits**

In addition to these limits, the minimum repurchase amount is reduced to the extent of any repurchase obligations falling due during the quarter or to give credit for voluntary advance repurchases:

- in the two quarters prior to the member being included for early repurchase, or
- subsequent repurchases in excess of minimum repurchase amounts.

The credits are intended to encourage members to accelerate repurchases voluntarily on their own terms.

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Early repurchase expectations can arise in other contexts. Provisions for early repurchase are built into the CFF, Contingent Credit Line (CCL), and Supplemental Reserve Facility (SRF). In addition, a member is required to take corrective action by making an early repurchase in the event that it makes a purchase under an arrangement that it was not entitled to make by the terms of the arrangement—that is, a noncomplying purchase. The requirement of corrective action can be waived if the IMF decides that the circumstances justify continued use of the purchased resources. A noncomplying purchase would arise if a member were permitted to make a purchase because, on the basis of information available at the time, the IMF was satisfied that the conditions applicable to the purchase under the arrangement had been observed but, on the basis of information subsequently available, it became evident that the conditions of the arrangement had not actually been met.<sup>17</sup>

The IMF can change the period of repurchases.<sup>18</sup> It has the authority to postpone the date for the discharge of a repurchase by a majority of the votes cast, provided that the postponement does not cause the repurchase to exceed the maximum repurchase period. Postponement beyond the maximum period allowed under the arrangement would be considered only in the event that the IMF determined that discharge on the due date would result in exceptional hardship for the member and if the longer period for repurchase is consistent with the revolving nature of the use of IMF resources. Such a decision requires approval by a 70 percent majority of the total voting power.<sup>19</sup>

A member is free to make advance repurchases at any time. At the discretion of the member, advance repurchases can be attributed to any outstanding purchases. In this way, a member is free to reduce the IMF's holdings of its currency corresponding to prior purchases and thereby reduce or eliminate its obligation to pay interest to the IMF. Repurchases can be made, at the choice of the repurchasing member, in SDRs or in currencies selected by the IMF according to the policies and procedures for the use and receipt of

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<sup>17</sup>See also the discussion in Chapter V on “Measures to Deal with Misreporting.”

<sup>18</sup>An 85 percent majority of the total voting power in the IMF is required to change the period of repurchase of holdings of currency acquired by the IMF pursuant to its policy on the use of general resources. A 70 percent majority is required in the case of holdings of currency not acquired as a result of purchases and subject to charges under Article V, Section 8(b)(ii). See Appendix II.

<sup>19</sup>No such decision has been taken in the past 25 years.

currencies under the quarterly financial transactions plan, as discussed below under “Financial Transactions Plan.”<sup>20</sup>

### **Financial Policies and Facilities**

The lending instruments of the IMF have evolved over the years. In its early years, IMF lending took place exclusively on the basis of general policies on access in what became known as the credit tranches and, in particular, under Stand-By Arrangements. Beginning in the 1960s, special policies were developed to deal with various balance of payments problems having particular causes, resulting over time in a multiplicity of policies on the use of IMF resources.<sup>21</sup> Special policies on the use of IMF resources outside the credit tranches are generally referred to as facilities.

All decisions on the extension of IMF credit are taken by the Executive Board. These decisions are supported by a formal request from the member and an assessment by the staff of the nature and magnitude of the balance of payments problem, the adequacy of the policy response, and the capacity of the member to repay the IMF. In 1995, the IMF specified streamlined procedures under an Emergency Financing Mechanism to allow for quicker Executive Board approval of IMF financial support. This mechanism is used in circumstances representing, or threatening, a crisis in a member’s external accounts that requires an immediate response from the IMF, as was the case in 1997 for Indonesia, Korea, the Philippines, and Thailand and in July 1998 for Russia.

A fundamental review of IMF financial policies and facilities took place in 2000, which resulted in a more streamlined structure, with a sharper focus on crisis prevention and ensuring effective use of IMF resources. This section describes the current structure of policies and facilities; earlier lending instruments are noted in Box II.5.

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<sup>20</sup>Members have the option of combining all repurchases due within a calendar month, provided that the combined repurchase is completed not later than the last day of the month and that no single repurchase remains outstanding for a period exceeding the maximum permitted under the relevant policy of the IMF.

<sup>21</sup>A comprehensive discussion of the evolution of IMF lending instruments is available on the web: “Review of Facilities—Preliminary Considerations,” [www.imf.org/external/np/pdr/fac/2000/index.htm](http://www.imf.org/external/np/pdr/fac/2000/index.htm).

**BOX II.5. EARLIER IMF LENDING INSTRUMENTS**

Over the years, the IMF has established a number of policies and facilities to meet particular balance of payments needs that were eventually either eliminated or allowed to lapse:

- The *Buffer Stock Financing Facility*, created in 1969 and eliminated in 2000, provided financing to members to help finance their contributions to approved commodity price stabilization funds.
- The first *Oil Facility* was created in June 1974 in response to the oil price shock, and lapsed in December 1974. A second *Oil Facility* was created in April 1975 to provide additional financing, and lapsed in March 1976.
- A policy of support for *debt and debt-service operations*, initiated in 1989, was a key element of the IMF's response to the debt crisis. The policy proved useful in facilitating commercial bank debt reduction but, by the late 1990s, had outlived its usefulness and was discontinued in 2000.
- An *oil import element* was added to the Compensatory Financing Facility (CFF) in November 1990, when oil prices rose sharply during the Middle East conflict. It was allowed to lapse at end-1991.
- The *Systemic Transformation Facility*, created in April 1993 and allowed to lapse in April 1995, provided support for the early stages of transition from centrally planned to market economies, in relatively small amounts and with relatively low conditionality.
- The policy on *currency stabilization funds* was established in 1995 as a means of providing additional, precautionary support under IMF arrangements during the early stage of an exchange rate-based stabilization program. No member made use of the policy, and it was discontinued in 2000.
- A *contingency element* was added to the CFF in 1988. Until its elimination in 2000, this instrument provided additional access under arrangements, according to prespecified calculations, in the event of unanticipated adverse current account developments.
- The *Y2K Facility* was created in September 1999 to deal with possible strains resulting from the Millennium (Y2K) computer dating problem. It was not used, and lapsed in March 2000.

***Credit Tranche Policies***

From its early history, IMF credit was made available in tranches (segments). Members could make purchases in four credit tranches, each equivalent to 25 percent of quota, within the prevailing annual access limit of 25 percent of quota and the cumulative access limit of 100 percent of quota. A

purchase in the first credit tranche raises the use of IMF credit to no more than 25 percent of quota. The three subsequent tranches are known as the upper credit tranches. Over time, access to IMF credit substantially above 100 percent of quota under the credit tranches has been permitted; accordingly, the upper credit tranches now refer more generally to any use of IMF credit beyond the first credit tranche. Resources drawn in the credit tranches can be used to meet any balance of payments need.

The segmentation in terms of first and upper credit tranches underscores the basic principle that the IMF requires stronger justification in terms of policy understandings from the member at higher levels of IMF credit outstanding. Conditionality is the mechanism that gives the IMF the needed assurances. The IMF adopts a more liberal attitude in making resources available in the first credit tranche than in the upper credit tranches, provided that the member is making reasonable efforts to solve its balance of payments problems. Requests for use of IMF resources beyond the first credit tranche require substantial justification for the expectation that the member's balance of payments difficulties will be resolved within a reasonable period of time.

Access to the upper credit tranches is normally made under Stand-By Arrangements. These are lines of credit from the IMF under which a "member is assured that it will be able to make purchases from the General Resources Account in accordance with the terms of the decision during a specified period and up to a specified amount."<sup>22</sup> Stand-By Arrangements have long been the core lending instrument of the institution. They were initially intended as precautionary instruments, to be drawn on only if payments difficulties emerged, but have been used more commonly as a source of external financing. Stand-By Arrangements that are treated by members as precautionary, either at the outset of the arrangement or after immediate financing constraints have eased, have again emerged following the opening of world capital markets.

Stand-By Arrangements typically cover a period of 1–1½ years but can be longer, up to a maximum of 3 years. Performance criteria, the phasing of purchases, and program reviews apply to the use of IMF resources in the upper credit tranches, but not in the first credit tranche, even under a Stand-By Arrangement.<sup>23</sup> Repurchases are expected each quarter 2¼–4 years after

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<sup>22</sup>Article XXX(b).

<sup>23</sup>Outright purchases without IMF arrangements can take place, but are rare.

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each purchase, but these expectations can be extended to a maximum repurchase period of 3¼–5 years. In addition to the charges for the use of IMF credit, members pay a commitment fee for Stand-By Arrangements, which is refunded to the extent that amounts under the arrangement are purchased (Table II.2 summarizes the terms of IMF credit under the various policies and facilities).

### *Extended Fund Facility*

The Extended Fund Facility (EFF) was established in 1974 as a vehicle for longer-term external financing for members undertaking needed structural economic reforms. The EFF is designed for economies:

- suffering serious payments imbalances relating to structural maladjustments in production and trade and where price and cost distortions have been widespread, or
- characterized by slow growth and an inherently weak balance of payments position, which prevent pursuit of an active development policy.

The EFF is especially appropriate for members graduating from the Poverty Reduction and Growth Facility (PRGF) programs or transition economies that lack adequate capital market access. At the same time, the EFF and all other IMF facilities are available in principle to any member that meets the eligibility criteria.

Members drawing under the EFF do so in the context of an Extended Arrangement. These are three-year IMF arrangements, which can be extended for a fourth year. Performance criteria and purchases typically follow a semiannual schedule. Repurchases are also made semiannually, and over a longer period than applies to the credit tranches: repurchases are expected 4½–7 years after each purchase but this can be extended to the maximum repurchase period of 4½–10 years. Members pay a refundable commitment fee for Extended Arrangements, as well as the applicable charges for the use of IMF credit.

### *Supplemental Reserve Facility*

The Supplemental Reserve Facility (SRF) was established at the end of 1997, at the height of the Asian financial crisis. Its purpose is to provide financial assistance to members experiencing exceptional balance of payments difficulties due to a large, short-term financing need following a sudden and disruptive loss of confidence reflected in pressure on the capital account and the member's foreign reserves. Access under the SRF is separate



from the limits that apply to the credit tranches and the EFF, and it has no explicit limits of its own. SRF resources are provided under Stand-By or Extended Arrangements. The conditionality in an arrangement involving SRF resources is that of the associated Stand-By or Extended Arrangement.

The repurchase period for SRF resources is much shorter than that governing the credit tranches and EFF, reflecting the likelihood of a quicker turnaround in the balance of payments. Repurchases are made in two installments and are expected 1–1½ years after each purchase; this period can be extended up to the maximum repurchase period of 2–2½ years. Resources drawn under the SRF are subject to the basic rate of charge applying to all IMF credit and a specific surcharge. During the first year from the date of the first purchase under the facility, the SRF surcharge is set at 300 basis points, and it rises by 50 basis points at the end of the first year and every six months thereafter, up to a maximum of 500 basis points. The standard commitment fee for Stand-By Arrangements applies.

### ***Contingent Credit Lines***

The Contingent Credit Line (CCL) is a new type of lending instrument for the IMF. Conceived in the midst of a series of severe financial crises involving large-scale use of IMF resources by a number of members, the CCL was established by the IMF in 1999 as a means of preventing the spread of capital account-driven crises. The CCL is intended to provide members maintaining strong policies with a precautionary line of defense against balance of payments problems arising from international financial contagion. Although it draws on IMF experience over several decades, the CCL has a number of novel features that set it apart from other IMF lending instruments, notably an element of pre-qualification and automaticity in using IMF resources.

The CCL is subject to demanding eligibility requirements:

- the absence of an immediate need to use IMF resources at the time of approval;
- a positive assessment of policies by the IMF, taking into account the member's adherence to internationally accepted standards (especially the IMF's Special Data Dissemination Standard or SDDS);
- constructive relations with private creditors, with a view to facilitating appropriate involvement of the private sector, and satisfactory management of external vulnerability; and

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- a satisfactory economic and financial program, which the member stands ready to adjust as needed.

