



# The Global Financial Crisis: Increasing IMF Resources and the Role of Congress

**Jonathan E. Sanford**

Specialist in International Trade and Finance

**Martin A. Weiss**

Specialist in International Trade and Finance

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## Summary

The current global financial crisis is testing the ability of the International Monetary Fund (IMF), and other international financial institutions (IFIs) to provide sufficient assistance to affected countries. It has also enhanced the IMF's role in crisis management and given it a key place in current efforts to reform the world financial system.

During the past half-year, many countries have come to the IMF for assistance and more are likely to apply. Several steps have been taken to expand the IMF's financial resources and to otherwise augment the funds available to help vulnerable countries weather the present crisis.

At their meeting in London on April 2, 2009, the leaders of the 20 systemically important industrialized and developing countries (G-20) agreed on several initiatives affecting the IMF and other international organizations. They agreed that the New Arrangements to Borrow (NAB), a supplemental fund to bolster IMF resources, should be increased by up to \$500 billion from its present level of \$50 billion. The Obama Administration has proposed a U.S. contribution of up to \$100 billion. Pledges totaling \$255 billion have been received from several countries and others are considering additional contributions. The G-20 also agreed that the IMF should create new Special Drawing Rights (SDRs) to a value of \$250 billion and to allocate them to its members through its SDR Department. These new resources would expand world foreign exchange reserves by about 4% and provide needed resources to countries in crisis. The G-20 said in addition that \$250 billion would be provided, through their bilateral agencies and through the multilateral development banks (MDBs), for new trade finance, and they said the MDBs should increase their level of assistance by \$100 billion to meet crisis needs. They also agreed that poor countries should be aided with some of the gold the IMF is planning to sell. Details of the plans for new trade finance and aid to poor countries have not yet been released. Already pending at the time of the G-20 meeting was a proposal for a new increase in IMF quota resources. Negotiations on a package of reforms and a new quota increase had been completed in April 2008 and submitted to the House and Senate leadership by the Bush Administration last November. The U.S. share would be SDR 4.97 billion (about \$8 billion). The package includes reforms in the IMF governance process, finances, and procedures. It also includes a proposal that the IMF sell 403 metric tons of gold to create a facility that would cover the costs of its country and global surveillance, technical assistance, research, and other non-lending operations. Also pending in 2008 was a proposed Fourth Amendment to the IMF Articles, originally proposed in 1997, that would create a new allocation of about SDR 21.4 billion.

Some elements of the above require congressional approval and some do not. U.S. participation in the new IMF quota increase and a U.S. subscription of \$100 billion for the NAB would require congressional approval. Likewise, amendments to the IMF Articles—including the prospective Fourth Amendment for a new SDR allocation—would require congressional approval. On the other hand, the proposed \$250 billion allocation of SDRs (which is being made under a different provision of the IMF Articles) is too small to trigger the legal requirement that Congress give its assent. Any contributions to the IMF, to fund increases in the U.S. quota or to subscribe new resources to the NAB, must be authorized by Congress. In 1967, a Presidential Commission on Budget Concepts recommended that U.S. payments to the IMF should not be treated as budget outlay but rather they should be counted as an exchange of assets which is matched by transfers of equivalent value to the United States from the IMF. Since that time, payments to the IMF have been deemed to have no impact on the Federal budget or on the Federal budget deficit.

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On April 2, 2009, leaders from 20 of the world's largest economies—the Group of 20 (or G-20)—met in London, U.K., to discuss measures that might be taken to address the current global economic crisis.<sup>1</sup> They reached agreement in general terms on some steps they might take to (1) help stimulate consumption and recovery in their countries as well as the world economy and (2) help coordinate and strengthen regulation of world financial markets, although they did not commit to any specific steps they should take to address these problems. The area of clearest and most specific agreement among the G-20, however, involved expanding the stock of financial resources available to the IMF (**Box 1**) by an additional \$500 billion to enhance its capacity to assist troubled countries requesting its aid.<sup>2</sup> G-20 members also agreed to create an additional \$250 billion in IMF Special Drawing Rights (SDRs). The G-20 agreement to increase the resources of the IMF was approved at the April 2009 spring meeting of the IMF Board of Governors' International Monetary and Financial Committee (IMFC).<sup>3</sup>

This report provides information on (1) the role the IMF has played in the financial crisis, (2) international agreement to increase the financial resources of the IMF, and (3) the role of Congress in increasing the Fund's resources. As will be discussed in detail at the end of the report, congressional authorization, and perhaps appropriation, would be required to increase U.S. contributions to the IMF.

## Background: Economic Impact of the Financial Crisis

What began as a bursting of the U.S. housing market bubble and a rise in foreclosures has ballooned into a global financial and economic crisis. The crisis has exposed fundamental weaknesses in financial systems worldwide. Despite coordinated easing of monetary policy and trillions of dollars in intervention by central banks and governments, economies continue to decline into what is turning out to be the most severe global recession since the Great Depression of the 1930s.

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<sup>1</sup> Members of the G-20 are: Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Africa, South Korea, Turkey, the United Kingdom, the United States, and the European Union.

<sup>2</sup> Global plan for recovery and reform: the Communiqué from the London Summit, available at: <http://www.londonsummit.gov.uk/en/summit-aims/summit-communicue/>

<sup>3</sup> The IMFC has the responsibility of advising, and reporting to, the Board of Governors on matters relating to the Board of Governors' functions in supervising the management and adaptation of the international monetary and financial system, reviewing developments in global liquidity and the transfer of resources to developing countries; considering proposals by the Executive Board to amend the Articles of Agreement; and dealing with disturbances that might threaten the system. The IMFC has 24 members who are governors of the Fund, ministers, or others of comparable rank. The membership reflects the composition of the IMF's Executive Board: each member country that appoints, and each group of member countries that elects, an Executive Director appoints a member of the IMFC.

### **Box I. The International Monetary Fund**

The IMF was created in 1946, a result of the 1944 international financial conference at Bretton Woods, New Hampshire. It was created in order to prevent a return of the international financial chaos that preceded -- and in some ways precipitated -- World War II. During the 1930s, many countries pursued "beggar-thy-neighbor" economic policies -- restricting purchases from abroad in order to save scarce foreign exchange, cutting the value of their currencies in order to underprice foreign competitors, and hampering international financial flows -- in ways that deepened the world depression and accelerated the decline in economic activity.

The IMF was designed to limit or prevent this kind of economic behavior. Technically, the IMF is a specialized agency of the United Nations, but it functions virtually independently of UN control. The IMF must obey directives of the U.N. Security Council, but it need not comply with directives from the U.N. General Assembly or other U.N. agencies. Rather than being organized on a one-country, one-vote basis, as is the United Nations, it has weighted voting. The IMF has 185 member countries, whose voting share depends on the size of their quota or financial commitment to the organization. A country's quota is determined by its GDP size, its openness to international trade and other factors. The amount a country can borrow is determined by the size of its quota. The United States is the largest single shareholder, with a 16.77% voting share. The nine Executive Directors (EDs) representing the G-7 countries and other advanced countries in Europe share nearly 56% of the vote. Most decisions are reached by simple majority, though this is generally expressed by consensus. Some special matters (changes in the Articles of Agreement or approval of new quota increases, for example) require an 85% vote. Because the U.S. vote exceeds 15%, however, no quota increases, amendments or other major actions can go into effect without its affirmative vote. The same can be said for other major blocks of IMF member countries.

As stated in its Articles of Agreement, the purposes of the IMF are (1) to promote international cooperation on international monetary problems, (2) to facilitate the expansion and balanced growth of international trade, promoting high levels of employment and real income and the development of productive resources in all member countries, (3) to promote exchange rate stability and to avoid competitive exchange rate depreciation, (4) to help establish a multilateral system of payments among countries for current transactions and to help eliminate foreign exchange restrictions which hamper world trade, (5) to make loans to countries on a temporary basis with adequate safeguards for repayment, "thus providing them with opportunity to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity," and (6) to shorten with such loans the duration and to lessen the degree of disequilibrium in countries' balances of payments.

The IMF is an international financial institution (IFI) which deals mainly with balance of payments (BOP), exchange rate, and international monetary concerns. It originally focused mainly on macroeconomic issues. It monitored the macroeconomic and exchange rate policies of member countries and it helped countries overcome BOP crises with short-term loans conditioned on their making improvements in macroeconomic performance. It left microeconomic issues and domestic institutional issues to the World Bank and the other multilateral development banks (MDBs). In recent years, however, the Fund has found that these issues have a much larger impact on countries' abilities to pursue effective macroeconomic and exchange rate policies. Increasingly, it has included them among the subjects which need to be addressed in the context of its loan programs. It has also given these issues more attention in its consultations with member country governments, its surveillance activities, and its technical assistance activity.

