

September 1999

INTERNATIONAL MONETARY FUND

Observations on the IMF's Financial Operations



G A O

Accountability * Integrity * Reliability

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Abbreviations

BIS	Bank for International Settlements
BSFF	Buffer Stock Financing Facility
CCFF	Compensatory and Contingency Financing Facility
CFF	Compensatory Financing Facility
DRC	Democratic Republic of Congo
EAR	Enlarged Access to Resources Facility
EFF	Extended Fund Facility
ERM	Exchange Rate Mechanism
ESAF	Enhanced Structural Adjustment Facility
GAB	General Arrangements to Borrow
G-7	Group of 7 Industrialized Countries
G-10	Group of 11 Industrialized Countries
GRA	General Resources Account
HIPC	Heavily Indebted Poor Countries
IMF	International Monetary Fund
NAB	New Arrangements to Borrow
SAF	Structural Adjustment Facility
SAMA	Saudi Arabia Monetary Agency
SCA	Special Contingent Account
SDA	Special Disbursement Account
SDR	Special Drawing Rights
SFF	Supplemental Financing Facility
SRF	Supplemental Reserve Facility
STF	Systemic Transformation Facility



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The International Monetary Fund was established to promote international monetary cooperation, facilitate international trade by promoting exchange stability and orderly exchange arrangements and assist in eliminating foreign exchange restrictions. To facilitate congressional oversight of U.S. policy concerning the Fund, the Omnibus Appropriations Act for fiscal year 1999 required us to report on several matters,¹ including the financial operations of the Fund during its current financial year ending April 30, 1999, and historical information on its lending activities. This report describes (1) the International Monetary Fund's liquidity position as of April 30, 1999, including its experience with borrowed resources to meet its members' financing needs; (2) the role of gold holdings in the Fund's operations; and (3) the Fund's process for determining the amount of quota contributions required from its members. The report also includes information on how the International Monetary Fund's lending² activities have evolved since it was founded in 1945 and discusses the status of preparedness of the Fund's mission-critical and other key computer systems and member country status for the year 2000.

¹The Omnibus Appropriations Act for fiscal year 1999 (Pub. L. 105-277, Oct. 21, 1998) appropriated about \$18 billion for the International Monetary Fund and required us to report on a seven-point mandate for reviews of the Fund. We are addressing this mandate in three reports—this report on financial operations and lending activities; a second that addressed the terms and conditions for borrower countries, *International Monetary Fund: Approach Used to Establish and Monitor Conditions for Financial Assistance* (GAO/GGD/NSIAD-99-168, June 22, 1999); and a third that addressed borrower countries' trade policies, *International Monetary Fund: Trade Policies of IMF Borrowers* (GAO/NSIAD/GGD-99-174, June 22, 1999).

²With the exception of some financing for low-income countries, the International Monetary Fund does not loan funds to a country. Rather, the country “purchases” the currency it needs from the Fund with an equivalent amount of its own currency and then later “repurchases” its own currency on terms established by the Fund. For the purposes of this report, we use the terms “financial arrangement,” “disbursement,” and “loan” to refer to “purchases” and “repayments” to refer to “repurchases.”

Much of the information reported is as of April 30, 1999, and to the extent possible, we used data audited³ by the Fund's External Audit Committee. To satisfy our objectives, we reviewed and analyzed the International Monetary Fund's financial statements, operational budgets, liquidity reviews, policy documents, and staff position papers and met with Fund, U.S. Treasury, and other officials. We also reviewed information on the status of the Fund's efforts to ensure that its mission-critical systems are Year 2000 compliant. The scope of our work was focused on a review of the International Monetary Fund's General Resources Account⁴ and did not include a review of the trust accounts for low-income members. Although historical data was not available for calculating the weighted average of interest rates on the Fund's lending portfolio for each year since its first loan in 1947, as the Omnibus Appropriations Act requested, we have provided information on the interest rates charged by the Fund over its history. An evaluation of Fund's efforts and related management structure and processes to address the Year 2000 problem was not within the scope of our work.⁵ See appendix VI for a full description of our objectives, scope, and methodology.

³The financial statements are audited annually. For the financial year ended April 30, 1999, the Fund's External Audit Committee issued on June 24, 1999, an audit opinion that was equivalent to an "unqualified" or "clean" audit opinion. The audit report was released on September 12, 1999.

⁴The General Resources Account is used for most transactions between member countries and the International Monetary Fund. These transactions include the receipt of quota subscriptions, purchases and repurchases, and the repayment of principal to the Fund's lenders. The assets held in this account include members' currencies, the Fund's own holdings of Special Drawing Rights and gold.

⁵The Year 2000 problem is rooted in the way dates are recorded and computed in automated information systems. For the past several decades, systems have used two digits to represent the year, such as "99" representing 1999, to conserve electronic data storage and reduce costs. With this two-digit format, however, the year 2000 is indistinguishable from 1900 or 2001 from 1901, etc. As a result, system or application programs that use dates to perform calculations, comparison, or sorting may generate incorrect results or not function at all.

Results in Brief

The International Monetary Fund's financial operations are supported by quota contributions of its members, Special Drawings Rights,⁶ and gold holdings. To supplement these resources, the Fund has access to credit lines with certain member countries, and it can borrow from sovereign governments, central banks, or private entities. The Fund uses its resources to lend to its members and to meet their requests for drawings on their reserve tranche positions.⁷ The International Monetary Fund has never borrowed from private sources and the use of its gold holdings in its financial transactions ended when the Fund amended its Articles of Agreement in 1978. Its financial condition is derived from the various components of its financial operations, including its liquid and nonliquid resources, its resources available from borrowing, and its lending practices.

For the financial year ended April 30, 1999, the International Monetary Fund had about \$287 billion in resources consisting primarily of currency holdings of members' national currencies, Special Drawing Rights, and gold holdings in the General Resources Account. These resources were primarily obtained from members' quota contributions. Of this amount, about \$195 billion was considered usable, that is, was from members that were sufficiently strong economically to permit their currencies to be used

⁶The SDR is a reserve asset that IMF has used since 1969. Its value comprises a weighted average of the values of four currencies: the U.S. dollar, yen, euros, and pound sterling. Because the value of the SDR relative to these currencies changes daily, the U.S. dollar value of amounts converted from SDR also changes daily. The SDR is the unit of account for the Fund.