As with the SRF, CCL resources are provided under Stand-By Arrangements, in combination with credit tranche resources. Access to CCL resources is expected to be in the range of 300–500 percent of quota, and does not count toward the access limits for the credit tranches and the EFF.

Upon approval of an arrangement with CCL resources, a small amount is made available but is not expected to be purchased. If a crisis strikes, the member may request the completion of an activation review, at which the Executive Board would ascertain that the member is affected by a crisis stemming from contagion and that the member's own policies had not been a significant cause of the pressures in its balance of payments. There is a presumption that one-third of the amount committed under the CCL would be released at this time. The phasing and conditionality for the remaining CCL resources would be specified in a post-activation review concluded shortly after or together with the activation review; conditionality would be expected to cover macroeconomic rather than structural policies, given the nature of the balance of payments difficulties.

The financial terms for CCL resources are identical to those governing SRF resources, except that the surcharge on CCL resources over the basic rate of charge is 150 basis points lower: the CCL surcharge is 150 basis points initially, rising by 50 basis points one year after the first purchase and every six months thereafter, up to a maximum surcharge of 350 basis points. The commitment fee for the CCL is the same as for the SRF.

### *Compensatory Financing Facility*

The CFF was the first facility aimed at helping members deal with special balance of payments problems. It was established in the 1960s to ensure timely external financing for members experiencing balance of payments difficulties resulting from a temporary decline in export earnings. A cereal import element was added in 1981; two other elements introduced since the establishment of the CFF have been removed (see Box II.5). In addition to having a balance of payments need related to export shortfalls or excess cereal import costs, the eligibility requirements include the following:

- the export shortfall or excess cereal import cost are of a short-term character;
- the shortfall or excess must be largely attributable to factors beyond the member's control; and

- if the member has balance of payments difficulties beyond the effect of the shortfall or excess, it must have a new or existing arrangement in place at the time of the request for a CFF purchase.

Access under the CFF is subject to its own limits, and does not count toward the access limits under the credit tranches and the EFF. The CFF access limits range from 45 percent of quota for each of the export shortfall and excess cereal import costs elements to a combined limit of 55 percent of quota. Within these limits, actual access is determined by the size of the shortfall or excess, and may be limited by concerns about the member's ability to repay the IMF. Access under the CFF counts toward the threshold for upper credit tranche conditionality—that is, the CFF does not “float” as regards conditionality.<sup>24</sup>

Under certain circumstances, purchases under the CFF may be phased, with purchases subsequent to the initial purchase being conditioned on the member's having an IMF arrangement in place and meeting all the conditions for a purchase or disbursement under that arrangement. They are subject to the same terms as credit tranche resources with respect to charges, repurchase expectations, and repurchase obligations; CFF purchases do not carry a surcharge, however, and do not count toward the calculation of surcharges applying to IMF credit outstanding in excess of 200 percent of quota.

In addition to the time-based early repurchase expectations, the CFF incorporates additional specific early repurchase provisions. If a member makes a purchase on the basis of estimated data for the shortfall in export earnings or excess in cereal import costs, and if the actual data, once they are available, indicate that the purchase exceeded the amount that would have been available had actual data been used, the member is expected to repurchase promptly an amount equivalent to the difference.

### ***Emergency Assistance***

The IMF has a long-standing policy of providing financial assistance to members experiencing emergencies. The conditionality associated with IMF lending for this purpose is similar to that required for purchases in the first

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<sup>24</sup>In practice, this means that a member with 25 percent of quota or more of credit outstanding under the CFF cannot access the credit tranches with first credit tranche (lower) conditionality.

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credit tranche. Two basic types of emergencies are covered by this policy: natural disasters, such as earthquakes, floods, or hurricanes; and post-conflict situations, following social disruptions.

Emergency assistance for natural disasters is available where the member cannot meet its immediate financing needs arising from a natural disaster without serious depletion of its foreign reserves. If this exigency were not present, however, IMF assistance for these members could be provided under the CFF or a Stand-By or an Extended Arrangement. The policy conditions include a statement of the general policies the member intends to pursue, and some assurance that the member will cooperate with the IMF in an effort to find, where appropriate, solutions for its balance of payments difficulties.

In post-conflict situations, emergency assistance can be made available where there is an urgent balance of payments need and a role for the IMF in catalyzing support from others, but where the institutional and administrative capacity of the member has been disrupted as a result of social conflict, so that the member is not yet able to develop and implement a comprehensive economic program that could be supported by an IMF arrangement. In these circumstances, there must nevertheless be sufficient capacity for planning and policy implementation and a demonstrated commitment by the authorities. Support from the IMF in these cases must be part of a concerted international effort to address the aftermath of the conflict situation in a comprehensive way.

IMF assistance in emergency situations was initially provided through the flexible application of policies on the use of the credit tranches, but since 2000 has been subject to a special policy outside the credit tranches. Access is normally limited to 25 percent of quota. Larger amounts can be made available on an exceptional basis: a further 25 percent of quota can be provided in post-conflict situations where progress on capacity rebuilding has been slow and the member is not in a position to move to an IMF arrangement after one year but where there is sufficient evidence of the authorities' commitment to reform and capacity to implement policies; tranching of disbursements may be appropriate in these cases. Purchases under emergency assistance are subject to the basic rate of charge and a maximum repurchase period of 3¼–5 years, but are not subject to time-based repurchase expectations and do not count toward the calculation of the surcharge on IMF credit in excess of 200 percent of quota. The IMF has set up a special administered account with the purpose of providing PRGF-eligible countries with post-conflict emergency assistance

at the concessional rate of interest of ½ of 1 percent a year (see Appendix III.) To achieve this objective, adequate donor resources will need to be mobilized.

The amounts of IMF credit outstanding by facility during 1990–2000 are shown in Figure II.4.

### **Currency Holdings**

In the balance sheet of the GRA, the IMF distinguishes between usable currencies and other currencies. Usable currencies comprise the currencies of those member countries that have a sufficiently strong balance of payments and reserve positions for their currencies to be used to provide credit to other members. These currency holdings represent the bulk of resources available to meet the future demand for IMF credit. Other currencies include the currencies of members with weaker external positions that are not being used for credit purposes, although they could become usable if the members' balance of payments positions improved, and the currencies of borrowers.

### ***Valuation of Currencies***

Currencies and securities held in the GRA's pool of resources are valued in terms of the SDR on the basis of each member's representative rate of exchange. Each member is obligated to maintain, in SDR terms, the value of the balances of the IMF's holdings of its currency in the GRA, but not those held elsewhere by the IMF, such as in the SDA or the Administered Accounts.<sup>25</sup> The total SDR value of the IMF's holdings of currencies in the GRA is kept constant through changes to the amount of members' currency balances. A member has to pay in additional currency if its currency depreciates against the SDR, and the IMF will refund some of these currency holdings if the currency appreciates. This requirement is referred to as the maintenance-of-value obligation. Because of this obligation the IMF's resources are insulated from exchange rate fluctuations.

A member's currency held by the IMF is revalued in SDR terms whenever:

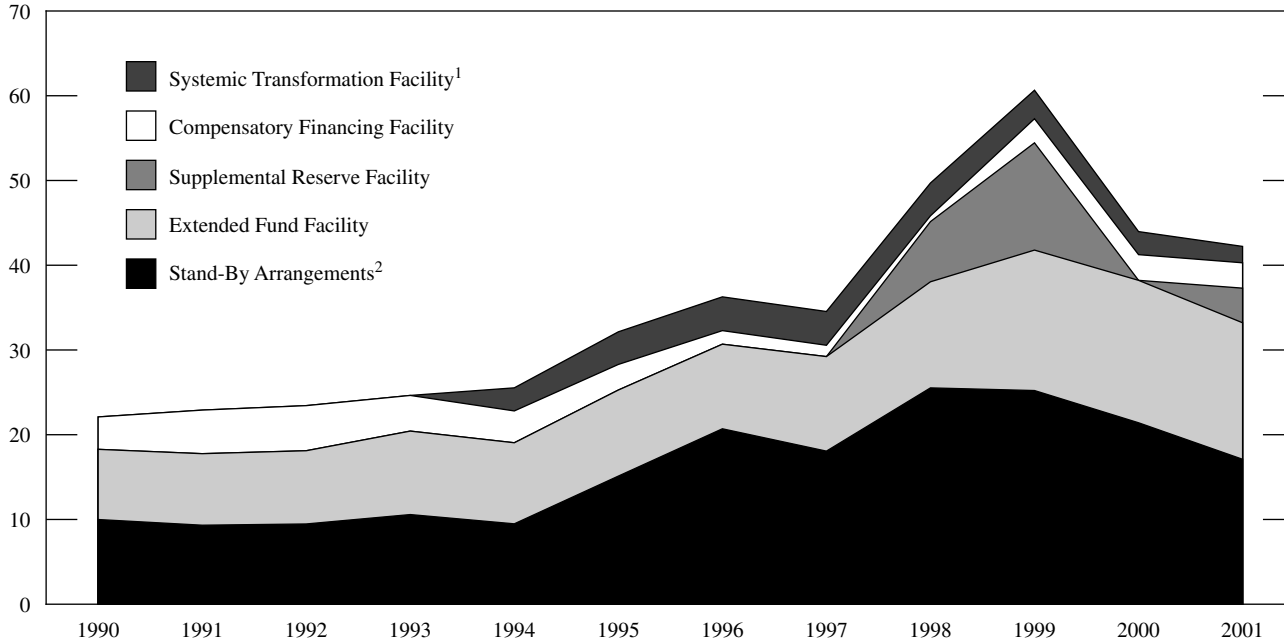
- the currency is used by the IMF in a transaction with another member,
- at the end of the IMF's financial year (April 30),

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<sup>25</sup>Revaluation changes in members' currencies in relation to the SDR in the other IMF accounts (the SDA and the Administered Accounts) are reported as valuation gains and losses for those accounts.

**FIGURE II.4. OUTSTANDING IMF CREDIT BY FACILITY, FINANCIAL YEARS ENDED APRIL 30, 1990–2001**

*(In billions of SDRs)*



<sup>1</sup>Credit extended under the 1993–95 Systemic Transformation Facility will not be fully repaid until 2005.

<sup>2</sup>Includes a small amount under the credit tranches and emergency assistance.

- at the request of a member during the year, for example, at the end of the member's financial year; and
- on such other occasions as the IMF may decide.

Whenever it becomes necessary to adjust the rate at which the IMF has recorded the use of a member's currency, the new rate becomes effective in the IMF's accounts at the close of business on the date that the new exchange rate is determined. All holdings of a member's currency in the GRA, including any unsettled obligations resulting from an earlier revaluation, are revalued at the new rate. The new rate is applied to all transactions in that currency, including administrative receipts and payments, until such a time as the rate may again need to be adjusted.

The currency valuation adjustments are part of the IMF's holdings of members' currencies. Whenever the IMF revalues its holdings of a member's currency, reflecting a change in its exchange rate with the SDR, an account receivable or an account payable is established for the amount of currency payable by or to the member in order to maintain the value of holdings of the member's currency in terms of the SDR.

### **SDR Holdings**

The IMF does not receive allocations of SDRs, but obtains its SDRs as payment of the reserve asset portion of quota subscriptions and in settlement of charges and, to a lesser degree, repayment of credit. The IMF, in turn, uses these SDRs to pay interest on creditor positions and to provide credit to members. Since SDRs were created as a supplement to existing reserve assets, the IMF does not maintain large holdings of SDRs for long periods of time, but rather recirculates the SDRs it receives back to the membership. The SDR system, and the key role of the GRA in the circulation of SDRs, is discussed in Chapter III.

### **Gold Holdings**

The IMF holds 103 million fine (troy) ounces (3,217 metric tons) of gold at designated official depositories, making it the third largest official holder of gold after the United States and Germany. IMF holdings account for about 10 percent of total official gold stocks. The IMF acquired its gold in various ways (Box II.6). The IMF's gold holdings are valued on its balance sheet on the basis of historical cost, with a book value of SDR 5.9 billion. Valued at end-April 2001 market prices, the IMF's holdings amount to over SDR 21 billion (about \$27 billion).