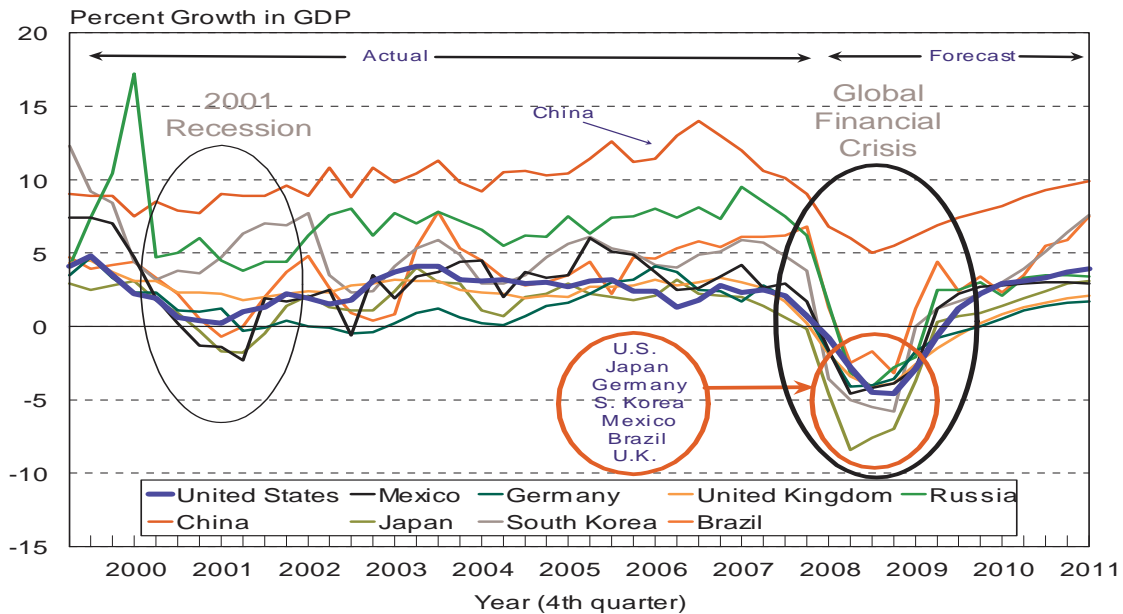
The IMF is a monetary institution, not a development agency. Its sister agency, the World Bank, was created at the same time as the IMF in order to provide long-term loans and to stimulate growth and economic development in war-damaged and developing countries. Even so, economic development and growth are core objectives of the IMF, as specified in purposes 2 and 4 above. The founders believed that international monetary stability would facilitate the growth of world trade and that this in turn would generate higher levels of employment, increased income, and expanded growth and development in the countries participating in the post-World War II international economy.

The founders expected (purposes 5 and 6) that the IMF would be a means through which countries could remedy their domestic economic problems without resorting to the kinds of "beggar-thy-neighbor" practices which sought to shift the burden of adjustment onto other countries. Countries with chronic BOP deficits could get short-term IMF loans to help them weather a balance of payments crisis. It was generally presumed that BOP deficits, inflation, unemployment and low levels of economic activity were the result of inappropriate domestic economic policies. Better policies and adjustments in the exchange rate for the country's currency were deemed to be the appropriate response to this situation. It was expected that IMF assistance would help countries shorten the depth and duration of their economic problems and help contain or prevent the spread of monetary instability to other countries.

## Economic Growth Rates

On April 22, 2009, the International Monetary Fund (IMF) revised its forecast for world economic growth down to -1.3% for 2009. This would be the lowest level of growth since World War II and would be down from the IMF’s forecast in January 2009 that global economic output would grow by 0.5% this year and its projection in November 2008 that growth in 2009 would be around 1.7%. The World Bank, in March 2009, issued an equally pessimistic outlook, projecting (without providing a specific figure) that the world economy will contract (negative growth) in 2009.<sup>4</sup> As shown in **Figure 1**, countries world-wide are experiencing a simultaneous downturn in economic activity. The advanced industrialized countries of North America, Europe, and Japan are declining into recession, and economic growth rates in most developing and emerging market countries are also in marked decline. Even China, though its economy continues to expand, has experience a substantial reduction in its rate of economic growth. These declines in economic activity have been accompanied by losses of trillions of dollars in equity markets and a credit squeeze that not only are affecting households and businesses worldwide but are putting a damper on the financing of activities such as world trade and oil exploration. The International Labor Organization expects global unemployment in 2009 to increase over 2007 by a range of 18 million to 30 million workers, and more than 50 million if the situation continues to deteriorate.<sup>5</sup> In the latter case, some 200 million workers, mostly in developing economies, could find themselves in extreme poverty.

**Figure 1. Selected Economic Growth Rates, 2000-2001**

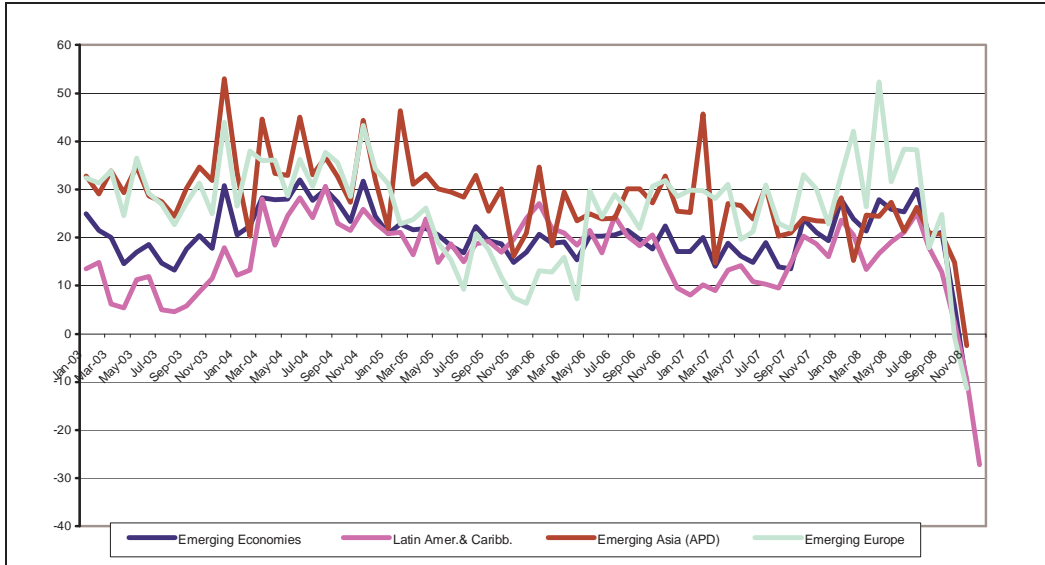


**Source:** Congressional Research Service with data from Global Insight, March 15, monthly forecast, using annualized quarterly changes in growth rates.

<sup>4</sup> *Swimming Against the Tide: How Developing Countries are Coping with the Global Crisis*, Background Paper prepared by World Bank Staff for the G20 Finance Ministers and Central Bank Governors Meeting, Horsham, United Kingdom on March 13-14, 2009.

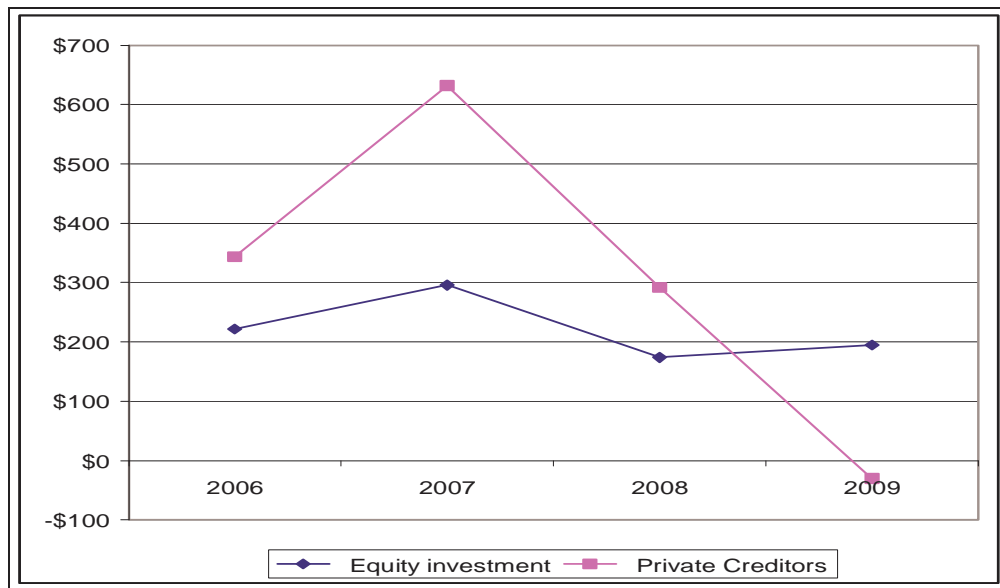
<sup>5</sup> *Global Employment Trends Report 2009*, International Labour Organization, January 2009.