⁷Up to 25 percent of members' quota contributions must normally be paid in reserve assets, which are currencies that are freely usable in the principal foreign exchange markets (U.S. dollars, yen, euros, and pound sterling) or the Special Drawing Rights. The balance may be paid either in a country's national currency or with noninterest-bearing promissory notes. The portion paid in freely usable currency, or Special Drawing Rights, is referred to as the member's reserve asset or initial reserve tranche position. This portion can be drawn by the member as needed based upon a representation of a balance-of-payments need.

for Fund operations. The remaining \$92 billion was considered unusable.⁸ Of the \$195 billion of usable resources, about \$118 billion had been lent, committed, or reserved as working balances, leaving about \$77 billion in liquid resources available for additional credit to International Monetary Fund members and to meet members' drawings on their reserve assets held by the Fund. The \$77 billion in liquid resources gives the Fund a liquidity⁹ ratio of nearly 89 percent compared to the Fund's historical low liquidity ratio, which has ranged between 25 percent to 30 percent. Fund officials told us that its financial condition is adequate to meet the projected needs of its members until the next scheduled quota review in 2002.

The International Monetary Fund has not drawn from its working balance reserve in over 20 years, as of April 30, 1999. Consequently, its resources available for lending, as of April 30, 1999, may be greater than reported. In addition, the Fund has established a liquidity ratio between 25 percent to 30 percent as a threshold below which it believes it would be imprudent to lend.¹⁰ While a low-end liquidity threshold appears reasonable, we found no analytical basis for the minimum ratio used by the Fund. If the Fund's liquidity were to fall to a level considered too low, the Fund could under specified conditions supplement its resources by using its \$46 billion in credit lines or by borrowing from sovereign governments, their central banks, or private entities.

With the end of the gold standard in the early 1970s and the passage of the second amendment to the International Monetary Fund's Articles of Agreement in April 1978, gold's formal role in the Fund and in international currency transactions was eliminated. The Fund's gold holdings as of

⁸The International Monetary Fund considers certain currencies and its gold holdings as unusable because they cannot be used to finance Fund transactions. Because the Fund holds substantial amounts of currencies of members that are indebted to the Fund and are experiencing balance-of-payments difficulties, and of other members whose financial positions are not strong, a considerable proportion of the Fund's national currency holdings is not considered usable. Quarterly, the Fund reassesses the financial strength and reserve positions of the members on the operational budget to determine if the members' currencies remain strong enough to be used or if other currencies have strengthened sufficiently to be included in Fund transactions.

⁹The Fund's liquidity ratio is determined by dividing its available and uncommitted liquid resources by its liquid liabilities, which consist of members' reserve tranche positions and any outstanding Fund borrowings.

¹⁰The underpinnings for the Fund's liquidity threshold derives from its unique nature among the international financial institutions.

April 30, 1999, had a market value of \$30 billion. The Fund believes that its gold holdings add to the “fundamental strength” of its financial condition. In addition, the Fund views its gold holdings as being available to (1) meet creditors' claims on the Fund in the event of liquidation of the Fund, (2) replenish currency holdings if the Fund does not have sufficient liquid resources to meet members' drawings on their reserve tranche positions, and (3) use during contingencies and for its general operations. The International Monetary Fund continues to consider gold an important resource despite restrictions under the Articles of Agreement, which the Fund interprets as including the lack of authority to invest or manage its gold in order to earn an investment return. Moreover, although the Fund considers gold to be an important resource, there is a decreased willingness of some official institutions to hold gold. In 1995, the Fund examined the effect of selling its gold and investing the proceeds in interest-bearing financial instruments compared to the decision to hold its stock of gold. The decision to hold gold has resulted in tens of billions of dollars in forgone realized gains and investment income since 1980.

The International Monetary Fund has never formally adopted a method for determining members' initial quotas and subsequent quota increases because it believes that quantitative measures cannot fully reflect the considerations that appropriately bear on each member's position or on the total size of the Fund's resources. Thus, the Executive Board uses several factors, including the prospective demand for Fund resources, growth of world trade, and trends in the Fund's liquidity position, to decide on members' quota levels. Its decisions on quota increases are matters of judgment that involve quantitative, qualitative, and political considerations. Historically, quota increases have almost always been lower than the increase recommended by the Fund's staff. For example, Fund staff recommended a quota increase of 100 percent for the most recent review, but the Executive Board¹¹ approved an increase of only 45 percent, after considering various factors, including whether member governments would support such a large increase.

As part of its role in the international monetary system, the International Monetary Fund provides balance-of-payments assistance to members when needed. Since its establishment in 1945, the arrangements under which

¹¹The Fund's Board of Governors votes on the recommendation made by the Executive Board for the quota increase. The recommendation is approved upon an 85-percent weighted majority of the voting power.

such assistance has been provided have evolved in response to changing world conditions and the needs of its member countries. This included a growth in the assistance provided, an expansion of the types of lending

facilities¹² used, and the addition of facilities with longer repayment periods. These changes came about to meet the needs of its members as the composition of the countries needing assistance moved from a mix of industrialized and developing countries to developing countries only. Since the late 1970s, there has been an increase in arrears, and the Fund has taken various measures that have reduced the number of countries in arrears to five as of April 30, 1999. In addition, there has been a greater concentration of the Fund's resources provided to a smaller number of countries since the late 1970s. As of April 30, 1999, about 86 percent of its outstanding loan portfolio had been provided to 10 countries.¹³ The Fund has increased its reserves for potential loan losses and adopted a program to share the cost of overdue obligations between debtor and creditor members.

The Year 2000 problem affects nearly every aspect of the international financial system—from the ability of internal systems that support International Monetary Fund operations to function properly to the ability of member nations to repay loans. While the Fund recognizes the importance of these actions and has taken steps to mitigate potential damage, it still faces some challenges in providing more complete assurance that its internal business processes will continue to function after the date change. Further, the Fund needs to complete its assessment of the impact of Year 2000 failures on the potential for increased demand for financing by its members.

Background

The International Monetary Fund (IMF) was established in 1945 as a cooperative, intergovernmental, monetary and financial institution that sought to promote currency exchange stability, provide balance-of-payments assistance, foster trade, and stimulate economic growth. Its initial membership of 39 member countries has grown to 182

¹²The International Monetary Fund provides resources to its members from the General Resources Account up to a specified amount and during a specified period, provided that the member observes the terms established in the arrangement.

¹³Refer to appendix IV for details.

members as of April 30, 1999. The IMF is managed by a Governing Board and a 24-member Executive Board, the IMF's primary decision-making body. The IMF's financial year ends on April 30 of each year, and its financial statements are audited annually by an external audit committee with assistance from an international public accounting firm. Although the Fund's financial statements are not bound by any national or international accounting principles, the IMF generally follows their concepts while taking into account the Fund's unique financial structure and operations. The key components of the IMF's financial operations are described in the following paragraphs.