**BOX II.6. SOURCES AND USES OF THE IMF'S GOLD**

The IMF acquired virtually all its gold holdings through four main types of transactions under the pre-Second Amendment (1978) Articles of Agreement.

- *Subscriptions.* The original Articles of Agreement prescribed that 25 percent of initial subscriptions and quota increases was normally to be paid in gold. This represented the largest source of the IMF's gold.
- *Payment of charges.* Originally, all charges, or interest, on members' outstanding use of IMF credit were normally payable in gold.
- *Repurchases.* Members could use gold to repay the IMF for credit previously extended.
- *Purchases.* A member wishing to obtain the currency of another member could acquire it by selling gold to the IMF. The major use of this provision was sales of gold to the IMF by South Africa in 1970–71.

Outflows of gold from the IMF's holdings occurred under the pre-Second Amendment (1978) Articles of Agreement through sales of gold for currency, and via payment of remuneration and interest. Sales of gold for currency were as follows:

- *Sales for replenishment (1957–70).* In the late 1950s and in the 1960s, the IMF sold gold on several occasions to replenish its holdings of currencies.
- *South African gold and mitigation.* In the early 1970s, the IMF sold gold to members in amounts roughly corresponding to the amounts purchased earlier from South Africa; it also sold gold in connection with payments of gold for quota increases by some members, in order to mitigate the impact of these payments on the gold holdings of reserve centers.
- *Investment in U.S. Government securities (1956–72).* In order to generate income to offset operational deficits, some gold was sold to the United States and the proceeds invested in U.S. Government securities. A significant buildup of reserves through income from charges prompted the IMF to reacquire this gold from the U.S. Government in the early 1970s.
- *Auctions and "restitution" sales (1976–80).* The IMF sold approximately one-third (50 million ounces) of its then-existing gold holdings following an agreement by its members to reduce the role of gold in the international monetary system. Half of this amount was sold in restitution to members at the then-official price of SDR 35 an ounce; the other half was auctioned to the market to finance the Trust Fund, which supported concessional lending by the IMF to low-income countries.

Since 1980, the IMF has had few transactions in gold. A very small amount of gold was received from Cambodia in 1992 in discharge of its overdue obligations. In 1993, the IMF pledged to sell up to 3 million ounces of gold if the resources of the PRGF Trust Reserve Account were insufficient to cover repayments to PRGF creditors resulting from loans made to encash rights under the rights accumulation approach. Finally, during 1999–2000, the IMF conducted a series of off-market transactions in gold that left its gold holdings unchanged, in order to generate resources to help finance its participation in the HIPC Initiative.



### ***Gold in the Articles of Agreement***

Before the Second Amendment of the Articles in April 1978, the role of gold in the IMF and in the international monetary system was central and pervasive. The Second Amendment contained a number of provisions that, in combination, were intended to achieve a gradual reduction of the role of gold in the international monetary system and in the IMF. The Second Amendment:

- eliminated the use of gold as the common denominator of the par value system and as the basis of the value of the SDR;
- abolished the official price of gold and abolished the obligatory uses of gold in transactions between the IMF and its members;
- required the IMF, in its dealings in gold, to avoid managing its price or establishing a fixed price of gold; and
- included an undertaking by members to collaborate with the IMF and other members with respect to reserve assets to promote better international surveillance of international liquidity.

The Articles now limit the use of gold in the IMF's transactions. Any transactions in gold by the IMF require a decision by an 85 percent majority of the total voting power in the IMF. The IMF:

- may sell gold outright on the basis of prevailing market prices;
- may accept gold in the discharge of a member's obligations to the IMF at an agreed price on the basis of prices in the market at the time of acceptance;
- does not have the authority to engage in any other gold transactions, for example, loans, leases, swaps, or use of gold as collateral; and
- does not have the authority to buy gold.

### ***The IMF's Policy on Gold***

The IMF's policies on gold are governed by the following five principles:

- As an undervalued asset held by the IMF, gold provides fundamental strength to its balance sheet. Any mobilization of IMF gold should avoid weakening its overall financial position.
- Gold holdings provide the IMF with operational maneuverability both as regards the use of its resources and through adding credibility to its precautionary balances. In these respects, the benefits of the IMF's gold holdings are passed on to the membership at large, including both creditors and debtors.

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- The IMF should continue to hold a relatively large amount of gold among its assets, not only for prudential reasons, but also to meet unforeseen contingencies.
- The IMF has a systemic responsibility to avoid causing disruptions to the functioning of the gold market.
- Profits from any gold sales should be retained in an investment fund, and only the investment income should be used for any purposes that may be agreed upon by the IMF members.

### *The IMF's Gold Since 1980*

Uses of the IMF's gold have occurred on two occasions since 1980 without changing the IMF's long-term holdings of gold. As was the case with the open-market auctions of gold in 1976–80, these uses of gold were for the benefit of the poorest members of the IMF. Toward this end, the IMF pledged gold in 1993 and decided in 1999 to conduct off-market transactions of gold.

### *Gold Pledge*

To reassure creditors to the Enhanced Structural Adjustment Facility (ESAF) that they would be repaid for ESAF (now PRGF) loans made to encash rights under the “rights accumulation approach,” it was agreed, if necessary, to mobilize some of the IMF's gold. For this purpose, in 1993 the IMF decided—with the required 85 percent majority of the total voting power—to sell up to 3 million ounces of gold if it were determined that the resources in the PRGF Trust Reserve Account (plus other available means of financing) were insufficient to meet payments to be made from that account to PRGF creditors. The shortfall would be covered by gold sales to the extent of previous drawings on the Reserve Account attributable to overdue repayments by borrowers of loans for the encashment of rights, plus the interest earnings forgone on such drawings.

It is difficult to assess the likelihood that the gold pledge for rights encashments under PRGF arrangements would be drawn on in the future, mainly because of uncertainty about future borrowings under the rights approach. Sierra Leone and Zambia still have loans outstanding to the PRGF Trust under the rights approach, but these loans are rapidly diminishing either because they are coming close to maturity or because they are covered under the enhanced HIPC Initiative. It is, therefore, highly unlikely that the gold

pledge would be activated in connection with these loans. Moreover, the gold pledge could not be called upon until after the resources of the Reserve Account of the PRGF Trust were exhausted.<sup>26</sup> Nevertheless, three countries—Liberia, Somalia, and Sudan—remain eligible for the rights approach and could conceivably borrow sizable sums from the PRGF in connection with rights encashments at some time in the future, provided the Executive Board continues to extend the availability of the rights approach. Whether these countries will follow the rights approach to arrears clearance is uncertain. In any case, the earliest rights encashments could not take place for a few years and repayment of those PRGF loans would only commence five and half years after such disbursements.

### *Off-Market Transactions in Gold*

To help finance its contribution to the HIPC Initiative, the IMF in 1999–2000 conducted a series of off-market transactions in gold. During December 1999–April 2000, the IMF sold a total of 12.944 million fine ounces of gold to Brazil and Mexico at the prevailing market price on the day of each transaction. The total amount sold was equivalent to SDR 2.7 billion (\$3.7 billion). After each sale, the gold was immediately accepted back by the IMF at the same price in settlement of financial obligations of these members to the IMF. The net effect of these transactions left the IMF’s holdings of physical gold unchanged, but the gold accepted back was included in the IMF’s balance sheet at the market price of the transactions, instead of at the original price of SDR 35 a fine ounce.

In accordance with the Articles, the equivalent of SDR 35 a fine ounce from the proceeds of the sales was retained in the GRA. The proceeds in excess of this amount (totaling SDR 2.2 billion, or about \$2.9 billion) are held in the SDA and invested. The income from these investments, which will be transferred to the PRGF-HIPC Trust when needed, will be used to help finance the IMF’s contribution to the HIPC Initiative. In this context, the Board of Governors of the IMF adopted a resolution in September 1999 stating that the off-market gold transactions would “be a one-time operation of a highly exceptional nature.”

These gold transactions affected the IMF’s balance sheet and income as follows:

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<sup>26</sup>The Reserve Account of the PRGF Trust is discussed in Chapter IV.

## FINANCIAL ORGANIZATION AND OPERATIONS OF THE IMF

- The IMF's holdings of usable currencies in the GRA were lower, and reserve tranche positions higher, than they would otherwise have been by the amount of profit (SDR 2.2 billion). This is because Brazil and Mexico paid in gold instead of usable currencies, which would have been used to reduce reserve tranche positions of creditor members.
- The IMF's net income is affected by the remuneration expense on the continuing enlarged reserve tranche positions. The additional remuneration expense varies with the rate of remuneration, and amounted to an estimated SDR 94 million in FY2001. For comparison, the IMF's net income target for FY2001, the first year in which the full income effect of the off-market gold transactions was felt, was SDR 48 million, and for FY2002 net income is targeted at SDR 51 million.

While the transactions were successful in that they allowed the IMF to contribute to the resolution of the debt problems of the HIPC's, they resulted in an increase in the IMF's cost of operations. Since, under standard procedures (see the discussion of "Operational Income" below), this relatively large increase in cost would have resulted in a higher rate of charge, the cost increase was mitigated or offset through the existing burden-sharing mechanism and placed in the SCA-1. In the same way, SDR 94 million is being generated in FY2002.

### **The Resource and Liability Side**

#### **Quotas**

Each member of the IMF is assigned a quota and pays a capital subscription to the IMF that is equal to its quota. As noted earlier, a quarter of a member's quota subscription is normally paid in reserve assets, with the remainder paid in the member's own currency.<sup>27</sup> Quotas are expressed in SDRs and their size is determined by the IMF's Board of Governors, broadly on the basis of the economic size of the country, and taking into account quotas of similar countries. To help in this determination, five formulas are used that relate the quota to the size of the country's GDP, current account transactions, and official reserves. As of April 30, 2001, total quotas

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<sup>27</sup>The IMF has made arrangements to assist members with insufficient reserves to pay the reserve asset portion of their quota subscription payment through a same-day, no-cost IMF lending operation (see Chapter III, Box III.4).

of all members amounted to SDR 212.4 billion. A list of members and their quotas is provided in Appendix I.

Members' quotas constitute the financial base of the IMF and determine its size, as well as serve other functions as determined by the IMF's Articles.

- Quotas provide the vast bulk of reserve assets that can be used in the provision of foreign reserves by the IMF, despite the availability of borrowed resources and the growing role of administered resources to provide concessional assistance to the IMF's poorest members.
- Quotas determine the distribution of voting power in the IMF.<sup>28</sup> Quotas determine members' financial relationships with the IMF and, through the effect on voting power, members' roles in IMF decision-making and representation on the Executive Board. Many decisions are taken by a simple majority vote, though special voting majorities are required for some important financial decisions (Appendix II).
- Quotas continue to play a crucial role in determining the demand for IMF resources. Quotas serve as the basis for access to such resources in the great majority of IMF-supported programs, subject to limits set by the Articles and the Executive Board.<sup>29</sup> Over the years, however, the relationship between quotas and access has become more elastic, especially as the demand for IMF resources has become more unpredictable because of the increased role of capital flows in balance of payments disequilibria. Waivers of the Articles' limits on access to IMF resources have been granted where necessary to allow access in line with operational requirements.
- Quotas also determine a member's share in a general allocation of SDRs.<sup>30</sup>

The initial quotas of the original members of the IMF were determined at the Bretton Woods conference in 1944 (Schedule A of the IMF Articles); those of subsequent members have been determined by the IMF's Board of

<sup>28</sup>A member's voting power is equal to 250 basic votes plus one additional vote for each SDR 100,000 in quota. Basic votes therefore help to strengthen the relative voting power of members with smaller quotas.

<sup>29</sup>While the IMF's holdings of a member's currency, which measure its access to IMF credit, are restricted to no more than 200 percent of quota under the Articles (Article V, Section 3(b)(iii)), this limit—which amounts to IMF credit of 100 percent of quota—is routinely waived. See the discussion of "Access Policy" above.