**Figure 2. Merchandise Exports from Emerging Markets, 2003 - 2008**  
(in percentage change from year earlier)



Source: International Monetary Fund

**Figure 3. Net Private Capital Flows to Emerging Markets**  
(\$ in billions)

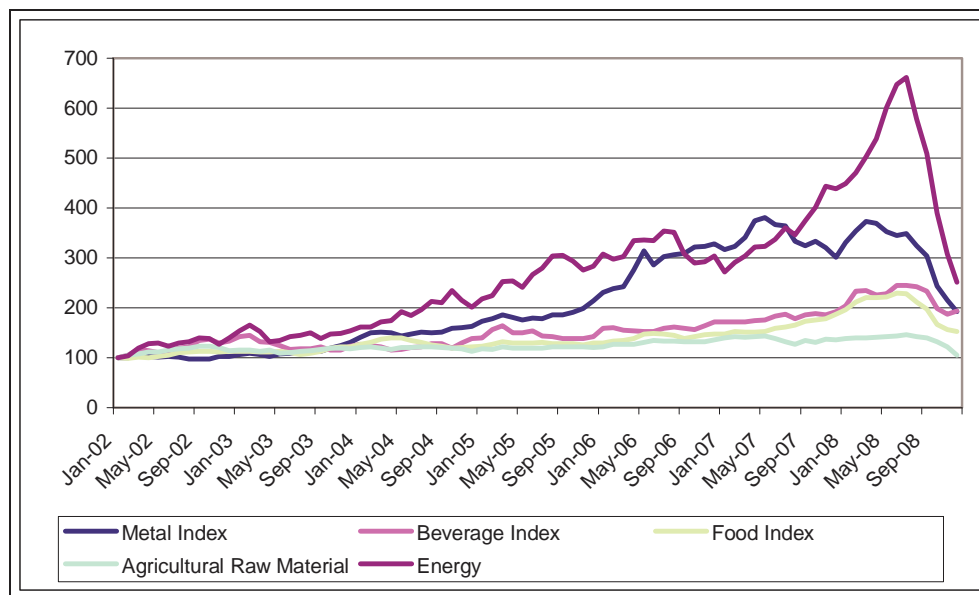


Source: Institute for International Finance: "Capital Flows To Emerging Market Economies." January 27, 2009



**Figure 4. Commodity Price Indices**

(index: Jan. 2002=100)



Source: International Monetary Fund

Developing and emerging market countries are seeing the collapse in growth through several channels. First, economic slowdown in the advanced economies is leading to decreased demand for exports (**Figure 2**) and a contraction of capital flows (**Figure 3**). Developing countries also suffer from the collapse of commodity prices (**Figure 4**). Rapid economic growth in China and India over the past decade led to record prices for petroleum, minerals, and other commodities. Between 2003 and 2008, oil prices rose by 320% and food prices by 138%. Since mid-2008, however, weakening demand for these exports has led to a rapid decline in the price of many of these commodities. Because many of the poorest countries are heavily dependent on a few primary export commodities, rapid swings in commodity prices can wreak havoc on their domestic economies. Yemen, for example, announced in January that it would have to decrease public expenditures by 50% because of the financial crisis and the lower government revenues from its oil exports.

## Impact of the Financial Crisis on World Poverty

While the poorest countries, many in sub-Saharan Africa, are less integrated into global capital markets than the advanced industrial nations or emerging economies in Eastern Europe, the global economic slowdown is affecting their standards of living and is expected to lead to higher levels of global poverty – and not just in the least developed countries. Many argue that the impact on poverty may be felt most strongly in the large, middle-income countries such as China and India, the world’s two most populous nations. Over the past two decades, the largest gains in raising people out of poverty have been made in these two countries. For several years China has averaged 10% annual economic growth, while India has grown upwards of 8% annually between 2002 and 2007. The World Bank estimates each one percentage point drop in world economic growth could trap another 20 million people in poverty. Slow economic growth in both of these countries could push millions into poverty as well as have other adverse effects in less-developed economies. The International Labor Organization predicts that some 50 million more people



around the world will be unemployed in 2009 compared to 2007. The majority of these newly unemployed will likely be in developing countries.<sup>6</sup>

According to recent World Bank research, almost 40% of developing countries are highly exposed to the poverty effects of the crisis due to both declining growth rates and high initial poverty levels. An additional 56% of countries are moderately exposed due to either decelerating growth or high poverty levels, but not both. Over 90% of developing countries face a greater risk of increased poverty because of the financial crisis. While advanced economies are expanding their fiscal deficits with robust stimulus packages, the World Bank finds that only one quarter of the exposed countries have the ability to expand their fiscal deficits. One third of developing countries with reasonable fiscal capacity are aid-dependent and will require extensive bilateral and multilateral support if they are to increase fiscal spending.<sup>7</sup>

Lower levels of world remittances will also impact poverty levels. The combination of slow growth rates, job losses, and the rising cost of living in advanced countries has led to fewer economic migrants from developing countries and lower levels of remittances. This could have major effects in countries which provide large numbers of migrant workers, including Mexico, India, Bangladesh, and the Philippines. The volume of remittances soared over the past decade, but recent data show significant deceleration since the beginning of the current crisis with Latin America and Caribbean the hardest hit. The Inter-American Development Bank calculates that remittances to the region declined by 1.7% between 2007 and 2008.

While many countries were already having difficulties making progress in meeting the Millennium Development Goals (MDGs),<sup>8</sup> the financial crisis will likely further hinder their efforts. According to the World Bank, by 2007, countries had only made sufficient progress toward achieving two MDGs, those for poverty reduction and access to safe water to be on track of reaching the 2015 targets (**Figure 5**). The decline in world employment; the shift away from export-oriented industries; and the decline of remittances are expected to jeopardize many of the recent gains in poverty reduction throughout the developing world. The World Bank notes that it is difficult to assess the exact impact the financial crisis is likely to have. However, research on prior crises suggests that:

countries that suffered economic contractions of 10 percent or more between 1980 and 2004 experienced, for example, more than one million excess infant deaths. Evidence suggests that growth collapses are costly for human development outcomes, as they deteriorate more quickly during growth decelerations than they improve during growth accelerations. The average GDP growth rate of developing countries is now projected to fall in 2009 to less than half the pre-crisis rate. The projected lower growth path will sharply slow the reduction in infant mortality. Preliminary analysis shows that, as a result, infant deaths in developing

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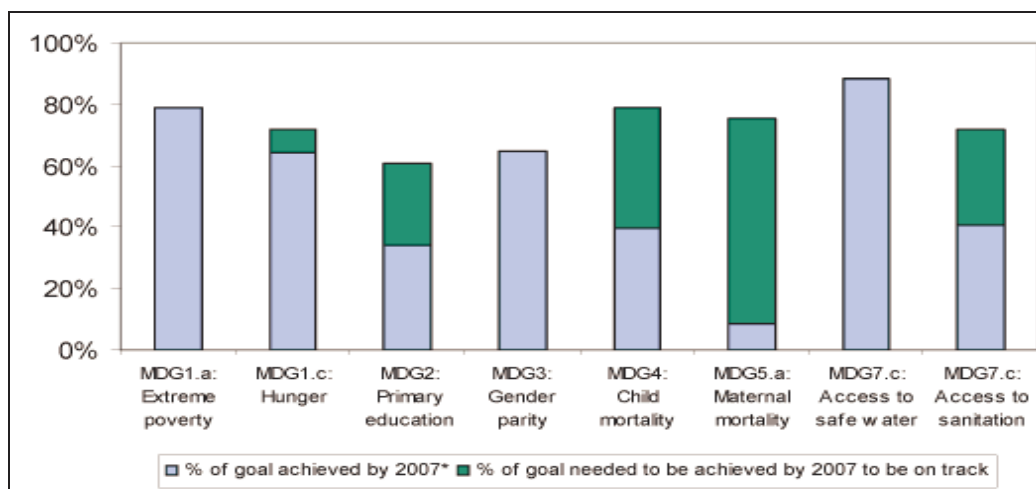
<sup>6</sup> “Unemployment, working poor and vulnerable employment to increase dramatically due to global economic crisis,” *International Labor Organization*, January 28, 2009.

<sup>7</sup> “The Global Economic Crisis: Assessing Vulnerability with a Poverty Lens,” *The World Bank*, February 2009.

<sup>8</sup> In September 2000, at the United Nations General Assembly’s Millennium Summit, world leaders issued the United Nations Millennium Declaration (A/RES/55/2) agreeing to a set of time-bound, measurable goals to fight poverty, hunger, and disease, combat illiteracy, protect the environment and promote gender equality. One hundred eighty-seven nations unanimously agreed to these objectives which became the eight Millennium Development Goals. These goals, which are to be achieved by 2015, are to serve as a framework as nations plan their development assistance programs.

countries may be 200,000 to 400,000 per year higher on average between 2009 and the MDG target year of 2015 than they would have been in the absence of the crisis.<sup>9</sup>

**Figure 5. Progress towards MDGs – All Developing Countries**



Source: World Bank

Despite the current global economic slowdown, estimates suggest that poverty rates are still likely to decline in the long-term. Over the medium-term (3-to-5), economic growth rates may still be higher than they were in the 1990s due to macroeconomic policy improvements and structural reforms such as privatization and regulatory initiatives within developing countries. This depends, however, on how quickly and fully the world can recover from current recessionary economic conditions.

## Impact of the Crisis on the IMF

The severity of the current financial crisis is a challenge for the IMF, whose financial resources have not kept pace with the global economy over the past decade. The IMF reports that its resources would need to grow by 55% to match the levels relative to global output that prevailed during the Asian financial crisis of 1997-1998. The leaders of the G-20 countries agreed in April 2009 that resources available to the IMF needed to be increased three-fold in order to deal with current world financial crisis and the risk that it might become even more serious in the future.