Liquid Resources

The IMF's liquid resources consist of Special Drawing Rights (SDR) and usable national currencies provided primarily from members' quota subscriptions. These resources are used to provide financial assistance to members with balance-of-payments problems. When a member borrows from the Fund, the country purchases the currency it needs from the IMF with an equivalent amount of its national currency. The member later repurchases its currency using SDR or other currency on terms established by the IMF. Because the Fund's financial assistance is in the form of currency purchases by member countries, it does not reduce the combined total of its currency holdings in terms of SDR equivalents; that is, the funds are not lent out.¹⁴ Instead, the composition of the IMF's currency holdings changes as "borrowers" replace the currency they purchase with their national currency. The relationship of the IMF's holdings of a member's national currency to the member's quota is an important one because it determines whether the member is a creditor, debtor, or in a neutral position with the IMF. With some exceptions, currencies of members who are creditors are considered usable by the IMF to finance transactions, while currencies of countries in a neutral borrowing or a debtor position are considered unusable by the IMF.

Borrowing Authorization

The IMF, in certain circumstances, has access to credit lines with groups of countries to finance lending to members and has activated these credit lines at various times in its history. Its principal credit lines are the General

¹⁴The IMF considers its financing to low-income developing countries on concessional (below-market-interest-rate) terms to be lending. This lending is financed from a trust account, the Enhanced Structural Adjustment Facility (ESAF) Trust that is administered by the IMF outside of its General Department.

Arrangements to Borrow (GAB), established in 1962, and the New Arrangements to Borrow (NAB), established in 1998. As of April 30, 1999, the combined amount available to the IMF was \$46 billion under the GAB and the NAB. The IMF also has had other arrangements to borrow from governments and central bank sources. It has authority for private-sector borrowing but has never utilized this source of funds.

Gold Holdings

The IMF holds about 103 million fine ounces of gold at designated depositories in four member countries.¹⁵ The IMF values its gold at SDR 35 per fine ounce (about \$47 per fine ounce as of April 30, 1999), its value at the time of acquisition.¹⁶ Therefore, the gold holdings were valued on its balance sheet at SDR 3.6 billion (about \$5 billion). However, the IMF reported in a footnote to its financial statements the market value of its gold holdings as of its financial year-end. On April 30, 1999, the market value of the IMF's gold holdings was about \$30 billion.

Members' Quotas

Quotas are the membership dues that countries pay when they join the IMF and when there is an approved increase in such dues (a review of quotas is held every 5 years). Quotas comprise the bulk of the Fund's resources for providing financial assistance. Up to 25 percent of quotas must normally be paid in reserve assets, which are currencies that are freely usable in the principal foreign exchange markets (U.S. dollars, yen, euros, or the pound sterling) or SDR.¹⁷ The balance may be paid either in a country's domestic currency or with noninterest-bearing promissory notes.¹⁸ The portion paid in freely usable currency, or SDR, is referred to as the member's "reserve asset" or "initial reserve tranche position."

¹⁵These gold holdings are held in the United States, the United Kingdom, France, and India and represent about 9 percent of the world's official gold holdings, as of March 1999.

¹⁶An exception is a small amount of gold (21,396 ounces) that Cambodia gave to the IMF in December 1992 in partial settlement of an overdue loan obligation. The IMF valued this amount at SDR 5.1 million (about \$6.8 million as of April 30, 1999).

¹⁷Articles of Agreement, Art. III, Sec. 3(a).

¹⁸Articles of Agreement, Art. III, Sec. 4. These promissory notes are made payable to the IMF, are denominated in the member's domestic currency, and are held by the member's designated central bank or other designated depository. The IMF views these notes as fully equivalent to its currency holdings because the IMF can cash the notes on demand within 24 hours to receive members' domestic currency. IMF members are obligated to maintain the SDR value of their quotas.

The IMF's Liquidity Position

As of April 30, 1999, the IMF estimated that it had about \$77 billion available to meet members' draws on their reserve tranche positions and future lending needs, giving it a liquidity ratio of nearly 89 percent. IMF officials told us that its liquid resources are adequate to meet its members' projected financing needs until the next quota review, which is scheduled to begin in 2002. In calculating its available resources, the IMF deducted \$19 billion for the maintenance of a working balance reserve, which the Fund believed was needed to pay members in specified currencies. Our analysis, however, indicates that the Fund has not drawn from this working balance in over 20 years, as of April 30, 1999. Consequently, the IMF's available and uncommitted resources may have been understated as of that date.

The Fund believes that it is necessary to maintain an amount of available and uncommitted resources that bears a reasonable relationship to its liquid liabilities to maintain the capacity of the Fund to meet its members' requests for their reserve positions. While the IMF does not consider its liquidity ratio to have a minimum level below which it should not fall, historically, the IMF has managed its resources in a way where this ratio has not fallen below 25 percent to 30 percent for an extended period. However, we found that the IMF had no formal methodology for deciding what the appropriate level should be; consequently, this threshold does not provide an analytical basis for determining whether the IMF's resources are constrained.

The IMF's Approach for Calculating Liquid Resources

To estimate the amount of its available and uncommitted resources, the IMF started with its total resources of about \$287 billion as of April 30, 1999. This amount was then reduced by the amount of the IMF's holdings of unusable resources—\$92 billion as of April 30, 1999. The remaining \$195 billion, or 68 percent, was considered usable by the IMF. These usable resources consisted of (1) holdings of currencies of members considered by the Executive Board to have sufficiently strong balance-of-payments and reserve positions for their currencies to be used in IMF operations and (2) the IMF's holdings of SDR. The IMF considered \$92 billion of its resources to be unusable to finance its transactions because as of April 30, 1999, they were

- currencies of members that were using IMF resources and were therefore in a weak balance-of-payments or reserve position;

- currencies of members with relatively weak external positions who may have drawn on their reserve tranche position but did not have outstanding loans from the IMF;
- gold holdings of the Fund that require an 85-percent vote by the Executive Board to be used and were not considered by the IMF as liquid resources; or
- other nonliquid assets, such as buildings and facilities.

After subtracting the unusable portion from its total resources, the IMF further reduced total usable resources for the amount of credit already extended to members in order to determine its available and usable resources. The IMF then reduced its available and usable resources by the amount of its estimates for commitments made and the minimum working balance reserve, as indicated in table 1.

Table 1: Calculation of the IMF's Available and Uncommitted Resources as of April 30, 1999

U.S. dollars in billions	
Total resources	\$287
Less: unusable ^a resources	(92)
Total usable resources (before IMF extends credit)	195
Less: resources used (credit extended)	(82)
Available and usable resources	114
Less: commitments	(18)
Less: working balance reserve	(19)
Available and uncommitted liquid resources	\$77^b

Note: SDR exchange rate = \$1.35123 for April 30, 1999, data.

^aThis includes currencies of members with relatively weak external positions, the IMF's gold holdings, and other nonliquid assets.