<sup>30</sup>Article XVIII, Section 2(b).

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Governors, based on principles consistent with those applied to existing members. The IMF has adjusted quotas within the context of five-yearly general reviews and on an ad hoc basis outside of general reviews. An 85 percent majority of voting power is needed to change quotas.

The determination of the quota of a new member of the IMF is based on the principle that a member's quota should be in the same range as the quotas of existing members of comparable economic size and characteristics. Operationally, this principle has been applied through the use of quota formulas. Since the IMF's inception, the calculated quotas derived from the quota formulas have been used to help guide decisions regarding the size and distribution of members' actual quotas.

Quota formulas have evolved over time starting from the formula — containing national income, official reserves, imports, export variability, and the ratio of exports to national income — that was devised at Bretton Woods in 1944 to give support to the broad configuration of initial quotas that was being negotiated.

A multiformula approach was adopted in the early 1960s, when the Bretton Woods formula was revised and supplemented by four other formulas containing the same basic variables but with larger weights for external trade and export variability. The Bretton Woods formula, with its relatively high weight for national income, has generally favored large economies, while the additional four formulas have tended to produce higher quotas than the Bretton Woods formula for smaller, more open economies. The five formulas, which are listed in Box II.7, were last modified in 1982–83.

### *General Reviews*

The IMF conducts general reviews of all members' quotas normally at five year intervals.<sup>31</sup> Such reviews allow the IMF to assess the adequacy of quotas in terms of members' needs for conditional liquidity and the IMF's ability to finance those needs. A general review also allows for adjustments of members' quotas to reflect changes in their relative positions in the world economy. Of the general reviews conducted to date, only one (in 1958/59) was outside the five-year cycle.

The main issues addressed in general quota reviews are the size of an overall increase in quotas and the distribution of the increase among the

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<sup>31</sup>Article III, Section 2(a).

**BOX II.7. THE PRESENT FIVE QUOTA FORMULAS**

The present five quota formulas, with the Bretton Woods formula listed first, are:

$$CQ = (0.01Y + 0.025R + 0.05P + 0.2276VC)(1 + C/Y),$$

$$CQ = (0.0065Y + 0.0205125R + 0.078P + 0.4052VC)(1 + C/Y),$$

$$CQ = (0.0045Y + 0.03896768R + 0.07P + 0.76976VC)(1 + C/Y),$$

$$CQ = 0.005Y + 0.042280464R + 0.044(P + C) + 0.8352VC,$$

$$CQ = 0.0045Y + 0.05281008R + 0.039(P + C) + 1.0432VC,$$

where  $CQ$  = calculated quota;

$Y$  = GDP at current market prices for a recent year;

$R$  = twelve-month average of gold and foreign exchange reserves, including SDR holdings and reserve positions in the IMF, for a recent year;

$P$  = annual average of current payments (goods, services, income, and private transfers) for a recent five-year period;

$C$  = annual average of current receipts (goods, services, income, and private transfers) for a recent five-year period; and

$VC$  = variability of current receipts, defined as one standard deviation from the five-year moving average centered on the third year, for a recent 13-year period.

For each of the four non-Bretton Woods formulas, quota calculations are multiplied by an adjustment factor so that the sum of the calculations across members equals that derived from the Bretton Woods formula. The calculated quota of a member is the higher of the Bretton Woods calculation or the average of the lowest two of the remaining four calculations (after adjustment).

members. Four reviews concluded that no increase in quotas was needed. In the other eight reviews, the overall quota increase ranged from 31 percent to 61 percent (Tables II.3 and II.4).

Increases in members' quotas during general reviews typically consist of two elements: (1) an equiproportional element which is distributed to all members according to their existing quota shares; and (2) a selective element which is distributed to either all members or a subset of members. The selective element is used to attain a change in quota shares among members. For any overall increase in quotas, the larger the selective increase, the greater the redistribution of quota shares. In practice, the selective component has tended to be relatively small.

Both the list of members eligible for a selective increase and the way of distributing the selective element are based on the Executive Board's judgment. The distribution of selective quota increases have generally been based on calculated quotas.<sup>32</sup> Calculated quotas are determined by the quota formulas, which have been designed to provide a quantified measure of a country's relative economic position.<sup>33</sup> The following examples illustrate the methods used.

- During the Sixth Review in 1976, the Executive Board decided to double the quota share of the major oil exporters with the stipulation that the collective share of all the developing countries should not fall. The decision was based on the judgment that such a reallocation would strengthen the IMF's liquidity. In this instance, the quota formulas played no role in identifying the members eligible for the selective increase.
- Under the Eleventh Review in 1998, 25 percent of the quota increase was selective. The quota formulas helped determine each member's share of the selective increase as follows: (1) 15 percent of the total increase (three-fifths of the selective element) was distributed to all members; (2) in addition, 10 percent of the total increase was distributed

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<sup>32</sup>Since the Eighth Review in 1982/83, all members have received an increase comprised of an equiproportional element and a selective element that reflected a member's share in calculated quotas.

<sup>33</sup>As further explained below, formulas are one element in determining actual quotas. While quota formulas are not mentioned in the Articles, and the Executive Board has not formally adopted any formula, the Board has usually relied on them as an independent measure of members' relative economic position in the world economy. Typically, the quota resulting from the formulas—the calculated quota—is different from the actual quota of a member and, in the most recent review, actual quotas were on average less than half of calculated quotas.



TABLE II.3. GENERAL REVIEWS OF IMF QUOTAS  
(In percent)

Review of Quotas	Board of Governors' Adoption of Resolution	Equiproportional Increase in Quotas <sup>1</sup>	Overall Increase in Quotas	Entry into Effect
First Quinquennial	No increase proposed	—	—	
Second Quinquennial	No increase proposed	—	—	
1958/59	February 2, 1959 and April 6, 1959 <sup>2</sup>	50	60.7	April 6, 1959
Third Quinquennial	No increase proposed	—	—	
Fourth Quinquennial	March 31, 1965	25	30.7	February 23, 1966
Fifth General	February 9, 1970	25	35.4	October 30, 1970
Sixth General	March 22, 1976	Increases were determined on the basis of different groups of countries	33.6	April 1, 1978
Seventh General	December 11, 1978	50	50.9	November 29, 1980
Eighth General	March 31, 1983	19	47.5	November 30, 1983
Ninth General	June 28, 1990	30	50.0	November 11, 1992
Tenth General	No increase proposed	—	—	
Eleventh General	January 30, 1998	33.75	45.0	January 22, 1999

<sup>1</sup>Uniform percentage increase for all members participating in the review.

<sup>2</sup>The February 1959 resolution provided for an equiproportional increase of 50 percent and special increases for 3 countries; the resolution adopted in April 1959 provided for special increases for 14 additional countries.

TABLE II.4. CHANGES IN IMF QUOTAS  
(Quotas in millions of SDRs)<sup>1</sup>

Year	IMF Membership (1)	Proposed Quotas (2)	Changes in Proposed Quotas				
			New members <sup>2</sup>		General reviews <sup>3</sup> (5)	Ad hoc and other (6)	Total <sup>4</sup> (7)
			Number (3)	Quotas (4)			
1944 <sup>5</sup>	40	7,514.00	40	7,514.00	—	—	—
1950	49	8,036.50	10	649.50	—	-2.00 <sup>6</sup>	522.50
			(1)	(125.00)	—	—	—
1955	58	8,750.50	10	837.00	—	2.00 <sup>6</sup>	714.00
			(1)	(125.00)	—	—	—
1959	69	14,640.25	11	404.50	5,328.75	156.50 <sup>7</sup>	5,889.75
1965	102	20,932.00	34	756.75	4,791.75	793.25	6,291.75
			(1)	(50.00)	—	—	—
1970	116	28,776.00	14	204.25	7,393.50	246.25	7,844.00
1976	133	38,976.40	17	445.40	9,755.00	—	10,200.40
1978	141	59,605.50	8	140.10	19,839.00	650.00	20,629.10
1983	146	89,236.30	5	394.40	28,176.50	1,059.90	29,630.80
1990	154	135,214.70 <sup>8</sup>	10	1,016.75	45,082.15	—	45,978.40
			(2)	(120.50)	—	—	—
1998	183 <sup>9</sup>	212,029.00	31	12,736.65	65,802.95	40.00	76,814.30
			(2)	(1,765.30)	—	—	—
2001	183	213,711.00	—	—	—	1,682.00 <sup>10</sup>	1,682.00

<sup>1</sup>Quotas in the IMF were expressed in U.S. dollars at the equivalent of the 1934 official gold price until the Sixth General Review of Quotas in 1976, when the IMF's unit of account had switched to the SDR, again valued at the 1934 official gold price. Consequently, the U.S. dollar and SDR, through 1970, are directly comparable at an exchange rate of SDR 1 = US\$1.

<sup>2</sup>Countries that withdrew from membership or whose memberships were conferred to successor countries are shown in parentheses.

<sup>3</sup>As of the dates of adoption of Board of Governors' resolutions proposing adjustments in members' quotas.

<sup>4</sup>Sum of columns (4), (5), and (6).

<sup>5</sup>Excluding Australia, Haiti, Liberia, New Zealand, and the U.S.S.R., which did not join the IMF at the time of the Bretton Woods Agreement (see Schedule A of the Articles of Agreement), and including increases agreed for Egypt, France, the Islamic Republic of Iran, and Paraguay shortly after the IMF began operations.

<sup>6</sup>The quota of Honduras was reduced at its request for 1948 but was restored to the original amount in 1951.

<sup>7</sup>Includes SDR 121.0 million of special allocations for countries with small quotas.

<sup>8</sup>Includes Cambodia, which did not participate in the Ninth General Review.

<sup>9</sup>Includes the Federal Republic of Yugoslavia, which had not yet succeeded to IMF membership. On December 20, 2000, the Executive Board of the IMF determined that the Federal Republic of Yugoslavia had fulfilled the necessary conditions to succeed to membership in the IMF.

<sup>10</sup>Ad hoc increase for China.

to those countries whose ratio of calculated to actual quotas was considered to be most “out of line.”<sup>34</sup>

Adjustments of quota shares have tended to take place within general reviews, usually in the context of an urgent need for additional resources on the part of the IMF. This reflects the fact that it has been easier to reach agreement if all members receive an increase in quotas. Agreement is more difficult to reach when only a subset of members receives an increase, as the quotas of all other members would remain unchanged and their quota shares would decline.

### *Ad Hoc Increases*

A member can request an adjustment of its quota at any time.<sup>35</sup> Ad hoc quota increases can occur both within and outside the context of a general review. In recent years, they have tended to occur within a general review. As with selective increases, both the quota formulas and the Executive Board’s judgment have played a role in determining the amount of the ad hoc adjustment. The following are examples.

- Five members (France, the Islamic Republic of Iran, Egypt, Paraguay, and the Philippines) received ad hoc increases between 1947 and 1959. The main factor underlying these increases was the view that the initial quotas of these members at the time of the Bretton Woods conference in 1945 had been set at unduly low levels. Between 1959 and 1969, the quotas of another nine countries were adjusted on an ad hoc basis. All of the foregoing increases occurred outside the context of a general review.
- Japan received an ad hoc increase under the Ninth Review. In this case, the seven largest industrial countries agreed to redistribute quota increases among themselves in such a manner that the quota increases for the rest of the membership were not affected.<sup>36</sup>

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<sup>34</sup>“Out of line” was defined as those countries with ratios of calculated to actual quotas above one. Thirty-eight members met this criterion. Five of these members, whose quotas were farthest out of line and which were able to contribute to the IMF’s liquidity over the medium term, received 1 percent of the 10 percent share going to the group of 38 members.

<sup>35</sup>Under Article III, Section 2(a), the IMF may, “if it thinks fit, consider at any other time the adjustment of any particular quota at the request of the member concerned.”