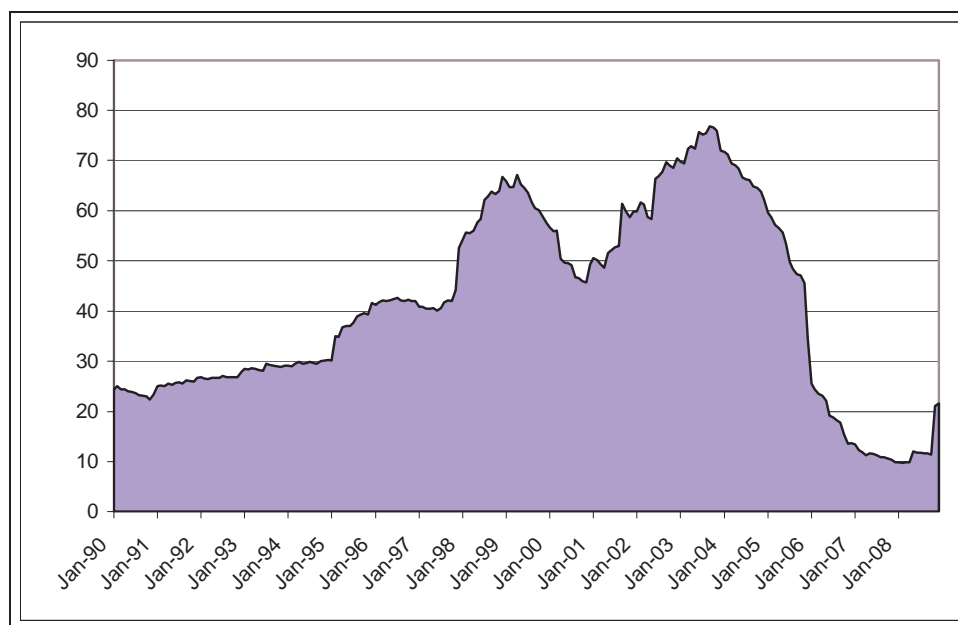
Demand for IMF resources in 2009 has been strong, though, as **Figure 6** indicates, the recent rise in IMF lending was preceded by historic lows in loan demand. On August 31, 2008, total IMF lending was SDR11.65 billion (about \$16.65 billion), down from a peak of SDR76.84 billion (then around \$116 billion) in September 2003.<sup>10</sup> Since the IMF's main source of income is the interest paid for its loans, the decrease in demand for IMF loans resulted in shortfalls in the IMF's

<sup>9</sup> *Swimming Against the Tide: How Developing Countries are Coping with the Global Crisis*, Background Paper prepared by World Bank Staff for the G20 Finance Ministers and Central Bank Governors Meeting, Horsham, United Kingdom on March 13-14, 2009. pg. 11.

<sup>10</sup> Total IMF Credit Outstanding for all members from 1984-2008, available at <http://www.imf.org/external/np/fin/tad/extcred1.aspx>.

administrative budget and a roughly 20% reduction in IMF staff during 2007-2008. The latest annual review of the IMF's income position was prepared in April 2008 and publicly released in July. Fund officials suggest that the projected shortfall for FY2009 is about SDR150 million or \$242 million. According to IMF officials, the Fund's income in FY2009 is likely to be somewhat higher, given the recent surge in lending in response to the global financial crisis. Between October and December 2008, lending almost doubled, from SDR11.3 billion (\$17.1 billion) to SDR21.48 billion (\$32.54 billion).

**Figure 6. Outstanding IMF Lending**  
(1990-2008, billion SDR)



**Source:** International Monetary Fund

The current financial crisis represents a major challenge for the IMF. The United States and other advanced industrial economies are at the center of the crisis, but the IMF would not have enough resources to provide them with significant financial assistance if they sought IMF aid. The IMF's total financial resources as of April 2009 were \$335.4 billion, of which \$228.2 billion were usable resources.<sup>11</sup> This is small compared to amount owed to other creditors by the emerging market countries. At the end of the third quarter of 2008, the latter had borrowed about \$2.75 trillion from the world's banks. Developing countries also had around \$4.5 trillion in foreign exchange reserves. If the G-20 pledges of \$500 billion in new resources are realized, the IMF would once again have the financial resources to credibly lend to developing countries impacted by the crisis.

<sup>11</sup> The IMF resources considered non-usable to fund its operations are (1) its gold holdings, (2) currencies of members that are using IMF resources and are therefore, by definition, in a weak balance of payments or reserve position, (3) the currencies of other members with relatively weak external positions, and (4) other non-liquid IMF assets.

## Increasing Fund Resources

At the 2009 Davos World Economic Forum, John Lipsky, the IMF's First Deputy Managing Director, said that to be able to effectively lend to all the potential countries affected by the crisis, the IMF should double its lending resources to around \$500 billion.<sup>12</sup> Momentum to boost IMF resources increased during the spring as the global economy worsened and many countries sought IMF financial assistance through a variety of the IMF's lending facilities (**Table 1**).

**Table 1. IMF Financial Arrangements as of May 4, 2009**

(in millions of SDR)

Member	Effective Date	Expiration Date	Amount Agreed	Undrawn Balance	Total Credit Outstanding
<b>Stand By Arrangements</b>					
Armenia	03/06/09	07/05/11	368	206	162
Belarus	01/12/09	04/11/10	1,618	1,100	518
Costa Rica	04/11/09	07/10/10	492	492	--
El Salvador	01/16/09	03/31/10	514	514	--
Gabon	05/07/07	05/06/10	77	77	--
Georgia	09/15/08	03/14/10	477	189	288
Guatemala	04/22/09	10/21/10	631	631	--
Hungary	11/06/08	04/05/10	10,538	4,215	6,323
Iceland	11/19/08	11/18/10	1,400	840	560
Latvia	12/23/08	03/22/11	1,522	986	535
Mongolia	04/01/09	10/01/10	153	102	51
Pakistan	11/24/08	10/23/10	5,169	2,533	2,639
Romania	05/04/09	05/03/11	11,400	11,400	--
Serbia	01/16/09	04/14/10	351	351	--
Seychelles	11/14/08	11/13/10	18	11	07
Ukraine	11/15/08	11/04/10	11,000	8,000	3,030
<b>Flexible Credit Line</b>					
Colombia	05/11/09	05/10/10	6,966	6,966	--
Mexico	04/17/09	04/16/10	31,528	31,528	--
Poland	05/06/09	05/05/09	13,690	13,690	--
<b>Exogenous Shocks Facility</b>					
Kyrgyz Rep	12/10/08	06/09/10	67	50	100
Malawi	12/03/08	12/02/09	52	17	81
Senegal	12/19/08	12/18/09	49	24	223

<sup>12</sup> "As Contingency, IMF Aims to Double its Lendable Resources," *IMF Survey Magazine: Policy*, February 2, 2009.

**Source:** IMF Financial Activities – Update April 30, 2009

**Note:** 1 U.S. dollar equals approximately 0.67 SDR

## **Box 2. IMF Lending Facilities**

**The Flexible Credit Line.** In April 2009, the IMF announced the creation of its new Flexible Credit Line (FCL). Countries with good economic track records may borrow – in amounts not subject to the Fund’s normal access limits – for periods of 6 to 12 months. Unlike other IMF loan programs, FCL loans can be disbursed up front rather than over a period of time.. The FCL replaced earlier facilities -- the Short-Term Liquidity Facility (SLF), created in 2008, the Contingent Credit Line (CCL), created in 1999 and closed in 2003, and the Supplemental Reserve Facility (SRF). No countries ever borrowed from the SLF or CCL. Colombia, Mexico, and Poland have borrowed from the new facility. FCL borrowers can borrow on a precautionary basis based on potential balance of payments needs. That is, they can use the loan as a line of credit, to bolster their foreign exchange reserves and improve their financial situation, without any requirement that funds need actually be disbursed. This aims to provide stability and to lessen the chance that incidental events might trigger capital flight or a run on the nation’s economy. Access is normally not to exceed 1000% of quota.

**Stand-By Arrangements (SBA)** are the IMF’s standard loan program and its most commonly used facility. Designed to address short-term BOP problems, these are lines of credit which may be used as needed during a specific period of time (generally 12 to 18 months). Repayment is expected within 3¼ to 5 years after each disbursement is made. SBA loans carry performance conditionality and are disbursed in stages as countries meet specified policy and performance goals. These generally address fiscal, and monetary criteria, though in recent years the IMF has also monitored institutional goals and sought steps to preserve borrower countries’ social safety nets. SBA loans can be approved on a precautionary basis, with funds being drawn only if the country needs them to address deteriorating conditions. In April 2009, the executive board decided that high-access precautionary SBAs (HAPAs) should be available on a more regular basis. It also said the design of SBAs should be more flexible, with respect to phasing, frontloading of access and the frequency of performance reviews, to take into account the borrowers’ varying circumstances.

The **Extended Fund Facility (EFF)** was created in 1975 to help countries address long-term BOP problems which required major restructuring of their economies. These loans are similar to SBAs, but credit is generally kept available for a longer period (3 years) and repayment is expected within 4 ½ to 7 years of disbursement. Surcharges also apply. The executive board decided in April 2009 to retain the EFF because of its importance for low-income countries.

The **Supplemental Reserve Facility (SRF)** was created in 1997 to provide short-term financing (2 to 2½ years) on a large scale. The IMF used this facility to fund the large loans it made to emerging market economies during the international financial crises of the 1990s. SRF loans carried a substantial surcharge of 3- to-5% and were intended to supplement SBA or EFF arrangements. The SRF was abolished in April 2009 when the FCL was established.

The **Compensatory Financing Facility (CFF)** was created in the 1960s to help countries experiencing a sudden loss of export income or a sudden rise in imported cereal prices due to fluctuating world prices. SBA repayment terms apply. The CFF was abolished in April 2009 when the FCL was established.