^bAmounts do not add up due to rounding. The \$77 billion in liquid resources gives the Fund a liquidity ratio of nearly 89 percent. The underpinnings for the IMF's liquidity threshold, which ranges between 25 percent to 30 percent, derives from its unique nature among the international financial institutions.

Source: The IMF.

Commitments represent lending arrangements in place to member countries needing financial assistance. A lending arrangement is a decision of the IMF by which a member is assured that it will be able to make purchases (drawings) from the General Resources Account (GRA) up to a specified amount and during a specified period of time, provided that the

member observes the terms and conditions set out in the arrangement. Commitments reflect an estimate of undrawn loan balances through their expiration date (which can be up to 3 years) and 50 percent of precautionary arrangements.¹⁹

Deduction for Working Balances

The Fund's approach to estimating its available and uncommitted resources, as of April 30, 1999, included a deduction of \$19 billion for maintaining a minimum working balance reserve. This working balance reserve is set at 10 percent of the quotas of members whose currencies are on the operational budget.²⁰ According to the IMF, it needs this working balance reserve to provide its members with specific currency denominations as requested. However, our analysis indicates that the IMF has not used this working balance reserve in over 20 years.

According to the IMF, a working balance reserve is needed because of the Fund's potential commitment to pay in specific currencies: (1) remuneration²¹ to members, (2) payment commitments from IMF borrowing, and (3) requests from members who need foreign exchange to buy back their national currencies from other countries. However, we found that it was unlikely that the working balance reserve would be needed to meet these obligations. For instance, we found that since 1987, almost all members have requested that remuneration payments be made in SDR rather than in currencies. Members obtain a slightly higher level of earnings on their reserve tranche positions when they receive SDR rather than a specific currency as payment for remuneration because of the IMF's burden-sharing policy. (See app. IV for a description of burden-sharing.) As of April 30, 1999, the Fund held about \$5 billion in SDR, which, according to

¹⁹The IMF makes precautionary arrangements to assist members interested in boosting confidence in the economic management of their country. Under such an arrangement, the member agrees to meet certain conditions in exchange for access to the IMF's resources but expresses its intention not to draw although it retains the ability to do so.

²⁰The IMF does not publicly disclose the number of countries on its operational budget, but it tends to range between 20 to 35 countries. Quarterly, the IMF reassesses the financial strength and reserve positions of the members on the operational budget to determine if the members' currencies remain strong enough to be used or if other members' currencies have strengthened sufficiently to be included in IMF transactions.

²¹Remuneration is interest paid to a member for use of its currency.

the IMF, can also be used for working balances.²² Thus, minimum working balances of specific currency denominations were not needed to pay remuneration as of April 30, 1999.

In addition, the second purpose of maintaining a working balance reserve is to repay any borrowings by the Fund in the specific currency borrowed. When the IMF accesses its GAB or NAB credit lines, it borrows directly from the participant providing the credit line and receives the currency of the participant. The IMF is obligated to repay any resources drawn from these credit lines in the same currency it borrowed.²³ Prior to 1998, the IMF had not activated its credit lines in 20 years. In July and December 1998, the IMF drew on the GAB and the NAB, respectively, borrowing about \$6 billion in members' currencies. However, in March 1999, the IMF repaid both the GAB and NAB borrowings using U.S. dollars, SDR, and other currencies without using the working balance reserve.

Further, the IMF's third reason for maintaining a minimum working balance reserve is to provide particular currencies for special purposes, such as for a member to buy back balances of its national currency to intervene in currency markets under the Exchange Rate Mechanism (ERM).²⁴ This could happen if a member needed to acquire its national currency from another member who held a significant amount of the member's currency.²⁵ The last time that an industrial country made any reserve tranche position drawing for settlements under the ERM was in 1988. In the event that a reserve tranche position drawing for an industrial country is needed, the IMF has up to \$46 billion in resources from its credit

²²According to the IMF, its holdings of SDR were temporarily increased due to the recent quota increase and will be reduced to a target level between about \$1.5 billion and \$2 billion.

²³"New Arrangements to Borrow, Paragraph 11, Repayment of the Fund." Under the instrument creating the NAB, the IMF "shall" repay in the participant's currency whenever feasible, in SDR or, after consultation with the participant, in convertible currencies.

²⁴The ERM was a feature of the European Monetary System (EMS) by which EMS members agreed to maintain the relative prices of their currencies within narrow limits. This was done by keeping each country's value in European Currency Units within an agreed range of par values.

²⁵Articles of Agreement, Art. V, Sec. 3 (d). The member could then draw on its reserve tranche position and obtain from the IMF the currency of the other member. The member would use the other member's currency to purchase its own currency from that member. The end result would be that the purchasing member would in effect be reducing the supply of its currency held internationally and, thus, could strengthen its own currency.

lines to accommodate such a request provided the conditions for the use of the credit line have been met.

Moreover, the IMF seeks to maintain a balance in the various types of currencies it holds to avoid the overuse of any particular currency. It does this by applying a systematic approach through its operational budget that allocates the specific currencies it plans to use to finance transactions and to receive for repayments. If a currency is overused, the IMF can discontinue use of this currency for disbursements and request that repayments be made in that currency to replenish the IMF's holdings of such currency to a level it considers acceptable. Due to this ability to manage the use and replenishment of specific currencies, the IMF is able to ensure that it retains sufficient levels of the various types of currencies it needs.

The most recent instance in which the IMF was unable to provide one of its members with the specific type of currency it wanted was in 1978. Even though the minimum working balance reserve policy had been established at 5 percent of quotas and totaled about approximately \$3 billion in 1978, the Fund did not have sufficient amounts of yen and deutsche marks to provide to the United States, which needed about \$5 billion worth of those currencies to strengthen the U.S. dollar following its depreciation. To obtain the needed currencies, the United States sold the equivalent of \$2 billion of its SDR holdings and drew the equivalent of \$3 billion from its reserve tranche position. Despite the IMF's policy, 5 percent of the quotas for Germany and Japan were not set aside as minimum working balances. Instead, the Fund provided yen and marks to the United States by activating the GAB credit lines with Japan and Germany. If in the future the IMF did not have enough of a specified currency on hand to meet a member's needs, the IMF could again activate its credit lines to obtain the specific currency denominations as it did in 1978.