<sup>36</sup>As a result of this redistribution to accommodate an ad hoc increase in the quota of Japan, the new quotas for Germany and Japan were equalized, as were the quotas of France and the United Kingdom (ranked just below those of Japan and Germany), and adjustments were made to the quotas of the United States, Canada, and Italy so that the total quotas for the seven countries as a group was maintained unchanged.

Since 1970, there have been only four ad hoc increases in quotas outside the framework of a general review. Ad hoc increases in the quotas of China in 1980 and of Cambodia in 1994 were associated with the change in representation of the member in the IMF (China) and the resumption of active relations with the IMF (Cambodia), as China's initial quota had never been increased and Cambodia's quota had not been increased since 1970. Saudi Arabia received an ad hoc increase in 1981. A major factor underlying Saudi Arabia's ad hoc increase was the desire to strengthen the IMF's liquidity position during the developing country debt crisis before the Eighth Review had been completed. China also received an ad hoc quota increase in 2001 to better reflect its position in the world economy following its resumption of exercising sovereignty over Hong Kong. For each of the post-1969 cases, the quota formulas played a role in determining the extent of the ad hoc increase.

### ***Role of the Quota Formulas***

In practice, the role of the quota formulas in determining actual quotas and quota share adjustments has been quite limited. As noted above, quota increases in the context of general reviews have been distributed largely on the basis of a uniform proportionate increase in actual quotas. The continuing significant difference between actual and calculated quota shares reflects:

- the Executive Board's view that general quota reviews should provide all members with an adequate increase in quota;
- a general reluctance to make politically difficult quota share adjustments; and
- widespread dissatisfaction with formulas that were viewed as overly complex, lacking in transparency, and not representative of actual conditions in the world economy.

In 1999, the IMF established an external panel of independent experts, the Quota Formula Review Group (QFRG), to assess the adequacy of the formulas used to guide the determination of quotas and to make recommendations for reforms that would take account of changes in the world economy and the international financial system and the increasing globalization of markets. The eight member panel, chaired by Professor Richard Cooper of Harvard University, submitted a report that was considered by the Executive

Board, along with a staff commentary, in August 2000. The report and staff commentary were subsequently published on the IMF's website.<sup>37</sup>

The QFRG report provided information about the history and operation of the quota formulas, suggested guiding principles for future reforms, and presented recommendations to simplify and update the formulas. The Executive Board discussion revealed a wide range of views on the issues raised in the report and the staff commentary. There was general recognition of the need to simplify the present formulas and to update them to take account of the growing role of capital flows. However, concern was expressed that a preliminary partial quantification of the formula recommended by the panel pointed toward a greater concentration of quotas among the largest industrial countries (subsequently confirmed by more complete and updated staff calculations).<sup>38</sup> Executive Directors agreed on the need to carry forward the work of the external panel with a view to developing quota formulas that more fully reflect members' roles in the world economy. The International Monetary and Financial Committee (IMFC) supported this view at their meeting in Prague in September 2001, and a work program has been adopted to further consider alternative quota formulas prior to the 2001 Annual Meetings.

### **Reserve Tranche Positions**

In making the reserve asset portion of their quota payment, members acquire a liquid claim on the IMF in exchange for the reserves they provide, much like a demand deposit in a commercial bank. This claim is called the reserve tranche position; it is equal to the member's quota less the IMF's holdings of the member's currency in the GRA (excluding currency holdings that stem from the member's own use of credit). The share of a member's subscription maintained in reserve assets varies over time from its initial level of some 25 percent at the time of quota payment. A member's reserve tranche position increases when the IMF uses its currency to lend to other members, and decreases when borrowing members use the currency to make repayments. Reserve tranche positions are part of members' liquid international reserves because a member may, subject only to its representation of a balance of payments need, convert its SDR-denominated reserve asset into

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<sup>37</sup>See <http://www.imf.org/external/np/tre/quota/2000/eng/qfrg/report/index.htm> and <http://www.imf.org/external/np/tre/quota/2000/eng/qfrg/comment/index.htm>.

<sup>38</sup>See <http://www.imf.org/external/np/tre/quota/2001/eng/erqfq.htm>.

one or more freely usable currencies by drawing on the IMF (Box II.8). A member is obligated, if necessary, to provide an amount of reserve assets of up to 100 percent of its quota. The amount of reserve assets provided to the IMF has in practice fallen well below this maximum (Figure II.5).

The IMF pays interest, called remuneration, on a member's reserve position in the IMF, except on a small portion that is provided to the IMF as an interest-free resource. This unremunerated (non-interest-bearing) portion of the reserve tranche position is equal to 25 percent of the member's quota on April 1, 1978—that part of the quota that was paid in gold prior to the Second Amendment of the IMF's Articles. The gold tranche was never remunerated historically, so it was natural to set aside this same amount in terms of SDRs on this date as the unremunerated reserve tranche. For a member that joined the IMF after that date, the unremunerated reserve tranche is the same percentage of its initial quota as the average unremunerated reserve tranche was as a percentage of the quotas of all other members when the new member joined the IMF. The unremunerated reserve tranche remains fixed for each member in nominal terms, but because of subsequent quota increases, it is now significantly lower when expressed as a percentage of quota.<sup>39</sup> The average is equal to 3.8 percent, but the actual percentage is different for each member.

### Precautionary Balances

The IMF's resources in the GRA increase through additions to its precautionary balances, which comprise reserves and balances that have been set aside in the first Special Contingent Account (SCA-1). The level and rate of accumulation of precautionary balances reflect the IMF's assessment of the risk of future operational deficits and general credit risk, including that aris-

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<sup>39</sup>In the past, the proportion of the reserve tranche that was remunerated was sometimes related to the concept of the "norm" for remuneration, which was calculated as the total of (1) 75 percent of a member's quota before the Second Amendment, plus (2) any subsequent increases in quota. For a country that became a member after April 1, 1978, the norm is a percentage of its quota equal to the weighted average relative to quota of the norms applicable to all other members on the date that the member joined the IMF, plus the amounts of any increases in its quota afterward. At each quota increase, a member's norm rises, becoming closer to 100 percent of its quota. The remunerated reserve tranche excludes certain holdings: all currency holdings acquired when the member used IMF resources, and currency holdings in the IMF No. 2 Account that are less than  $\frac{1}{10}$  of 1 percent of the member's quota. See the section on "IMF Accounts in Member Countries."

**BOX II.8. RESERVE TRANCHE POLICIES**

The reserve tranche can be considered as the “facility of first resort.” It stands apart from the credit tranches and the various facilities in that a member’s reserve tranche position is part of its own foreign exchange reserves. Purchases in the reserve tranche do not therefore constitute use of IMF credit. To preserve this character as a reserve asset available at the discretion of the member, the IMF has adopted reserve tranche policies:

- The definition of the reserve tranche (quota less holdings of the member’s currency) explicitly excludes currency holdings arising from past use of IMF credit. This is intended to enable members to make purchases in the credit tranches without having first to use their reserve tranche. The member can choose which resources to use first.
- Purchases in the reserve tranche are subject to a representation by the member of a balance of payments need, as with any use of IMF resources, but the member’s representation of need cannot be challenged by the IMF.
- Reserve tranche purchases are not subject to conditionality, charges, or repurchase expectations and obligations.

ing from overdue obligations and the risk that debtor members in good standing might at some point fall into arrears. This latter risk increases with the level and concentration of outstanding credit, but is contained by the positive economic effects of members’ adjustment policies and the IMF’s preferred creditor status. Reserves also provide a small amount of liquidity in the GRA. The level and composition of the precautionary balances in the GRA in recent years are shown in Table II.5.

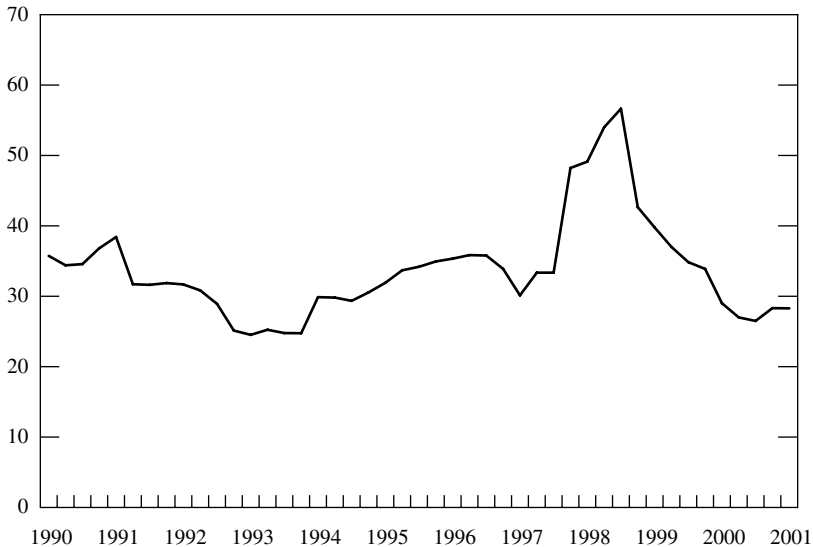
Reserves reflect accumulated net income and comprise the Special Reserve and the General Reserve. Resources in the Special Reserve may be used for any purpose for which resources in the General Reserve may be used, except distribution.

- The Special Reserve was established in 1957, initially with the proceeds from a gold investment program, to provide safeguards against operational deficits that were subsequently charged against this reserve. Additions to the Special Reserve have since been financed from net income, other than income derived from the SRF.
- The General Reserve was established in 1958 to meet capital losses or administrative deficits. From FY1998, SRF net income has been placed



**FIGURE II.5. AVERAGE RESERVE POSITION OF MEMBERS IN THE FINANCIAL TRANSACTIONS PLAN, JANUARY 1990–APRIL 2001**

*(In percent of quota)*



in the General Reserve, which is the only income placed in this reserve since 1971. Any distribution of the General Reserve must be made to all members in proportion to their quotas.

Special Contingent Accounts (SCAs) are established and balances accumulated as part of the IMF's overall strategy to protect itself against the negative financial impact of protracted arrears, that is, obligations that have remained overdue for at least six months.<sup>40</sup> The SCA-1 was established in 1987 as a safeguard against potential losses resulting from an ultimate failure of members in protracted arrears to settle their financial obligations to the IMF. After an initial placement of SDR 26.5 million of excess income in that year, annual additions to the SCA-1 have been generated through "burden-

<sup>40</sup>The IMF also levies special charges on repurchases and charges overdue for less than six months. See Chapter V, "Protecting the IMF's Financial Position."

**FINANCIAL ORGANIZATION AND OPERATIONS OF THE IMF**
**TABLE II.5. LEVEL OF PRECAUTIONARY BALANCES IN THE GRA**

	End of Financial Year					
	1996	1997	1998	1999	2000 <sup>1</sup>	2001 <sup>1</sup>
	<i>(In billions of SDRs)</i>					
Reserves	1.9	2.0	2.1	2.6	2.8	3.0
SCA-1	0.7	0.8	0.9	1.0	1.1	1.2
SCA-2 <sup>2</sup>	<u>0.9</u>	<u>1.0</u>	<u>1.0</u>	<u>1.0</u>	<u>—</u>	<u>—</u>
Precautionary balances	3.5	3.8	4.0	4.6	3.9	4.2
Less: credit in arrears	-1.1	-1.1	-1.0	-1.0	-1.0	-0.9
SCA-2 <sup>2</sup>	<u>-0.9</u>	<u>-1.0</u>	<u>-1.0</u>	<u>-1.0</u>	<u>—</u>	<u>—</u>
Free reserves	1.5	1.7	2.0	2.6	2.9	3.3
	<i>(In percent)</i>					
Free reserves as a percentage of credit in good standing	4.2	5.1	4.1	4.3	7.0	8.0
Precautionary balances as a percentage of total credit outstanding	9.7	10.9	8.1	7.5	9.0	10.0

<sup>1</sup>Excludes cumulative effects of change in accounting method in FY2000.