**Concessional Rate Facilities.** Low income countries may borrow on concessional repayment terms from the **Poverty Reduction and Growth Facility (PRGF)** and the **Exogenous Shocks Facility (ESF)**. To qualify for such loans, countries must be eligible to borrow from the World Bank only through its concessional aid facility, the International Development Association (IDA). Most borrowers have per capita income levels of about \$865 a year. PRGF loans are intended to help low-income countries surmount BOP or financial crises. Unlike SBA and other loans, however, conditionality for PRGF loans is based more on the economic strategies outlined in Poverty Reduction Strategy Papers (PRGF), which are prepared jointly by the borrower country, the IMF and World Bank staff, and civil society groups. The ESF is intended to provide countries with quicker and easier access to assistance to help them cope with economic shocks that have a negative impact on their economy but are beyond their governments’ control. Conditionality is focused on steps needed to adjust to the economic shock, with less attention to the structural adjustment measures more commonly associated with SBA, EFF and PRGF assistance. In 2008, access was made more flexible and the earlier requirement that countries must have PRGF in place was dropped.

**Loan Terms.** The IMF funds its loans from its General Resources Account (GRA), using money paid in quotas or money borrowed through the NAB or other procedures. The amount a country may borrow will depend on the type of loan but is generally a multiple of its quota. Surcharges are applied to loans which represent high multiples of the borrower country’s quota. IMF non-concessional loans carry an interest rate (“rate of charge”) which is based on the

IMF's SDR interest rate. The SDR rate is calculated weekly, for a basket of major currencies, based on a weighted average for short-term government debt in major international money markets. There is a margin (currently 100 basis points) over the SDR interest rate to cover intermediation costs and build reserves. There is also an interest rate premium ("surcharge.") In April 2009, the rate was 2.1%. Loans from the PRGF and ESF carry an interest charge of 0.5% and are repayable over a period of between 5 ½ and 10 years, depending on the borrower's situation. A subsidy account funded by donor countries enables the IMF to charge this reduced rate to PRGF and EFF borrowers.

## Expanding the NAB

At the G-20 meeting in April 2009, the major countries agreed that the resources of the New Arrangements to Borrow (NAB) should be expanded by about \$500 billion. This would not expand the IMF's core resources, but it would triple the funds available to the IMF for use in fighting the current crisis. The G-20 leaders said the expanded NAB would be more flexible than the existing program, but the details are still being worked out and have not yet been released.

The NAB is a facility from which the IMF may borrow supplemental funds to help it respond to financial crises in countries of key significance to the world economy. An 85% majority of the NAB creditor countries must agree before NAB resources can be used for assistance to a specific country, and the IMF must repay the NAB creditors within five years. The NAB was proposed in 1994 and created in 1998 after the Mexican debt crisis raised concerns about the adequacy of IMF resources in the face of a worldwide crisis. An earlier facility, the General Arrangement to Borrow (GAB), was created in 1962 to augment the IMF's resources in case it were needed to backstop the major European currencies after they became freely convertible after the Second World War. The NAB/GAB currently has commitments totaling \$50 billion from 26 countries.<sup>13</sup>

**Table 2. G-20 Commitments to the NAB**  
(in billions of U.S. Dollars)

<b>Country</b>	<b>Amount</b>
Japan	\$100.0
European Union	\$100.0
Switzerland	\$10.0
Norway	\$4.5
South Korea	\$10.0
Canada	\$10.0
China	\$40.0*
U.S.	\$100.0

<sup>13</sup> The NAB are a set of credit arrangements between the IMF and 26 developed country members and institutions. These arrangements have been renewed twice, most recently in November 2007 for a further period of five years from November 2008. The NAB are a supplemental, emergency mechanism. They provide temporary financing for the IMF only when necessary. Thus, they are a non-quota based source of financing for the IMF. The NAB are not, therefore, intended to substitute for a quota or capital increase. The NAB has 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, of which SDR 2.9 billion was used.



<b>Country</b>	<b>Amount</b>
<i>Needed from others to reach \$500 billion target</i>	<i>\$125.5</i>
<i>* Possibly through SDR bond purchases</i>	

**Source:** Deutsche Bank

The G-20 agreed that \$250 billion should be made available immediately through bilateral arrangements between the IMF and individual countries (Japan had just signed an agreement loaning \$100 billion to the IMF and the European Union had pledged to do the same). The also agreed that the NAB would be increased in size by an additional \$250 billion as more countries pledged their participation. At the time of the G-20 meeting, Japan had already lent \$100 billion to the IMF, and members of the European Union had agreed to provide an additional \$100 billion. Subsequently, Canada (\$10 billion), South Korea (\$10 billion), Norway (\$4.5 billion), and Switzerland (\$10 billion) agreed to subscribe additional funds. The Obama Administration has asked Congress to approve a U.S. subscription of \$100 billion to the NAB and expects that major emerging market countries will also agree to lend supplemental funds to the IMF. The sources for the remaining funds have not been announced.

China has agreed, in principle, to contribute another \$40 billion to the IMF to be invested in IMF SDR-denominated bonds.<sup>14</sup> The IMF, however, has not publicly announced a plan to issue SDR-denominated bonds, although it has the legal authority to do so. If these bonds are issued, an additional \$125.5 billion will still need to be pledged by other countries if the \$500 billion goal announced by the G-20 is to be achieved (**Table 2**).

## **SDR Allocation**

In addition to the planned expansion of the NAB, the G-20 leaders agreed that the IMF should create \$250 billion worth of new SDRs and allocate them to its member countries. The First Amendment to the IMF Articles, which went into effect in 1969, authorized the IMF to create a new international reserve asset that could be used to supplement its member countries' foreign exchange reserves. SDRs are distributed to member countries in proportion to their IMF quotas. They are held in the SDR Department of the IMF and are separate from quota resources. The SDR serves as the unit of account of the IMF and some other international organizations. Its value is based on a basket of key international currencies.

The new \$250 billion allocation of SDRs is not an expansion of the IMF's resources but rather is an expansion of the international reserves of all its member countries. Each country will get a portion of the new SDRs based on its ownership share (its quota) in the IMF. This will increase the size of each country's foreign exchange reserves without any requirement that some country must run a deficit in order for another to accrue a surplus.

If a country wishes to exchange some of its allocated SDRs for money, it applies to the IMF and the IMF sells those SDRs to another participating country in order to generate the needed funds. The IMF does not use its own resources to fund these operations. In effect, the IMF's SDR Department is a medium through which countries trade resources among themselves. Technically speaking, there is no borrowing or lending, since the value of each country's assets stays the same

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<sup>14</sup> Daisy Ku, "China to contribute to IMF through SDR bond-sources," *Reuters*, April 8, 2009.



even though the composition of their assets (SDRs or cash) may change. However, countries pay interest to the IMF whenever the number of SDRs they hold is less than the amount originally allocated to them and the IMF pays interest to countries that hold more SDRs than the amount they originally received. Because these are not “loans,” countries are not required to repurchase their SDRs within any specific period of time, but they pay interest on the outstanding balance.

Articles XVII, XVIII, and XIX of the IMF Articles of Agreement set down the rules by which SDRs may be created and exchanged among members for usable currency. If a country wants to encash some of its SDRs, the IMF facilitates the exchange among member countries. In recent years, all transactions in SDRs have been conducted on a voluntary basis. Countries must pay interest if the number of SDRs they possess is less than the amount originally issued to them, and these payments are received by those members that own more SDRs than they were originally allocated. The rate of interest paid and received in connection with use of SDRs is fixed by the IMF – currently a weighted average of short-term dollar, euro, yen, and sterling interest rates.

The \$250 billion allocation of SDRs would greatly expand the volume of SDRs allocated to date (currently worth about \$32 billion). A proposal has been pending since 1997 (commonly referred to as the “Fourth Amendment” to the IMF Articles) that would roughly double the number of SDRs allocated to date. The Obama Administration has asked Congress approve U.S. consent to this amendment. With U.S. approval, the amendment will have received sufficient votes to go into effect. An amendment is required for this allocation of SDRs because it is not a straight pro rata distribution. Rather, countries that did not receive previous allocations because they were not members of the IMF (or participants in the SDR Department) would get a catch-up allocation to remedy that situation.

## **IMF Bond Sales**

Several developing countries with considerable foreign exchange reserve holdings have been approached about contributing to the G-20 pledge to increase IMF resources. Many have expressed their unwillingness to lend money to the institution until broader governance reform at the institution is achieved. While some changes were agreed on at the April 2008 IMF spring meetings (these are discussed in more detail below) that will increase developing country representation, they have been widely characterized as modest. Many developing countries have thus sought a temporary means to provide assistance to the IMF, while delaying a more permanent contribution until more substantial governance reforms give them a larger representation in the institution.<sup>15</sup> At the IMF’s spring 2009 annual meetings, Brazil, China, India, and Russia signaled their interest in purchasing bonds issued by the IMF in SDRs.<sup>16</sup> For countries with large reserves, these bonds could prove an attractive way to diversifying the currency composition of their foreign exchange reserves. (Most foreign exchange reserves are currently held in only a few currencies including U.S. dollars, euros, and Japanese yen.)

Article 7 of the IMF’s Articles of Agreement provides the Fund the authority to borrow from the capital markets. No additional congressional authorization is needed. While the IMF has never issued bonds in its 60-year history, a framework for issuing bonds in the official sector was

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<sup>15</sup> For background, see: CRS Report RL33626, *International Monetary Fund: Reforming Country Representation*, by Martin A. Weiss.

<sup>16</sup> Cai Hong, “Use IMF Bonds to Fight Crisis,” *China Daily*, April 24, 2009.

developed in the early 1980s. While details about the current proposal are still being negotiated, some details have emerged. It is expected that the bonds would be traded only amongst official agencies, and countries would not be allowed to sell the bonds to private firms or individuals on the secondary market.<sup>17</sup> The implication for the United States of the proposal would be mixed. If successful, the proposal could lead to greater international macroeconomic security from which the United States could benefit.