Basis for IMF's Liquidity Ratio Threshold

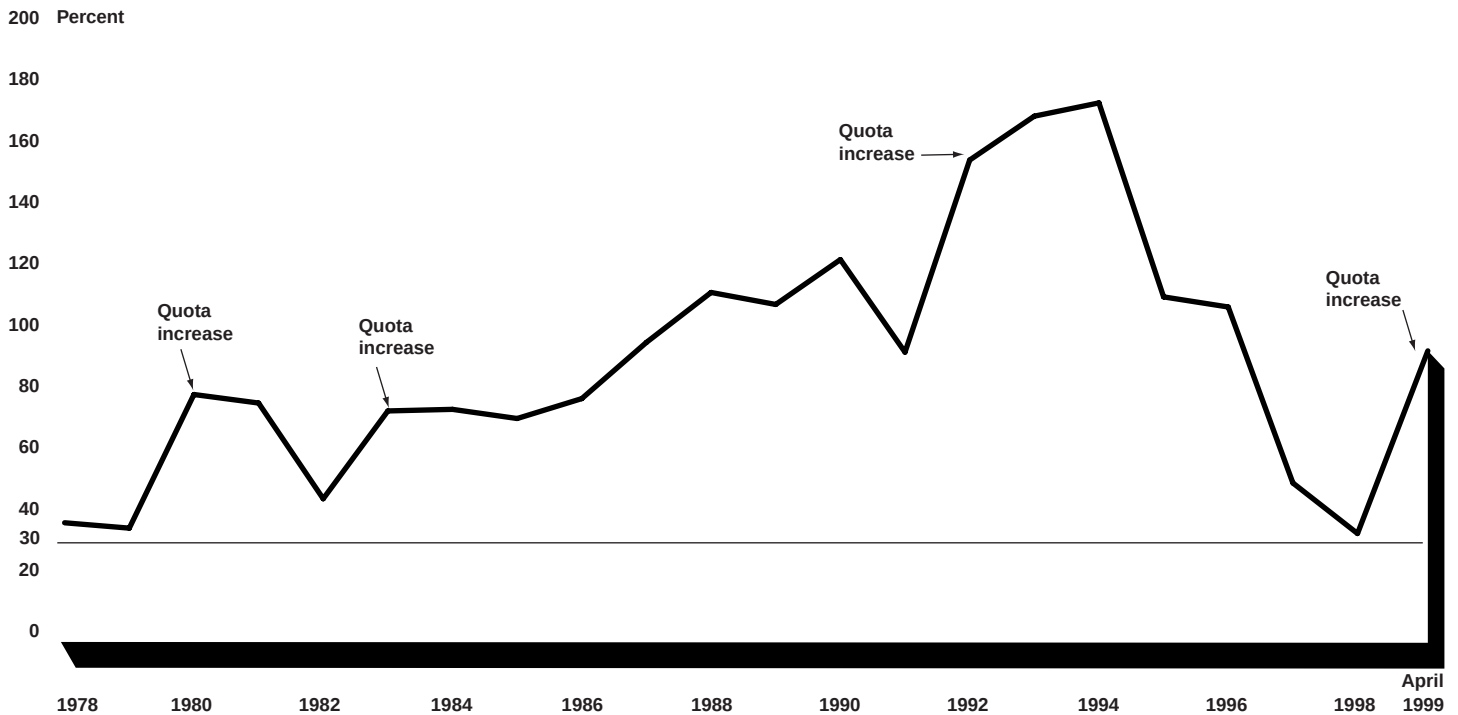
The IMF uses its liquidity ratio as a measure of the adequacy of its resources to meet members' financing needs, including a member's request to draw on its reserve tranche position. The IMF considers such a withdrawal to be the first claim on its resources, and as of April 30, 1999, this amounted to about \$86 billion in potential claims, compared to \$77 billion in available, uncommitted resources. According to the IMF, while it is difficult to project the probability that a member will draw on its reserve tranche positions at any particular time, the IMF must be in a position to meet any member's request for use of its reserve tranche

position.²⁶ The IMF considers the likelihood that all of its liquid liabilities would be withdrawn over a short period of time to be relatively small. Between January 1999, when the quota increase went into effect, and April 30, 1999, 92 developing countries withdrew their reserve assets from the IMF. Such withdrawals totaled about \$3.6 billion. (See app. I for further details.)

The Fund has managed its resources so that historically its liquidity ratio, the relationship between its available and uncommitted resources and its liquid liabilities, has not fallen below a 25-percent to 30-percent threshold for an extended period. The IMF uses the liquidity ratio as a benchmark of the adequacy of its resources. The IMF does not have a formal method to determine the appropriate minimum level of resources and the prevailing threshold was not based upon the IMF's analysis of variables that affect its liquidity. Such factors include members' historical reserve tranche drawings and/or forecasts of members' future reserve tranche drawings. Consequently, this liquidity threshold does not provide an analytical basis for determining whether the Fund's resources are, in fact, constrained. Moreover, the formula to calculate the liquidity ratio has changed four times in the last 20 years, further complicating the historical relevance of the ratio in IMF decision-making. (See fig. 1 for the IMF's liquidity ratio since 1978.)

²⁶Articles of Agreement, Art. V, Sec. 3.

Figure 1: Trends in the IMF's Liquidity Ratio, December 31, 1978-98, and April 30, 1999



Note: The liquidity ratios were calculated using the formula that was operational at each date. The numbers have not been adjusted to reflect a consistent methodology over time. The date of IMF quota increases are reported to help explain periods where the liquidity ratio rose rapidly. The underpinnings for the IMF's liquidity ratio threshold derive from its unique nature among the international financial institutions.

Source: The IMF.

IMF Borrowing and Credit Lines

Historically, the IMF has borrowed to supplement its liquidity, but only from official sources. This has included member countries and their central banks, one country that was not a member at the time the funds were borrowed (Switzerland) and its central bank, and the Bank for International Settlements.²⁷ The Fund has not borrowed from private capital markets, although the IMF's Articles of Agreements permit it to do

²⁷The Bank for International Settlement is an organization of central banks that is based in Basle, Switzerland. It is the principal forum for consultation, cooperation, and information exchange among central bankers.

so.²⁸ According to the IMF, the preference for borrowing from official rather than private sources reflects the nature of the Fund as a cooperative, intergovernmental institution whose basic purpose was to facilitate the overall adjustment process by making surpluses of some countries available to deficit countries.

The GAB²⁹ credit lines were established in 1962. The first drawing on the GAB was in 1964. In the 1970s, during periods of large payment imbalances, the IMF continued to use the GAB. In addition, the IMF began other official sector borrowings in the mid-1970s, and borrowing financed 45 percent to 62 percent of IMF credit between 1974 and 1979 and between 40 percent and 50 percent between 1980 and 1985. Since 1985, there has been a substantial decrease in borrowing, and there was no new borrowing between 1992 and 1997.

Borrowing resumed in July 1998, when about \$2 billion was borrowed from the GAB to finance credit assistance to Russia. Also, in December 1998, about \$4 billion was borrowed from the IMF's most recently established credit line, the NAB,³⁰ in connection with a 3-year credit arrangement with Brazil. Both of these amounts were promptly repaid by the Fund in March 1999, shortly after the IMF received funds from the recent quota increase. (See app. V for a more detailed description of IMF borrowing.)