<sup>2</sup>See Box II.9.

sharing” adjustments to the rate of charge and the rate of remuneration (Box II.9). These allocations have amounted to 5 percent of GRA reserves at the beginning of the year up until FY2001, when the allocation was reduced to 3.3 percent. Balances in the SCA-1 are refundable to the contributing debtor and creditor member countries when all overdue obligations have been settled, or earlier if the IMF so decides.<sup>41</sup>

The IMF’s objective to date has been to maintain a level of total precautionary balances at least equal to credit to members in protracted arrears, a goal that was first achieved in FY1993, and which has since been maintained.

<sup>41</sup>A second Special Contingent Account (SCA-2) was established as a safeguard against possible losses arising from purchases made through the encashment of rights accumulated under a rights accumulation program (RAP), and to provide additional liquidity for the financing of those encashments (see Box II.9 and Chapter V). SCA-2 was terminated in 1999.

### BOX II.9. THE BURDEN-SHARING MECHANISM

Since 1986, the burden-sharing mechanism has made up for the loss of income from unpaid charges and has been used to accumulate resources in two Special Contingent Accounts (SCAs). The mechanism works by providing for additions and deductions to the rates of charge and remuneration, respectively.

Resources collected from individual members under the mechanism are refundable to them as arrears cases are resolved, or as may be decided by the IMF. Thus, resources collected for unpaid charges are refunded when these charges are eventually settled. At end-April 2001, cumulative deferred charges that were subject to burden sharing amounted to SDR 1,796 million and settlements of unpaid charges of SDR 993 million had been made and refunded.

Of the two Special Contingent Accounts, the first, SCA-1, was established specifically to protect against the financial impact of arrears in general. The second, SCA-2, collected resources (1) to finance the encashment of “rights” earned by eligible members in arrears to later draw on IMF resources, and (2) to safeguard against the risk of loss arising from purchases made in connection with the encashment of rights. SCA-2 was terminated in 1999, and the balances in the account refunded, after it was concluded that other precautionary balances in the GRA provided adequate protection against the risks associated with rights-related credit. The termination of SCA-2 was also part of an overall agreement on the financing of the PRGF (then ESAF) and HIPC initiatives, for which it was envisaged that some members would voluntarily contribute resources refunded from SCA-2.

In the aggregate, creditor and debtor members have contributed equal amounts for unpaid charges and for allocations to the SCA-1, whereas creditors provided three-fourths of the amounts contributed to the SCA-2. A total of SDR 1.2 billion had been accumulated in the SCA-1 at end-April 2001. A total of SDR 1 billion was accumulated during the operation of the SCA-2 in 1990–97.

In addition, to protect itself against general credit risk, the IMF has established a target for precautionary balances in excess of overdue credit. The target range for these “free reserves” is 3–5 percent of the amount of outstanding “credit in good standing.” Free reserves had risen to 8.0 percent of credit in good standing at end-April 2001 (see Table II.5).

### *Income and Expenses*

The amount added to reserves each year is the net income resulting from the difference between operational income and operational and administrative expenses.

Virtually all of the IMF's operational income is derived from the charges (interest on loans) that are levied on the outstanding use of credit in the GRA. In addition to the basic rate of charge (i.e., the rate of charge before burden sharing), the use of IMF credit under certain circumstances is subject to surcharges, and all IMF credit is subject to service charges, commitment fees on credit lines, and special charges (see Table II.2).<sup>42</sup> A small amount of income is also generated by receipts of interest on the IMF's SDR holdings (as explained in Chapter III).

Operational expenses consist of the remuneration (interest) paid on remunerated reserve tranche positions, the allocation to the SCA-1, and the payment of interest on outstanding IMF borrowing, if any. Net operational income (operational income less operational expenses) is used to cover the IMF's administrative expenses, and the remainder constitutes net income (Table II.6).<sup>43</sup>

### *Operational Income*

The IMF aims to achieve a target level of net income each financial year to add to its reserves.<sup>44</sup> Based on the net income target, the SDR interest rate, projected credit, and the outlook for administrative expenses, the IMF estimates the basic rate of charge that is necessary to achieve the income target.<sup>45</sup> The basic rate is set for the year as a proportion of the SDR interest rate. For FY2001, this proportion was set at 115.9 percent.

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<sup>42</sup>The IMF also has access to a relatively small amount of interest-free resources, including its precautionary balances and the unremunerated portion of reserve tranche positions of members.

<sup>43</sup>The Income Statement of the General Department also includes the income of the SDA, which is discussed later in this chapter.

<sup>44</sup>The annual increase in reserves was set as 3 percent of reserves in the GRA at the beginning of the year for financial years 1981–84, 5 percent for financial years 1985–99, 3.9 percent for financial year 2000, and 1.7 percent for financial years 2001–02. These figures exclude income from surcharges.

<sup>45</sup>The procedure setting the basic rate of charge is governed by Rule I-6(4).

TABLE II.6. INCOME STATEMENT OF THE GENERAL DEPARTMENT,  
FINANCIAL YEAR ENDED APRIL 30, 2001  
(In millions of SDRs)

GRA operational income	
Interest and charges	2,207.1
Interest on SDR holdings	112.5
Other charges and income	68.7
	<u>2,388.3</u>
GRA operational expenses	
Remuneration and financing costs	1,734.3
Allocation to SCA-1	94.0
	<u>1,828.3</u>
GRA administrative expenses	384.6
Net GRA income	<u>175.5</u>
SDA income	
Income earned on investments	150.0
Interest on loans	1.4
Net SDA income	<u>151.4</u>

Note: Numbers may not add to totals due to rounding.

A separate midyear review is undertaken to establish whether an adjustment to the basic rate of charge is required in view of developments during the year.

At the end of the financial year, if net income exceeds the amount projected at the beginning of the year, the Executive Board has, in recent years, decided to reduce the rate of charge retroactively. Alternatively, the Board can decide to:

- place all or part of any excess to reserves; or
- make a distribution of excess income to members; or
- take the excess into account to lower the net income target for the subsequent financial year.

When net income falls short of the target, the Executive Board has generally decided to increase the rate of charge in the subsequent financial year to make up for the shortfall.

### *Operational Expenses*

The IMF pays remuneration (interest) on members' reserve tranche positions equal to the SDR interest rate, except on a small portion, as indicated earlier (see section on "Reserve Tranche Positions").<sup>46</sup> Remuneration payments account for almost all of IMF operational expenses when there is no outstanding IMF borrowing. If borrowing is outstanding, the IMF also pays interest on it. The interest rate on borrowing under the General Arrangements to Borrow (GAB) is equal to the SDR interest rate, while under the New Arrangements to Borrow (NAB), it may be equal to or higher than the SDR interest rate, as explained below under "Borrowing."

### *Administrative Expenses*

The IMF's administrative expenses can be divided into personnel, travel, building occupancy, and other such costs. Personnel and travel-related outlays typically account for about 80 percent of total administrative expenses. The GRA is reimbursed for the cost of administering the SDR Department through an assessment levied in proportion to each participant's allocation of SDRs. The GRA is also to be reimbursed for the expenses incurred in administering the PRGF Trust. However, following the establishment of the SRF and the consequent increase in net income, this reimbursement has been forgone and the amount that would otherwise have been reimbursed has been transferred to the PRGF-HIPC Trust. This arrangement has been in place since 1998 and is expected to continue up to 2004.

## **Borrowing**

The IMF can borrow to supplement its quota resources. It maintains two standing borrowing arrangements with official lenders and can borrow from private markets, although it has not done so to date. Borrowing has played an important role in providing temporary, supplemental resources to the IMF at critical junctures in the past (Table II.7). In recent years, the borrowing arrangements with official lenders have been enlarged and their participation broadened, strengthening IMF liquidity.

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<sup>46</sup> The basic (unadjusted) rate of remuneration has been equal to the SDR interest rate since February 1, 1987. However, refundable adjustments to that rate are made under "burden sharing." The Articles require that the rate of remuneration be maintained in the range of 80–100 percent of the SDR interest rate. The current relationship between the rate of remuneration and the SDR interest rate is governed by Rule I-10.

TABLE II.7. IMF BORROWING  
(In billions of SDRs)

	Number of Countries or Central Banks	Agreed Amount
<b>Current borrowing arrangements</b>		
General Arrangements to Borrow (1983–2003)	11	17.0
Associated agreement with Saudi Arabia (1983–2003)	1	1.5
New Arrangements to Borrow (1998–2003)	25	34.0
<b>Past borrowing arrangements</b>		
General Arrangements to Borrow (1962–83)	10	6.4
Oil facility (1974)	7	2.8
Oil facility (1975)	12	2.9
Supplementary financing facility (1979–84)	14	7.8
Enlarged access to resources		
Medium-term (1981)		
Saudi Arabian Monetary Agency (SAMA)	1	8.0
Short-term (1981)		
Bank for International Settlements (BIS) and others	19	1.3
Short-term (1984)		
SAMA, BIS, Government of Japan, and National Bank of Belgium	4	6.0
Government of Japan (1986)	1	3.0

### ***Current Borrowing Arrangements***

The General Arrangements to Borrow have been in place since 1962. The GAB were originally conceived as arrangements whereby the main industrial (Group of Ten) countries agreed to stand ready to lend the IMF up to specified amounts of their currencies, thereby strengthening its financial position. These loans would be made when supplementary resources were needed by the IMF to help finance drawings by GAB participants in a setting where such financing would forestall or cope with an impairment of the international monetary system. Because the industrial countries have the largest quotas and may, when they need to, claim a large proportion of the IMF's usable resources, the GAB provide strong support for the IMF's financial soundness and for ensuring that resources available to other countries are not reduced.

## FINANCIAL ORGANIZATION AND OPERATIONS OF THE IMF

The GAB enable the IMF to borrow specified amounts of currencies from 11 industrial countries or their central banks, under certain circumstances, at market-related rates of interest (Table II.8). The potential amount of credit available to the IMF under the GAB is SDR 17 billion, with an additional SDR 1.5 billion available under an associated agreement with Saudi Arabia.

The GAB are reviewed and renewed regularly. A broad review of the GAB was undertaken in 1983, at the outset of the developing country debt crisis. The most important changes to emerge from that review were the substantial enlargement of the GAB to its present size (from about SDR 6 billion), the addition of SDR 1.5 billion under the associated agreement with Saudi Arabia, and the change to permit use of the GAB to finance IMF lending to nonparticipants in the GAB if the IMF faces an inadequacy of resources. Since 1983, the GAB and the associated agreement with Saudi Arabia have been renewed every four or five years without further modification, most recently for a further five-year period from December 26, 1998.

The GAB have been activated ten times. The GAB were last activated in July 1998 for an amount of SDR 6.3 billion (SDR 1.4 billion of which was drawn) in connection with the financing of an Extended Arrangement for Russia. The activation for Russia was canceled in March 1999, when the IMF repaid the outstanding amount following the coming into effect of the Eleventh General Review of Quotas and payment of the bulk of the quota increases. Prior to the activation for Russia, the most recent activation occurred in 1977, when the IMF borrowed for lending to the United Kingdom and Italy under Stand-By Arrangements, and in 1978 to finance a reserve tranche purchase by the United States. A proposal for calls on the GAB by the IMF's Managing Director can become effective only if it is accepted by the GAB participants, and the proposal is then approved by the Executive Board.

The IMF also has New Arrangements to Borrow to deal with financial crises. Following the Mexican financial crisis in December 1994, concern that substantially more resources might be needed to respond to future financial crises prompted participants in the June 1995 Group of Seven Halifax Summit to call on the Group of Ten and other financially strong countries to develop financing arrangements that would double the amount available to the IMF under the GAB. The NAB became effective on November 17, 1998.