A concern about the bond sales is that if increasing amounts of foreign exchange reserves are transferred out of dollars into IMF bonds, the future demand for U.S. Treasury bills and agency instruments, which are used to finance the country's deficits, might decrease, thus increasing the yield on low-risk assets. This would raise the cost to the United States of future debt placements and possibly accentuate a trend of countries slowly diversifying their reserves out of the dollar. Many analysts have argued that since the Asian financial crisis (and during the current crisis), foreign demand for U.S. Treasury assets (largely from central banks) has played a crucial role in depressing U.S. interest rates. Should demand for U.S. Treasury assets decrease because of asset allocation decisions by foreign central banks, or because foreign governments need to spend more of the reserves domestically and have less to invest, there could be upward pressure on U.S. interest rates. However, the overall demand for U.S. Treasury bonds may also be little affected, if they are held instead by an emerging market country that receives IMF loans rather than by an emerging market country purchasing IMF bonds.

## **Other Pending IMF Reforms**

Several proposals affecting the IMF were already pending at the time of the G-20 meeting on April 2, 2009. These proposals are part of an IMF governance reform package negotiated between 2006 and 2008. The George W. Bush Administration submitted proposed legislation regarding these reforms in November 2008, but it was not taken up by the 110<sup>th</sup> Congress. The reforms included plans for an increase in IMF quotas for selected members and several procedural, policy and financial reforms. Also pending was an amendment to the IMF Articles of Agreement, originally proposed in 1997, that would permit a special allocation of SDRs to IMF member countries as discussed above.

The quota increase involves a targeted realignment in the voting shares of member countries in order to give poor countries and dynamic emerging market countries more say in the organization. The U.S. voting share in the IMF would remain at its present 16.77% and the United States would retain the capacity to block the 85% vote that is required to approve most major initiatives in the Fund. Under this reform of IMF quotas, 54 under-represented countries would see their combined quota share in the Fund increase by about 5% of the total.

Other reforms included in the governance reform package include: (1) a new formula for determining country quotas, giving much more weight to GDP and thus better reflecting countries' weight in the world economy; (2) a tripling of "basic votes" – equally allocated votes – thus giving the poor countries an increased voice in the organization; (3) an additional Alternate Executive Director for the two constituencies of the executive board representing countries in sub-Saharan Africa; and (4) changes in the IMF's investment and financial procedures, including the sale of gold to finance the establishment of an income-generating endowment fund to help

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<sup>17</sup> Eswar Prasad, "Details and Implications of IMF Bonds," May 4, 2009.

pay for the IMF's activities (research, policy and technical assistance, etc.) that are not related to its loan operations.

The proposed Fourth Amendment to the IMF Articles would permit a one-time allocation of about SDR 21.4 billion disproportionately to all IMF member countries in order to make total SDR allocations more equitable. In dollar terms, the allocation would be worth about \$32 billion and would include about \$5 billion in new resources for Eastern Europe. Under the IMF's Articles of Agreement, specifically Article XVIII, each allocation of SDRs is made to members on a pro rata basis according to quota. However, the proposed allocation of resources under the proposed Fourth Amendment is not a straight pro rata distribution. Rather, in this allocation, in which all countries would receive some additional SDRs, countries that joined the Fund after 1981, or between 1972 and 1978, and therefore did not participate in the SDR allocations that took place before those dates (about one-fifth of the total membership), would receive additional SDRs equivalent to the amounts they would have received had they been members before that date. An amendment to the IMF Articles is required to allow this "catch-up" allocation of SDR resources.

## The Role of Congress

### Some Initiatives Would Require Congressional Approval

Some of the provisions discussed above would require congressional assent and some do not. In general, action by Congress is not required before the United States can vote for increases in IMF resources that do not require contributions from the United States, changes in IMF policy, or procedures that implement existing provisions of the IMF Articles. On the other hand, congressional action is required before the United States can vote for amendments to the IMF Articles, for gold sales, or for quota increases that involve contributions by the United States.

**Table 3. Congressional Action Needed on Various IMF Options**

<b>Option</b>	<b>Congressional Action</b>
Ad Hoc Quota Increase for selected countries	None required (even though this may lower the U.S. voting share.)
Quota increase for the United States	Requires congressional authorization (because it changes the amount of quota resources held by the United States) .
Loan to IMF Through NAB	Requires congressional authorization.
Sale of IMF Gold	Requires congressional authorization under most circumstances.
Revise quota formula	No congressional authorization or appropriation required.
Reorganize Executive Board	No authorization or appropriation required under most circumstances. However, if Board reform is done through an amendment of the Articles, congressional authorization is required. This is the case for the current proposed amendment to allow the largest Board constituencies to be represented by two Alternate Executive Directors.
Increase Basic Votes	The proposal requires amending the IMF's Articles of Agreement and thus requires congressional authorization.
4 <sup>th</sup> Amendment	Requires congressional authorization, as it is an amendment to the IMF Articles,. It would

<b>Option</b>	<b>Congressional Action</b>
Allocating SDRs	allocate SDR 21.4 billion, some countries getting more because they did not participate in the earlier allocations.
New Allocation of SDRs	Not required if the total amount of SDRs allocated to the United States is smaller than the current U.S. quota in the fund. U.S. receipts in the new allocation would be smaller than that amount.

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## **Congress and the New Allocations of SDRs**

Two new allocations of SDRs are currently under discussion. Under U.S. law, the smaller allocation requires the assent of Congress before it can go into effect, but no action by Congress is needed before the larger allocation may occur. The Bretton Woods Agreements Act (BWAA) says that Congress must give its assent before the United States may vote for any amendment to the IMF or World Bank Articles of Agreement.<sup>18</sup> The smaller (SDR 21.4 billion) allocation would be accomplished through adoption of the Fourth Amendment to the IMF Articles. As noted before, this allocation provides countries that did not participate in the earlier allocations of SDRs with a catch-up distribution equivalent to the amount they would have received if they had been members when the previous allocations were made. Because of this catch-up provision, the allocation must be done through an amendment rather than through the regular SDR allocation process. Because it is an amendment to the IMF Articles of Agreement, Congress would be required to give its assent before the United States may vote for the plan.

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<sup>18</sup> The Bretton Woods Agreements Act, P.L. 79-171 (22. U.S.C. 286, et seq.), is the key act governing procedures for U.S. participation in the IMF and World Bank. Sec.5 says that that no one may vote on behalf of the United States for an increase in the U.S. quota in the IMF or an amendment to the IMF Articles unless Congress authorizes that action.

### **Box 3. U.S. Participation in the IMF**

As the largest single contributor (\$50.4 billion cumulatively) to the IMF, the United States has a leading role in shaping the IMF's lending, surveillance, and advisory operations. Both House and Senate committees frequently hold hearings on IMF activities in developing countries and on IMF reform. Other countries are also concerned that steps should be taken to make the IMF more effective.

The President has the ultimate authority under U.S. law to direct U.S. policy and instruct the U.S. representatives at the IMF, and the multilateral development banks (MDBs). The President, in turn, has generally delegated authority to the Secretary of the Treasury. The Treasury's Under Secretary for International Affairs and his staff manage day-to-day U.S. participation. With the advice and consent of the Senate, the President names individuals to represent the United States on the executive boards of the IMF and MDBs. The Executive Boards have authority over operations and policy and must approve any loan or policy decision.

The Secretary of the Treasury serves as the U.S. representative on the World Bank Board of Governors, where each country has its own representative. The Board of Governors is the highest level decision making body of the World Bank. In both the World Bank Executive Board and Board of Governors countries have voting shares comparable to their financial contributions. At the World Bank, the United States has a 16.84% vote in the principal loan window.

Congress must give its consent by law before the United States may agree to participate in any new funding agreements. The Senate has advise and consent authority over all persons nominated to represent the United States at the IMF and the multilateral development banks. On many occasions, Congress has enacted legislation specifying what U.S. policy shall be in the international financial institutions (IFIs) and how the U.S. executive directors at these institutions shall vote and the objectives they shall pursue. Congress has also frequently made specific suggestions to the Administration through Sense of Congress resolutions or language in committee reports accompanying legislation suggesting specific goals and priorities the United States ought to emphasize in the IFIs. Since the World Bank and the other multilateral institutions are not agencies of the U.S. government, but rather international institutions, their activities and policies are not subject to U.S. law.

By contrast, the proposed \$250 billion allocation of new SDRs would be accomplished through the procedure set forth in Article XVIII of the IMF Articles of Agreement. This says that, upon an 85% majority of the IMF membership, the SDR Department of the Fund may create new SDRs and allocate them to member countries in proportion to their IMF quotas in the institution. The SDR mechanism at the IMF was created in 1969, following adoption of the First Amendment to the Articles. In the Special Drawing Rights Act of 1968, Congress gave the Administration authority to vote for the First Amendment, and it set forth the guidelines for U.S. participation in the SDR Department.<sup>19</sup> Section 6 of the Act says that, before the United States can vote for any allocation of SDRs that would be equal to or greater than the existing U.S. quota in the Fund, Congress must give its consent. However, the Act also says that, if the U.S. share of a new allocation of SDRs is less than the size of the U.S. quota, the United States can support it as long as the Treasury Department consults with leaders of the House and Senate authorizing committees at least 90 days in prior to the vote. The 90-day period began on April 13, 2009, when a Treasury official notified Congress that the United States planned to vote in favor of the proposed new allocation of SDRs.