The IMF's Gold Holdings

The IMF held a reserve of about 103 million fine ounces of gold with a market value of about \$30 billion as of April 30, 1999.³¹ This gold was largely acquired through members' quota reserve payments that up until the early 1970s had to be made in gold. With the end of the gold standard in

²⁸Articles of Agreement, Art. VII, Sec. 1 (i). However, a member can object to its currency being borrowed from whatever source.

²⁹The GAB is an arrangement of credit lines that the IMF maintains with the Group of 10 Industrialized Countries (G-10) for use in emergencies. The G-10 originally comprised 10 industrialized countries: Belgium, Canada, France, Germany, Italy, Japan, the Netherlands, Sweden, the United Kingdom, and the United States. Switzerland became the 11th member in 1984.

³⁰The NAB is an enlarged version of the GAB with 25 members. Together, GAB and NAB had a combined total of about \$46 billion as of April 30, 1999.

³¹As of August 30, 1999, the market value of the Fund's gold holdings had declined to about \$26 billion.

the early 1970s and the passage of the second amendment to the IMF's Articles of Agreement in April 1978, gold's formal role in the IMF and international currency transactions was eliminated. While a formal role for gold no longer exists, current IMF policy stresses the importance of gold as a reserve for the IMF. In 1995, the IMF's Executive Board reviewed the IMF's position on holding gold as a reserve asset and established several governing principles for managing its gold reserves. These principles state that

- gold provides a “fundamental strength” to the IMF;
- gold provides operational maneuverability in the IMF's use of its resources and adds credibility to its precautionary balances;
- gold should be held to meet unforeseen contingencies;
- the IMF has a responsibility to avoid disruption to the functioning of the gold market; and
- profits from gold sales should be retained and invested, and only the income from such investments should be used for agreed-upon purposes such as providing balance-of-payment assistance to developing nations.

The IMF continues to view gold as a valuable reserve asset despite events over the past 10 years suggesting that a consensus on this point among official holders³² has begun to weaken. Several official government holders of gold have sold a portion of their holdings, and an estimated 80 official holders have lent their gold to the private market to earn a return on their holdings. Since the mid-1970s, the Fund has only considered or allowed gold sales to support specific balance-of-payment or debt relief proposals. The “opportunity costs” associated with this policy are significant. For example, in 1995, the IMF examined the effect of its decision to hold its stock of gold. The decision to hold gold instead of selling it and investing the sales proceeds has resulted in tens of billions of dollars of foregone realized gains and investment income.

The Size and Value of the IMF's Gold Holdings

The IMF values its gold at SDR 35 per fine ounce (about \$47 per fine ounce as of April 30, 1999), its value at the time of acquisition. Therefore, the IMF's gold holdings were valued on its balance sheet at SDR 3.6 billion (about \$5 billion). However, the IMF reported in a footnote to its financial

³²The United States, the official holder with the largest amount of gold reserves, continues to view gold as a valuable reserve asset.

statements the market value of its gold holdings as of its financial year-end. On April 30, 1999, the IMF estimated its gold had a market value of about \$30 billion.

The IMF treats gold as a “nonliquid” resource that is generally not available to finance its operations. Gold is considered nonliquid by the IMF because mobilization of this resource must be approved by 85 percent of the Executive Board's total voting power. As a result of this fact and the length of time required to dispose of gold reserves without significantly disrupting the financial markets, gold cannot be easily used to meet near-term financial crises.

The IMF has determined that ownership rights to the Fund's gold reside with the IMF.³³ Under the IMF's Articles of Agreement, members may have residual rights to the gold in two instances: if the Fund elects to restitute³⁴ gold to members or to liquidate the Fund. In the first instance, gold could be restituted to all countries that were members on August 31, 1975, based on their quotas at that time.³⁵ In the latter case, gold may be distributed to members on the same basis after the Fund's liabilities have been satisfied.³⁶ If the IMF elected to restitute its current stock of over 100 million fine ounces of gold, the United States would receive almost 24 million fine ounces of gold based on the formula described in the Articles.

The IMF's gold holdings have fluctuated over time, peaking in the 1972-75 period when the Fund held a total of about 153 million fine ounces of gold. By 1980, the IMF's total gold holdings had dropped to the current level of 103.4 million fine ounces.³⁷ No sales of gold have occurred since May 1980. The IMF's gold holdings since the Fund's inception are shown in figure 2. The large increase in gold holdings between 1969 and 1970 (from about 66 million ounces to 124 million fine ounces) is due to the relatively large fifth general quota increase and the repurchase of gold that had been

³³IMF Executive Board, Dec. No. 170-3 (5/20/47).

³⁴According to the IMF, the term “restitute” describes the sale of the IMF's gold holdings to members at the official price of SDR 35 per fine ounce instead of at market rates.

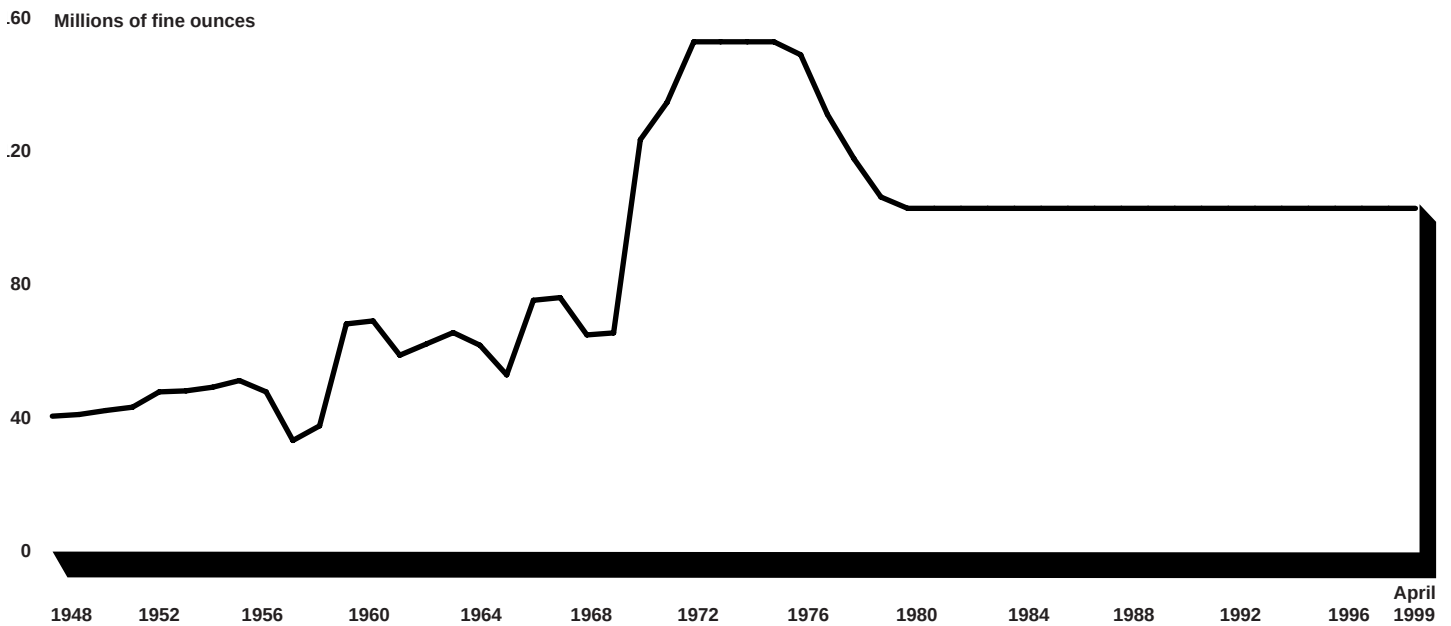
³⁵Articles of Agreement, Art. V, Sec. 12 (e).