The NAB effectively double the resources available under the GAB. The NAB are a set of credit arrangements between the IMF and 25 members and institutions to provide supplementary resources to the IMF to forestall or cope with an impairment of the international monetary system or to deal with an exceptional situation to the stability of that system. The NAB do not



TABLE II.8. GENERAL AND NEW ARRANGEMENTS TO BORROW  
(In millions of SDRs)

Participant	General Arrangements to Borrow	New Arrangements to Borrow
Australia	n.a.	810.0
Austria	n.a.	412.0
Belgium	595.0	967.0
Canada	892.5	1,396.0
Denmark	n.a.	371.0
Deutsche Bundesbank	2,380.0	3,557.0
Finland	n.a.	340.0
France	1,700.0	2,577.0
Hong Kong Monetary Authority	n.a.	340.0
Italy	1,105.0	1,772.0
Japan	2,125.0	3,557.0
Korea	n.a.	340.0
Kuwait	n.a.	345.0
Luxembourg	n.a.	340.0
Malaysia	n.a.	340.0
Netherlands	850.0	1,316.0
Norway	n.a.	383.0
Saudi Arabia	n.a.	1,780.0
Singapore	n.a.	340.0
Spain	n.a.	672.0
Sveriges Riksbank	382.5	859.0
Swiss National Bank	1,020.0	1,557.0
Thailand	n.a.	340.0
United Kingdom	1,700.0	2,577.0
United States	4,250.0	6,712.0
Total	17,000.0	34,000.0
Associated agreement with Saudi Arabia	1,500.0	n.a.

replace the GAB, which remain in force. However, the NAB are the first and principal recourse in the event of a need to provide supplementary resources to the IMF. The total amount of resources available to the IMF under the NAB and GAB combined is SDR 34 billion.

The NAB can be renewed and enlarged. The NAB decision will be in effect for five years from its effective date and may be renewed, at which time an IMF member or institution that is not currently a participant in the NAB may be accepted as a participant, if the IMF and participants representing 80 percent of the total credit arrangements agree to the request. New participants may be accepted at other times by way of an amendment to the NAB adopted by a decision of the IMF's Executive Board and with the concurrence of participants representing 85 percent of total credit arrangements. Commitments from participants are based on relative economic strength, as measured by actual IMF quotas, as a predominant criterion.

Activation procedures for the NAB are modeled on the GAB. The NAB have been activated once — to finance a Stand-By Arrangement for Brazil in December 1998, when the IMF called on funding of SDR 9.1 billion (SDR 2.9 billion of which was used). This activation was canceled on March 11, 1999, when the IMF repaid the outstanding amount following the entry into effect of the Eleventh General Review of Quotas and payment of the bulk of the quota increases.

### *Past Borrowing Arrangements*

The IMF borrowed extensively when payments imbalances were large and persistent. Reliance on borrowing was especially heavy during the period of large payments imbalances between the early 1970s and the mid-1980s, when borrowing financed 40–60 percent of IMF credit. The need for supplemental resources to meet the heavy demand for IMF resources stemmed in part from the relatively small increases in quotas approved in the 1970s, and the need to bridge to the increases in quotas in 1980 and 1983. Also important was the skewed distribution of payments imbalances relative to the distribution of quotas at the time:

- large payments surpluses were concentrated in a comparatively small number of members with relatively small quotas; and
- payments deficits were far more widely dispersed and were large relative to the quotas of most members.

The IMF has borrowed only from official sources. Borrowing has been almost exclusively from members or their monetary authorities, the exceptions being nonmember Switzerland (now a member), the Hong Kong Mon-

etary Authority (under the NAB), and the Bank for International Settlements (BIS). Borrowing from official sources has the advantage that these lenders are familiar with the IMF's needs and operational features, and there is by now a substantial body of experience from which to draw. The IMF is permitted to borrow from private sources and has considered this option on several occasions: the prevailing view has been that resort to private market borrowing would change the cooperative and monetary nature of the institution in ways that would be undesirable; a number of operational issues would also need to be addressed, such as the use of collateral, managing financial risk, and the cost relative to official borrowing.

Borrowing arrangements share many common characteristics:

- *Denomination of borrowing.* The indebtedness of members to the IMF is denominated in SDRs. To avoid exchange risks, IMF borrowing has generally been denominated in SDRs or the currencies that make up the SDR basket in proportion to their weight in that basket.
- *Media of payment.* The IMF cannot borrow SDRs. In most bilateral borrowing agreements, the lender has provided U.S. dollars or its own freely usable currency, or the lender has undertaken to convert its currency into a freely usable currency as needed by the IMF. For repayment, the IMF has generally sought maximum flexibility in the borrowing agreement but lenders have on occasion insisted on repayment in the currency of their choice, usually U.S. dollars or their own currency.
- *Maturities.* The IMF seeks to match the maturities of its assets and liabilities. Under the two Oil Facilities and the SFF, for example, the IMF borrowed when currency was needed for purchase and repaid lenders when the corresponding repurchases were made. This was not possible under the borrowing agreements established for the Enlarged Access Policy (EAP), as some central banks were willing to lend only at the short end of the maturity spectrum (see Table II.7). The resulting mismatch of maturities led to the establishment of Borrowed Resources Suspense Accounts within the GRA as a means of holding and investing temporarily currencies not yet needed to finance purchases under the EAP.
- *Liquidity and transferability.* Borrowing agreements with lenders other than the BIS have consistently provided for encashability at face value upon representation of balance of payments need. These agreements further stipulate that the IMF would give such a representation the overwhelming benefit of the doubt. A member's lending to the IMF is therefore regarded as a liquid reserve asset and is included as part of the member's international reserves. In addition, claims on the IMF are

normally transferable to other official holders, which provides some protection to the IMF's liquidity.

- *Interest rates.* In the early years of the IMF, interest rates on IMF borrowing and charges on purchases financed by borrowed resources were very low. Following the introduction of remuneration with the First Amendment of the Articles of Agreement in 1969, more attention was paid to the rate of return on the reserves that members made available to the IMF. Market rates were increasingly seen by members as the opportunity cost of lending to the IMF. In line with market practice, borrowing agreements since 1977 have provided for floating interest rates. To protect the IMF's income position, the cost of borrowing plus a small margin has been reflected in the rate of charge on the use of borrowed resources.

### **Management of Financial Resources and the Liquidity Position**

As noted above, not all of the IMF's resources are immediately available for lending. The IMF's usable resources consist of currencies of IMF members with a strong balance of payments position and SDRs, which stem mainly from quota payments. The institution maintains substantial holdings of gold and other fixed assets, but these are not used in lending operations. Borrowing by the IMF to finance the extension of credit through the GRA is an important complement to the use of its quota resources but remains the exception rather than the rule. Borrowing is, however, a central feature of IMF lending under the PRGF, as discussed in Chapter IV.

The usability of the IMF's currency holdings varies over time. In principle, the currencies of all members are available for use in IMF transactions. Members have an obligation to convert balances of their currency purchased from the IMF by other members into one of the four freely usable currencies: the U.S. dollar, the euro, the Japanese yen, and the pound sterling.<sup>47</sup> The IMF determines which members are in a sufficiently strong external position to meet this currency exchange obligation when drawing up its quarterly financial transactions plan (see below). The currencies of these

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<sup>47</sup>Article V, Section 3(e)(i).

members are considered to be usable in IMF transactions for the duration of that quarter, while all other currencies are considered unusable.

The IMF's holdings of SDRs are a readily usable resource, but these holdings account for only a small fraction of the IMF's assets. The use of SDRs held by the IMF is therefore not limited to the same extent as the use of its currency holdings. The IMF periodically establishes a long-term target range for the level of its SDR holdings, which guides the actual use of SDRs in IMF transactions. Other factors affecting the level of the IMF's holdings of SDRs are discussed in Chapter III.

The IMF closely monitors its liquidity position. Table II.9 presents the IMF's financial resources and liquidity position as of April 30, 2001.<sup>48</sup> For this purpose, the stock of usable resources is adjusted downward to take into account amounts already committed to members under existing IMF arrangements. A further downward adjustment is made to ensure that the IMF retains at all times sufficient working balances of each of the currencies of members included in the financial transactions plan. The resulting amount of net uncommitted usable resources is in principle available to meet new demand for IMF resources. In practice, however, the adequacy of the IMF's liquidity position must also take into account the existence of liquid claims accumulated by its creditor members: reserve tranche positions and any outstanding loans under the GAB and NAB. These are considered liquid liabilities because they can be drawn at short notice in the event of balance of payments need, akin to demand deposits in a commercial bank, and are thus the first claim on IMF resources. The liquidity ratio ties these two concepts together in a single measure of the IMF's liquidity. Historically, the liquidity ratio has never fallen below 25–30 percent.

### **Financial Transactions Plan**

The IMF manages its usable resources through a financial transactions plan. This is the mechanism through which the IMF selects the members whose currencies are to be used in IMF transactions and allocates the financing of those transactions among members included in the plan. Both currencies and SDRs are included in the financial transactions plan for transfers (credits) from the IMF to borrowing members but only currencies

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<sup>48</sup>The IMF's "Financial Resources and Liquidity Position" is posted monthly on the IMF's website (<http://www.imf.org/external/np/tre/liquid>).

**FINANCIAL ORGANIZATION AND OPERATIONS OF THE IMF**TABLE II.9. IMF FINANCIAL RESOURCES AND LIQUIDITY POSITION,  
APRIL 30, 2001*(In billions of SDRs unless otherwise indicated)*

I.	Total resources	217.5
	Members' currencies	207.9
	Gold holdings	5.9
	SDR holdings	2.4
	Other assets	1.3
	Available under GAB/NAB activation	—
II.	Unusable resources	105.4
III.	Usable resources (I – II)	112.1
IV.	Amounts committed under arrangements	18.1
V.	Minimum working balances	15.3
VI.	Net uncommitted usable resources (III – IV – V)	78.7
VII.	Balances available under the GAB/NAB	34.0
VIII.	Liquid liabilities	46.7
	Reserve tranche positions	46.7
	Outstanding borrowing under the GAB/NAB	—
IX.	Liquidity ratio (VI/VIII, in percent)	168.4

Note: Numbers may not add to totals due to rounding.

are included for receipts (repayments) from borrowing members; receipts in SDRs are not managed through the plan as the IMF has little or no discretion over their use by members. The total amount for transfers in the transactions plan is based on the expected volume of credit to be extended to members and operational payments by the IMF (such as interest on official borrowing by the IMF) during the plan period. Receipts in currencies are estimated on the basis of the schedule of forthcoming repayments and the preferences of members with respect to the media of payment (i.e., currencies versus SDRs).

Currency selection is based on judgments about the external positions of members. The currencies of members are selected for inclusion in the financial transactions plan based on a finding by the IMF that the member's balance of payments and reserve position is sufficiently strong. Specific indicators of external strength are used to maintain a reasonable degree of consistency among members, but the assessment of a member's combined balance of payments and reserve position is ultimately a matter of judgment. It has not therefore been considered desirable to rely on automatic indicators or to define rigidly the notion of a sufficiently strong external position; the circumstances of members, including their need to hold reserves, differ considerably.

All relevant factors and data are considered in this assessment. Particular emphasis is placed on recent and prospective current account balances, external competitiveness, and external debt indicators, especially those offering insights into the member's exposure to short-term liquidity strains. Members may be included in the financial transactions plan even though there may be some elements of weakness in their overall balance of payments and reserve position.

Two broader considerations underlying the financial structure of the IMF have guided the staff and the Executive Board in coming to conclusions about a member's external strength for the purpose of participation in the financial transactions plan.

- First, the IMF draws on a wide range of members—large and small, advanced, developing, and transition—for its financial activities, reflecting first and foremost the cooperative nature of the institution. Broad participation of members in the financial transactions plan also works to maximize the liquidity of the GRA.
- Second, the use of a member's currency in the financial transactions plan generally entails a change in the composition of the member's international reserves. For most of these members, IMF transactions involve a reduction (increase) in their foreign exchange holdings, which is fully offset by an increase (decrease) in their reserve tranche position in the IMF. This creditor position is included as part of the member's international reserves as it is a liquid claim on foreign exchange resources that can be drawn on demand in the event of balance of payments need.