The IMF's total quota resources amount to about SDR 217 billion and the U.S. quota is equal to about SDR 37.15 billion. The \$250 billion allocation is equivalent to about SDR 168 billion and the U.S. share would be worth about SDR 28 billion. On May 1, 2009, the U.S. dollar was worth

<sup>19</sup> P.L. 90-349, 22 U.S.C. § 286o. Any SDRs allocated by the IMF or otherwise acquired by the United States are resources of the Exchange Stabilization Fund. For background on the ESF, see: CRS Report RL30125, *The Exchange Stabilization Fund of the U.S. Treasury Department: Purpose, History, and Legislative Activity*, by Arlene E. Wilson, *The Exchange Stabilization Fund of the U.S. Treasury Department*, by Arlene Wilson.

about SDR 0.67. If the dollar goes up in value compared to the euro, UK pound or Japanese yen, the dollar's value vis-à-vis the SDR would increase. Therefore, a \$250 billion allocation of SDRs allows some scope for the dollar to appreciate relative to the other currencies in the SDR basket without triggering the requirement for congressional action.

## **Gold Sales**

It also expected that President Obama will request congressional authorization for the Administration to vote in favor of selling 403 metric tons of IMF gold for the purpose of increasing the Fund's liquid reserves. Income earned on these reserves, in turn, would finance a portion of the IMF budget related to its provision of global public goods, such as economic and financial surveillance. The gold sales to benefit poor countries, announced by the G-20 leaders, would be included in this agreed total, as it is expected that the currently high price of gold may provide some additional income beyond what is expected for budget financing. However, any additional income would likely be modest since the current price of gold (around \$925 an ounce on May 14, 2008) is not significantly difference from the assumption on which the new income model was based (\$850 per ounce). The IMF Articles of Agreement specify that any sale of IMF gold must receive an 85% affirmative vote by the member countries.

In the late 1990s, limited gold-sales were proposed to finance the IMF's initial contribution to the Heavily Indebted Poor Countries (HIPC) initiative. Due to the concerns raised above, 13 million ounces of gold were sold in off-market transactions with two members, Brazil and Mexico, that had financial obligations to the IMF. Gold was sold at the market price, and profits were placed in a special IMF HIPC account. At the same time, the IMF accepted back the gold sold to Brazil and Mexico in settlement of their financial obligations to the Fund. The result was that the balance of the IMF's holdings of physical gold remained unchanged, although its usable resources shrank relative to what they otherwise would have been if the Fund had received currencies in settlement of these financial obligations.<sup>20</sup> The transaction was structured in this way because, in the past, proposals to sell IMF gold reserves have been unpopular among some Members of Congress. Some have argued that there is a potential lack of IMF transparency. Some claim that the gold held by the IMF belongs to the member nations and that it is not the IMF's place to propose gold sales to fund current operating expenses. Some also argue that gold sales have the potential to weaken the global price of gold, and the effect on the IMF balance sheet is unclear. The sale contemplated now, however, would only include gold acquired by the Fund after the Second Amendment to the IMF Articles of Agreement, which occurred in 1978, after which members no longer paid quota contributions in gold. Therefore, the gold sold is in no way attributable to member countries.

Under Article V, Sec. 12 of the IMF's Articles of Agreement, approval of gold sales by the IMF requires an 85% IMF voting majority. The United States has almost a 16.77% vote and could thus block any sale of IMF gold. Understanding this "virtual" veto, Congress, in 1999, enacted legislation in the FY 2000 Consolidated Appropriations Act that authorized the United States to vote at the IMF in favor of a limited sale of IMF gold to fund the IMF's participation in HIPC debt cancellation. However, the act, amending section 5 of the Bretton Woods Agreements Act

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<sup>20</sup> The IMF may hold gold as an asset, but it cannot lend gold nor can it use gold as security for borrowing funds. The transactions in 1999 shifted money out of the IMF's general resources account into a special fund for HIPC debt cancellation. To offset this deduction, the IMF revalued some of its gold by an equal amount. See Jonathan E. Sanford, "IMF Gold and the World Bank's Unfunded HIPC Mandate," *Development Policy Review*, January 2004.



(22 U.S.C. 286c), requires the explicit consent of Congress before the executive branch can support future gold sales. However, the law provides that the United States may support the sale of IMF gold without congressional action if the Secretary of the Treasury certifies to Congress that the sale of gold is necessary for the Fund to reconstitute gold to its members, or to provide liquidity that will enable the Fund to meet member countries' claims on it or to meet threats to the systemic stability of the international financial system.<sup>21</sup>

## **Budgetary Treatment of IMF Contributions**

On May 12, the White House and Congress reached an agreement to treat the U.S. subscription to the IMF as a line of credit for budgetary purposes. Reminiscent of the method used for the 1966 quota increase, Congress has been asked by the Administration to authorize the United States to extend a line of credit to the IMF for the NAB and quota subscriptions that total \$108 billion. Unlike IMF quota increases since 1967, that were treated as an exchange of assets with no budgetary impact, under the new agreed framework, the U.S. contribution would be scored for budgetary purposes under the existing credit reform legislation. This legislation says that Congress need not appropriate the full face value but only the expected amount of loss for any loans made by the United States Government. When U.S. contributions to the IMF were treated as an exchange, there was considered to be no risk of default by the IMF in its obligations to the United States. Under credit reform, a small fraction of the total would be appropriated to cover possible losses. Reportedly, CBO has determined that the U.S. contributions to the IMF would require \$5 billion to be appropriated.<sup>22</sup> This re-calculation of the cost is expected by many to ease the prospects for enacting this legislation.

Prior to the May 12<sup>th</sup> agreement, Congress had appropriated budget authority to facilitate U.S. subscriptions to the IMF, but the actual payments were treated as an exchange of assets with the IMF. Thus, from a U.S. budgetary perspective, there were no net outlays and no net impact on the U.S. budget. In the past 60 years, Congress has handled the bookkeeping aspects for U.S. participation in the IMF in a variety of ways. This system was the result of a compromise among the leading figures on the relevant congressional committees in 1980.

Payments to the IMF were considered to be an exchange of assets because the United States receives back from the IMF a monetary instrument of equal value which it adds to its foreign exchange reserves. The United States receives an increased holding of SDRs in the Fund's SDR Department whenever it purchases SDRs from another country, and an increased reserve tranche position whenever the IMF draws on the U.S. quota to finance loans to borrower countries. Both the SDR and reserve tranche positions are liquid interest bearing assets. SDRs cannot be used to make purchases in the marketplace, but they can be exchanged with other IMF members for currencies or used to satisfy international obligations which in most cases involve the Fund. In the case of loans through the NAB, the United States receives a promissory note from the IMF pledging to repay the loan with interest at a certain time. Credits provided to the IMF through the NAB are considered to be monetary assets and are included in countries' foreign exchange reserves. The proceeds are considered to be readily available because NAB participants can obtain immediate early repayment from the IMF if they have a balance of payments need.

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<sup>21</sup> P.L. 106-113, Consolidated Appropriations Act, 2000, Sec. 504(d).

<sup>22</sup> "Obama IMF Aid Request goes into Senate Bill," *Reuters*, May 13, 2009.



In 2009, there was concern that the procedural aspects of the budget process may have an impact on congressional consideration of the proposed new U.S. subscriptions to the IMF. Some are concerned that Members of Congress may vote against providing budget authority for the proposed \$100 billion line of credit to the IMF through the NAB on account of “bailout fatigue,” even though the payment would have no outlay effect under then-existing congressional budget scorekeeping procedures.

Peter Orszag, director of the Office of Management and Budget (OMB), was quoted in April 2009 as saying that he cannot see “any analytical rationale for why something would score zero as an outlay but then score as something in budget authority.” He reportedly urged the Congressional Budget Office (CBO) and the House and Senate Budget Committees to use an alternative “exchange of assets” procedure (like that use for IMF payments in 1976 and 1977) in which no appropriations would be required to put the \$100 billion line of credit through the NAB and U.S. participation in the IMF quota increase into effect.<sup>23</sup> Others have been concerned, though, that changing the existing budgetary procedure for IMF subscriptions at the present moment might weaken their support because it might be seen as an effort to change the rules in the face of controversy or a signal that the Administration fears that it may not have the votes to approve the measure through the established process. By contrast, critics of the current scorekeeping system say that it would be unfortunate if bookkeeping procedures hindered Congress from considering the IMF proposals on their merits.

The Treasury Department is required by law to report to Congress quarterly the financial cost of U.S. participation in the IMF. The most recent report, current through 2007, was submitted in April 2009.<sup>24</sup> The Department reports that, in 2007, the United States earned a net \$68 million from its participation in the SDR Department, and it earned a net \$362 million from its transactions with the IMF General Department (which deals with quota accounts.)

The United States has used various methods over the years to account for the cost of its participation in the IMF. Before 1967, the United States funded its participation in the IMF through a variety of procedures, including public debt transactions and payments from the Exchange Stabilization Fund. In the 1966 quota increase, the U.S. payment took the form of a letter of credit to the IMF which, for technical reasons, the United States mostly borrowed back during the following years.

In 1967, the U.S. Government adopted a unified Federal budget that consolidated the operating budget of the government with other previously off-budget accounts. This was intended to improve clarity and to enhance the government’s management of fiscal policy. In the process, the President’s Commission on Budget Concepts (PCBC) also examined the procedures by which the United States managed its payments to the IMF. It recommended that payments to the IMF should be treated as monetary exchanges akin to bank withdrawals and deposits rather than as international lending operations. As such, these payments would be handled as an exchange of assets and would be excluded from budget receipts and expenditures. Congress would be asked to authorize new U.S. payments to the IMF, but the cost of those payments would not be included in the Federal budget.