³⁶Articles of Agreement, Schedule K.

³⁷In 1992, the Fund accepted 21,396 fine ounces of gold from Cambodia as payment for repurchase obligations.

previously sold to the United States. Appendix II provides additional details on the sources and uses of the Fund's gold holdings.

Figure 2: The IMF's Gold Holdings, 1948-April 30, 1999



Source: The IMF's *International Financial Statistics*.

Trends in Gold Reserve Management Practices

For almost a 20-year period after the United States left the gold standard in 1971, official holders of gold preferred to hold gold as a reserve asset rather than dispose of their gold holdings, including the United States, which has

monetized but not sold its gold holdings.³⁸ Beginning in 1988, this consensus began to weaken among certain official holders, with the sale of official gold holdings by Canada.³⁹ These sales were followed by gold sales and gold leasing by several additional countries, including the most recent sale of official gold by Great Britain in July 1999. Other sellers include Argentina, Australia, Belgium, the Czech Republic, and the Netherlands. In addition, a recently approved referendum in Switzerland, which removed the Swiss franc from the gold standard, has opened the possibility for a Swiss sale of an estimated 1,300 tons (about 42 million fine ounces) of gold, or over half of its national reserve.

An Estimate of the Cost of Holding Gold

The IMF has continued to examine various scenarios on the possible use of gold to produce income for the Fund taking into account its Articles, which place certain restrictions on the sale of gold. In addition, the IMF interprets its Articles as precluding the trading of gold by the Fund. According to one scenario, if the IMF sold 6 million fine ounces of gold each year from May 1980 to December 1996 (when the stock of the IMF's gold would have been fully depleted), and the proceeds were invested in financial instruments yielding the SDR rate of interest, the IMF would have received tens of billions of dollars in realized gains and investment income. Since gold prices fluctuate and have declined since the mid-1990s, the Fund may realize less now if it sold its gold than it would have realized at an earlier date, but the amount would still be in the billions of dollars.

Process for Determining the IMF's Quota Resources

The IMF's Eleventh General Review of Quotas began on August 9, 1995, and was completed on January 30, 1998, when the Board of Governors adopted a resolution proposing to increase the total of IMF quotas by 45 percent from SDR 146 billion to SDR 212 billion (about \$288 billion). During this process, IMF staff provided quantitative analyses of various factors to the Executive Board for its consideration and recommended that the size of the quotas be increased by 100 percent as a result of those factors. IMF documents showed that the executive directors examined the staff's

³⁸The Secretary of the Treasury is authorized to issue gold certificates to the Federal Reserve, which then issues an equivalent credit (at the official price of gold) to a Treasury deposit account. The 1998 *Financial Report of the United States* notes that \$11 billion of the U.S. gold reserves of 262 million fine ounces has been monetized in this fashion.

³⁹Canada reduced its official gold reserve from 17 million ounces to 4 million ounces, between 1988 and 1995.

analyses and recommendation but did not reveal any alternative analytical basis on which the Executive Board's recommendation to the IMF's Board of Governors for a 45-percent increase was made. From the early stage of the review process, most directors had favored a much higher increase than 45 percent and had maintained that position through April 1997. However, between June 1997 and September 1997, a consensus was reached among the executive directors on the 45-percent increase and on the manner in which the increase would be distributed.

The IMF has never formally adopted a method for determining members' initial quotas and subsequent quota increases because it believes that quantitative measures cannot fully reflect the considerations that appropriately bear on each member's position or on the total size of the Fund's resources. Both the staff and the Executive Board have acknowledged that many of the factors that influence the size of the IMF's quotas are difficult to quantify. These factors include the prospective demand for IMF resources, the growth of world trade, and the trend in the IMF's liquidity position. In addition, the Executive Board takes into consideration the political feasibility of getting approval for the quota increase from the IMF's member governments. Consequently, the process for determining the size of the quota increase and the distribution among the IMF's members involves a great deal of judgment on the part of the Executive Board.

Although the distribution of quotas among the members determines the share of voting power in the IMF, the member's representation on the Executive Board, and the amount members can borrow from the Fund,⁴⁰ these issues were not a major source of debate in the Eleventh General Review. Most of the executive directors had agreed early in the quota review process that the distribution should be predominantly equiproportional,⁴¹ thus maintaining the quota structure. However, there were considerable differences of opinion on the share of selective increases to be included in the total as well as on the distribution method to

⁴⁰The amount of funds that a member may borrow from the IMF is typically limited to a certain percentage of that member's quota.

⁴¹Equiproportional increases are allocated based on a uniform percentage for members participating in the review. They are allocated irrespective of members' relative positions in the world economy and by definition, tend to maintain historical shares in quotas.

be used.⁴² In the end, the quota structure remained essentially unchanged, and the Eleventh General Review's increase was distributed based on an equiproportional element of 75 percent, a selective element of 15 percent, and an ad hoc element of 10 percent.⁴³ The selective element was distributed in proportion to members' shares, based on the quota calculations of IMF staff.⁴⁴ The ad hoc element focused on those members whose quotas were farthest out of line with their relative economic positions. A discussion of the history of the IMF's quota review process is provided in Appendix III.

The Evolution of IMF Lending

Since 1945, the IMF's GRA lending has evolved due to global events and to meet its member countries' needs. The GRA arrangements have expanded from short-term currency purchases for balance-of-payment problems to nine types of arrangements and facilities that have tended to have longer repayment periods. These changes came largely in response to the shift in the IMF's lending from a mix of industrialized and developing countries to developing countries only.