Decisions on the selection of currencies are taken by the Executive Board. The staff proposes a list of members it considers sufficiently strong each quarter, and the Executive Board takes a decision based on this list. It

## FINANCIAL ORGANIZATION AND OPERATIONS OF THE IMF

is open to an Executive Director to request the exclusion or inclusion of any member, but the decision rests with the Executive Board as a whole. A member's consent to its inclusion is not required, although its views on its balance of payments and reserve position are taken into account by the Executive Board before a decision is taken. The outcome of the financial transactions plan is published on the IMF's website.<sup>49</sup>

Currency allocation aims to maintain broadly even participation among members. The allocation of transfers and receipts among members in the financial transactions plan is based on guidelines established by the Executive Board.<sup>50</sup> The currencies of all members included in the financial transactions plan are allocated for transfers in direct proportion to their quotas. Receipts are allocated to members' currencies included in the plan so as to ensure that the creditor positions of members included in the plan remain broadly balanced over time in relation to quota. The net impact of both transfers and receipts on reserve tranche positions is illustrated in Figure II.6.

If a currency included in the financial transactions plan is not one of the currencies that the IMF has determined to be freely usable in the principal foreign exchange markets, the issuing member is required, if requested by a purchasing member at the time of the purchase, to exchange the amount of its currency sold by the IMF for a freely usable currency (in most cases, the U.S. dollar) at the representative exchange rate as advised by the IMF. Procedures have also been established for the exchange of each freely usable currency into other freely usable currencies. Similar procedures apply to exchanges of currencies related to repurchases.

### Special Disbursement Account

The SDA was initially activated to receive transfers from the Trust Fund. The Trust Fund had been funded largely from the sale of gold and upon its termination in 1981, all Trust Fund loan repayments were transferred to the SDA. Loans were provided from the SDA under the Structural Adjustment Facility (SAF), which was established in March 1986 to provide balance of

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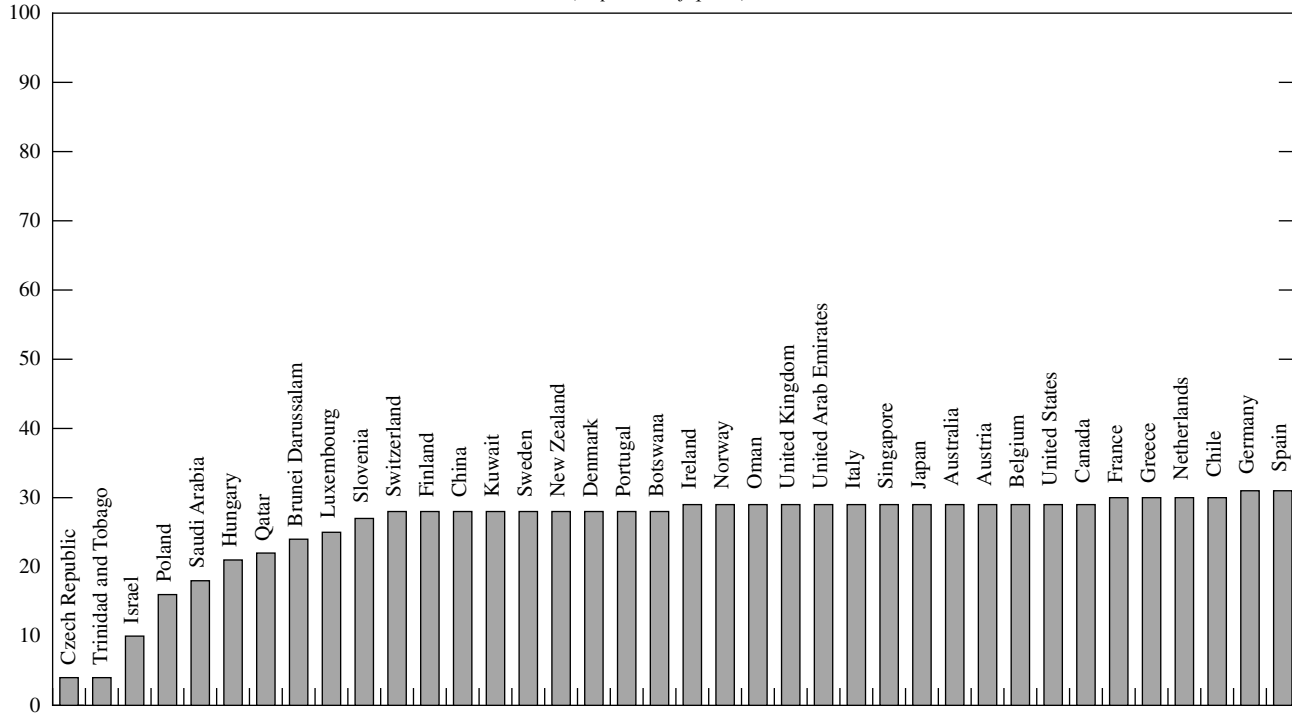
<sup>49</sup>The "Quarterly Report on Financing IMF Transactions" is posted one quarter after the end of the period on the IMF's website (<http://www.imf.org/external/np/tre/ftp>).

<sup>50</sup>See *Selected Decisions and Documents of the International Monetary Fund* (Washington: IMF, Twenty-Fifth Issue, June 30, 2000), pp. 260–65.



**FIGURE II.6. RESERVE POSITIONS, AS OF APRIL 30, 2001**

(In percent of quota)



Source: International Monetary Fund, *International Financial Statistics*.

## FINANCIAL ORGANIZATION AND OPERATIONS OF THE IMF

payments assistance on concessional terms to qualifying low-income member countries, from 1986 until the end of 1995, when the SAF itself was phased out.<sup>51</sup> From the establishment of the Enhanced Structural Adjustment Facility (ESAF) in December 1987 until February 1994, unused SDA resources were also used to finance ESAF loans.

The assets of the SDA now consist of the remaining loan balances outstanding under the SAF and investments in marketable fixed-income securities. These assets originate from the transfers received from the Trust Fund and the profits from the sale of a portion of the IMF's gold in financial year 2000. The net income from the investment of gold profits has been authorized for transfers, on an as-needed basis in accordance with the decisions of the IMF, to the Poverty Reduction and Growth Facility–Heavily Indebted Poor Countries Trust (PRGF-HIPC Trust).

Chapter IV discusses the financing and conduct of concessional lending by the IMF, including the investment of SDA resources.

### **IMF Accounts in Member Countries**

The IMF conducts its financial dealings with a member through the fiscal agency and the depository designated by the member. The fiscal agency may be the member's treasury (ministry of finance), central bank, official monetary agency, stabilization fund, or other similar agency. The IMF can only deal with, or through, the designated fiscal agency, which is authorized to carry out transactions with the IMF on behalf of the member country. In addition, each member is required to designate its central bank as a depository for the IMF's holdings of the member's currency, or if it has no central bank, a monetary agency or a commercial bank acceptable to the IMF. Most members of the IMF have designated their central bank as both the depository and the fiscal agency. The depository is required to pay out of the IMF's holdings of the member's currency, on demand and without delay, sums to any payee named by the IMF in the member's own territory, and to hold securities on behalf of the IMF should the member decide to issue nonnegotiable, non-interest-bearing notes, or similar instruments, in substitution for part of the IMF's currency holdings. Each member guarantees all assets of the IMF against loss resulting from failure or default on the part of the

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<sup>51</sup>Interest on SAF loans is charged at ½ of 1 percent a year.

depository. Thus, the IMF's pool of currencies and reserve assets in the GRA are not held at the IMF, but in depositories in the member countries.

The depository maintains, without any service charge or commission, two accounts that are used to record the IMF's holdings of the member's currency: the IMF No. 1 Account and the IMF No. 2 Account. The No. 1 Account is used for IMF transactions, including subscription payments, purchases and repurchases (i.e., use and repayment of GRA resources), and repayment of resources borrowed by the IMF. Payment of charges on the use of IMF credit and the IMF's payment of interest on reserve tranche positions are conducted in SDRs and therefore not recorded in these accounts. Provided that a minimum is maintained in the No. 1 Account, as explained below, all these transactions can alternatively be carried out through the IMF Securities Account. A member may establish an IMF Securities Account in order to substitute parts of the holdings in the IMF No. 1 Account with nonnegotiable, non-interest-bearing notes, or similar instruments payable to the IMF on demand when the currency is needed for the IMF's transactions. The depository holds these notes for safekeeping and acts as the agent of the IMF to obtain encashment of the notes in order to maintain, at all times, the minimum required balance in the No. 1 Account.<sup>52</sup>

The No. 2 Account is used for the IMF's administrative expenditures and receipts (for example, from sales of IMF publications) in the member's currency and within its territory. The balances in both the No. 1 and No. 2 Accounts that originate from the payment of the local currency portion of quota subscriptions do not yield any interest for the IMF. The currency portion of the subscribed capital, while fully paid, is held in non-interest-bearing form and generates no income for the IMF until used and converted into claims on members in the form of use of IMF credit.

### **Disclosure of Financial Position with the IMF in the Member Country<sup>53</sup>**

When a member has designated the central bank as both depository and fiscal agent, the central bank should present the full financial position of the

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<sup>52</sup>If any payment by the IMF reduces the balance in the No. 1 Account below a minimum of  $\frac{1}{4}$  of 1 percent of the member's quota, the balance is to be restored to that level by the next business day through the encashment of sufficient notes.

<sup>53</sup>This discussion presents IMF member positions in the General and SDR Departments.

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member with the IMF in its balance sheet.<sup>54</sup> A central bank may choose to indicate this on either a gross or net basis. The position in the General Department is presented on a gross basis if the IMF No. 1, No. 2, and Securities Accounts are shown as liabilities and the member's quota is shown as an asset. Membership in the SDR Department would be indicated by showing SDR holdings as an asset and the cumulative SDR allocation as a liability.

Members may also choose to reflect their financial position on a net basis. A member who has a net reserve tranche position in the IMF and is not using IMF credit would present the net reserve tranche position as an asset.<sup>55</sup> Members with a net reserve tranche position who are also using credit in the GRA would disclose the reserve tranche as an asset and currency holdings stemming from the use of IMF credit as a liability, since the IMF is not entitled to demand settlement or offset a member's use of credit from its reserve tranche position. The members' position in the SDR Department may also be shown on a net basis. The presentation of IMF-related assets and liabilities should be further elaborated in the explanatory notes to the financial statements and, as a minimum, provide information not available in the balance sheet regarding the member's quota, the composition of the IMF's currency holdings, and the maturity structure of IMF credit, if any.

In cases where the central bank acts as depository and the ministry of finance, treasury, or a similar agency is the fiscal agent, it is recommended that the central bank record all IMF-related assets and liabilities and offset these against government accounts.<sup>56</sup> While practices may differ depending on the relationship between the central bank and the agency acting as fiscal agent, this approach ensures public disclosure of the member's financial relationship with the IMF, since government agencies typically do not pre-

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<sup>54</sup>For this reason it is also recommended to include the Securities Account in the IMF position, even though the actual securities may be issued by the government. The IMF considers securities issued in lieu of currency deposits to the IMF No. 1 Account equivalent to currency holdings because they are encashable on demand. Exclusion of the Securities Account would therefore misrepresent the member's overall IMF position.

<sup>55</sup>A member has a net reserve tranche position when its quota exceeds the IMF's holdings of its currencies, excluding currencies stemming from the use of IMF credit and holdings in the No. 2 Account that are less than  $\frac{1}{10}$  of 1 percent of quota.

<sup>56</sup>Of the IMF's 183 member countries, only 41 have not designated their central bank as the fiscal agent.

pare financial statements.<sup>57</sup> Consolidating the IMF position in the balance sheet of the central bank also allows for a simple reconciliation between foreign reserves data monitored under an IMF-supported program or published by a member and the balance sheet of the central bank. Since most central banks are subject to an annual audit, full inclusion of the IMF position provides additional assurance about the accuracy and availability of foreign reserves.

Appendix IV illustrates how IMF membership could be presented on either a gross or net basis in the balance sheet of a central bank that acts as both fiscal agent and depository for the member with the IMF.

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<sup>57</sup>PRGF transactions would also be shown in the balance sheet of the central bank if the central bank were the recipient of the proceeds of PRGF disbursements.