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<sup>23</sup> David Rogers. “How to spend without ‘spending.’” *Politico*, April 22, 2009, p. 1.

<sup>24</sup> [Department of the Treasury.] *Report to Congress on Financial Implications of U.S. Participation in the International Monetary Fund*. Available at <http://www.ustreas.gov/press/releases/reports/imfreportq1q42007.pdf>

The new budget concept was not fully implemented when the next quota increase was considered by Congress. In addition to legislation authorizing U.S. participation, the Nixon Administration sought and Congress approved appropriations to effect U.S. participation in the plan. They agreed, however, that the exchange of assets concept was sufficient to cover the resulting payments, and they would have no net outlay impact on the U.S. budget.<sup>25</sup> In 1976, when the following quota increase was considered, the Ford Administration proposed and Congress agreed that the transaction would be treated solely as an exchange of assets. Legislation was enacted authorizing U.S. participation in the plan, but no appropriations were required. The same procedure was used the following year to approve a loan by the United States to the IMF's Supplemental Financing Facility ("Witteveen Facility").<sup>26</sup> CBO found, in a study of the budgetary scorekeeping issue in 1978, that any procedure – appropriated, exchanged, on-budget, off-budget – is intrinsically arbitrary and not consistent with similar or comparable programs that are treated differently from a scorekeeping perspective elsewhere in the U.S. budget process.<sup>27</sup>

Many Members of Congress, reportedly, were not happy with this arrangement. Some argued, citing the provision of the U.S. Constitution which says that no money shall be drawn from the Treasury except through an appropriation by law, that the funding for U.S. participation in the IMF must be appropriated. Some also said that treating the U.S. payments to the IMF as an off-budget transaction was inconsistent with the principle of budgetary unity which underlay the work of the Presidential budget commission in 1967 and a violation of the prohibition against "backdoor spending" in the Congressional Budget Act of 1974.

The issue came to a head in 1980 during congressional consideration of legislation to approve U.S. participation in a new quota increase for the IMF. A compromise was ultimately agreed to. Under this arrangement, the full amount of the U.S. subscription to the IMF would be appropriated as budget authority.<sup>28</sup> This gave Congress control over the size of the U.S. payments and the amount of contingent liability the United States undertook through its participation in the IMF. However, consistent with the exchange of assets concept, no outlays would be counted and the payments to the IMF would be deemed to have no net impact on the U.S. budget. This procedure remains in effect to this day.

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<sup>25</sup> P.L. 91-599 and P.L. 91-619, enacted in December 1970, added Sec. 22 to the BWAA and appropriated necessary funds. The Administration had requested that funds for the quota increase be both authorized and appropriated. U.S. Bureau of the Budget. *The Budget of the United States Government, Fiscal Year 1971*, Appendix, p. 105.

<sup>26</sup> P.L. 94-564, enacted in October 1976, added Sec. 25 to the BWAA, saying that "the U.S. Governor of the Bank (*sic*) is authorized to consent to an increase in the quota of the United States in the Fund equivalent to 1,705 million Special Drawing Rights." The next year, P.L. 95-435, enacted in October 1977, added Sec. 28 to the BWAA, saying that "The Secretary of the Treasury is authorized to make resources available as provided in decision 5509-(77/127) of the Fund, in amounts not to exceed the equivalent of 1,450 million Special Drawing Rights." In neither case were appropriations required. See also Treasury Secretary William E. Simon's paper, "The Exchange of Assets Concept," reprinted in U.S. Congress. Committee on Banking, Currency and Housing. Subcommittee on International Trade, Investment and Monetary Policy. *Hearings on H.R. 13955, June 1 and 3, 1976*. USGPO, 1976, p. 31.

<sup>27</sup> Congressional Budget Office. *U.S. Participation in the Witteveen Facility: The Need for a New Source of International Finance*. March 1978. This paper is available at <http://www.cbo.gov/ftpdocs/67xx/doc6727/78-CBO-027.pdf>.

<sup>28</sup> P.L. 96-389, enacted in October 1980, added Sec. 32 to the BWAA. This says the Secretary of the Treasury "is authorized to consent to an increase in the quota of the United States in the Fund equivalent to 4,202.5 million Special Drawing Rights, limited to such amounts as are appropriated in advance in appropriation Acts." Congress substituted the latter language for the original text, which approved participation in the quota increase "to such extent or in such amounts [as] are provided in appropriation Acts." The latter language would have required action by the appropriations committees but would not have required formal appropriations to effect the U.S. increase in the IMF.

Congress has taken a different approach in its budgetary treatment of the contingent liability associated with U.S. participation in the multilateral development banks (MDBs). The MDBs fund their market-rate loan programs with money borrowed in commercial markets. Because they are backed by substantial reserves and by the callable capital subscriptions of their member countries, the banks can sell their bonds and notes at favorable interest rates, and they pass these relatively low rates on to their borrower countries. MDB member countries subscribe some of their purchases of capital stock in callable capital and some (a fixed ratio, now a very small percent of the cost for each share) in paid-in capital. Callable capital is a type of full faith and credit guarantee to the banks' bondholders from their member countries. Most analysts believe that it is very unlikely that one of the MDBs would go bankrupt, exhausting all its resources, and needing to call on the callable capital of its members in order to satisfy its creditors.

Before 1982, Congress appropriated the full amount necessary for the callable portion of U.S. subscriptions to capital stock in the multilateral development banks (MDB). About \$12 billion for callable capital had been appropriated by that time, roughly \$8 billion for the World Bank and \$4 billion for the regional development banks. No outlays were associated with this budget authority and it had no impact on the budget or the budget deficit. During the 1970s, however, cuts were adopted reducing the appropriations for MDB callable capital. The proponents of these cuts often claimed that they were saving the taxpayers and reducing the budget deficit by hundreds of millions of dollars. The cuts in callable capital were not program oriented, since the full paid-in portion of the subscriptions for MDB capital stock was generally appropriated. The resulting mismatch in appropriations had a negative effect on U.S. participation in the banks.

Consequently, in 1981, Congress decided that funds would no longer need to be appropriated for new U.S. subscriptions to callable capital. Instead, as is now the current arrangement, the size of the annual U.S. subscription is regulated through program limitations in appropriations acts.<sup>29</sup> No formal appropriations are required, though appropriations would be required if there ever were to be a call on callable capital. In the case of the IMF, neither the Balanced Budget Act of 1977 nor Sec. 17 of the BWAA require that budget authority must be appropriated to facilitate future increases in the U.S. quota in the IMF or future loans to the IMF through the NAB. The law is silent as to the budgetary procedures that Congress should use on such occasions.

The procedures are different for the IMF and the multilateral banks, but the budgeting issue in both situations is essentially the same. Should the outlay effect of the U.S. commitment to these institutions be counted as zero or is there a likelihood that the IMF will not pay the United States back or a possibility that a call might be made on callable capital? Congress has used a variety of mechanisms to effect the U.S. payments to international financial institutions – in some cases appropriating the full amount in budget authority, in other cases setting a program limitation on new liability, and in other cases treating the entire transaction as an off-budget exchange of assets. None of these arrangements seems to be superior to the others, either in terms of maintaining congressional control or in reflecting or controlling the liabilities that the United States faces through its participation in international financial programs.

In 2004, CBO Director Douglas Holtz-Eakin told the Senate Banking Committee that, “The current budgetary treatment does not fully reflect the U.S. share of the credit risk associated with

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<sup>29</sup> P.L. 97-35, enacted August 1981, adding Sec. 39 to the Bretton Woods Agreement Act. This authorized U.S. participation in a new capital increase for the World Bank, providing that ‘any subscription to such additional shares shall be effective only to such extent or in such amounts as are provided in advance in appropriations acts.’ This is the same language Congress had chosen not to enact the previous year in connection with U.S. payments to the IMF.

the lending and other transactions of the international financial institutions.” He had no recommendations for change, however. He said that CBO hoped to discuss these issues further in a future paper.<sup>30</sup> For various reasons, that study was never completed and no paper was released. It may be difficult, in the present moment, for Congress to determine what the “right” budgeting procedure might be in this situation. Over the longer term, however, Congress may want to consider whether an analysis of these budgetary issues might be desirable and whether some changes in the scorekeeping system for international financial institutions might be appropriate.

## Author Contact Information

Jonathan E. Sanford  
Specialist in International Trade and Finance  
jsanford@crs.loc.gov, 7-7682

Martin A. Weiss  
Specialist in International Trade and Finance  
mweiss@crs.loc.gov, 7-5407

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<sup>30</sup> Statement of Douglas Holtz-Eakin, Director. Congressional Budget Office. *The Costs and Budgetary Treatment of Multilateral Financial Institutions' Activity*. Testimony before the Senate Committee on Banking, Housing and Urban Affairs, May 19, 2004. A copy of this testimony is available at <http://www.cbo.gov/ftpdocs/54xx/doc5458/05-19-MFIs.pdf>. CBO's last scored IMF legislation in 1998 when it considered H.R. 3114, the International Monetary Fund Reform and Authorization Act of 1998, a bill that was reported by committee but not considered by the House. A copy of the CBO cost estimate is available <http://www.cbo.gov/ftpdocs/3xx/doc385/H.R.3114.pdf>.