Developments in the IMF's Lending

As indicated in figure 3, industrial countries comprised about half of the total amount of the IMF's GRA outstanding credit from 1947 through 1977. However, industrial countries use of IMF resources decreased rapidly, and by 1988, all users of IMF resources were developing countries. The main cause of this change over time is that industrial countries developed increased access to funds provided by financial markets to satisfy their external financing requirements. However, many developing countries do

⁴²The various methods include: Method A, which allocates the selective element in proportion to members' shares in calculated quotas; Method B, which distributes the selective increase to only those members, or subset of members, whose shares in calculated quotas exceed their shares in present quotas; and Method C, which combines Method A with a technique providing for a further (selective) increase in quotas that becomes progressively larger as the discrepancy between the member's shares in calculated and actual quotas becomes larger.

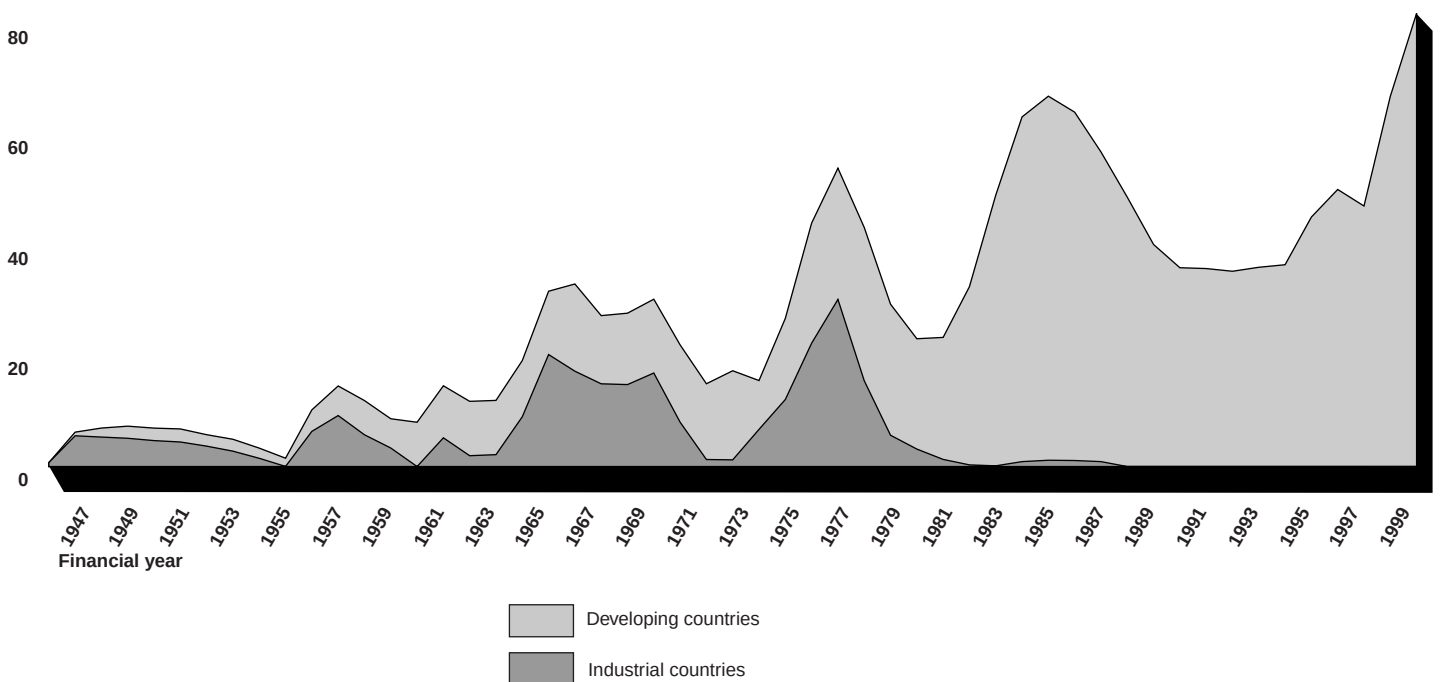
⁴³In a voluntary redistribution of quota shares, the quotas of France and the United Kingdom were equalized, as established in an agreement reached under the Ninth General Review, and there was a further reallocation of the quotas of Italy and Germany.

⁴⁴The quota calculations are based on formulas, which take into account each member's GDP, current payments and receipts, variability of current receipts, and reserves.

not have sufficient access to capital markets, particularly in periods of financial distress, and continue to rely upon the IMF for financial support.

Figure 3: IMF GRA Lending, 1947-99

100 Billions of 1998 dollars



Source: GAO analysis of IMF annual reports amounts adjusted to 1998 U.S. dollars.

Since 1947, the IMF's GRA lending has involved increasingly larger amounts of financial assistance in response to the needs of its members, as follows:

- From 1947 through 1975, the level of GRA lending was low and consisted primarily of currency purchases for balance-of-payments assistance, with many transactions paid in gold. The first lending peak of about \$33 billion (in 1998 U.S. dollars) as of April 30, 1967, reflected a high demand for balance-of-payments assistance particularly by the United Kingdom, which accounted for about 55 percent of the outstanding GRA credit.

- From 1976 through 1982, the level of GRA lending was moderate, with an expansion of the types of lending facilities and the end of the gold standard in 1978. A second lending peak of about \$54 billion (in 1998 U.S. dollars) as of April 30, 1977, was due to Oil Facility loans made in response to the worldwide oil crisis of 1974-75, which accounted for about 33 percent of the outstanding GRA credit.
- Since 1983, the level of GRA lending has been high, with a further expansion of the types of lending facilities and several world events requiring extensive IMF economic assistance. This included a third lending peak of about \$67 billion (in 1998 U.S. dollars) as of April 30, 1985, for economic assistance to Latin America during its debt crisis of 1983-90, which accounted for approximately 38 percent of the outstanding GRA credit. The fourth lending peak of \$82 billion as of April 30, 1999, reflected a high demand for lending to Indonesia, Korea, and Thailand in response to the 1997 Asian financial crisis and large borrowings by Brazil, Mexico, and Russia. These six countries accounted for about 73 percent of outstanding GRA credit.

Since 1947, the IMF has increased the number of its GRA lending arrangements and facilities in response to the increased demand for credit. This included an expansion of lending arrangements and facilities from currency purchases for short-term balance-of-payment problems to assistance for longer term structural balance-of-payment problems. Fund facilities grew to address shortfalls in export earnings, to finance oil purchases and other imports, to provide assistance to low-income countries, to fund the transition from centrally planned economies to market-based economies, and to give financing for exceptional balance-of-payment problems that could threaten the international monetary system.

With the expansion of IMF lending facilities, repayment terms have also tended to lengthen. This was due to greater extended fund arrangements and assistance to countries in transition to market-based economies. An exception to this trend was the creation of the Supplemental Reserve Facility (SRF) in 1997, with a repayment period of between 1 and 2-½ years.

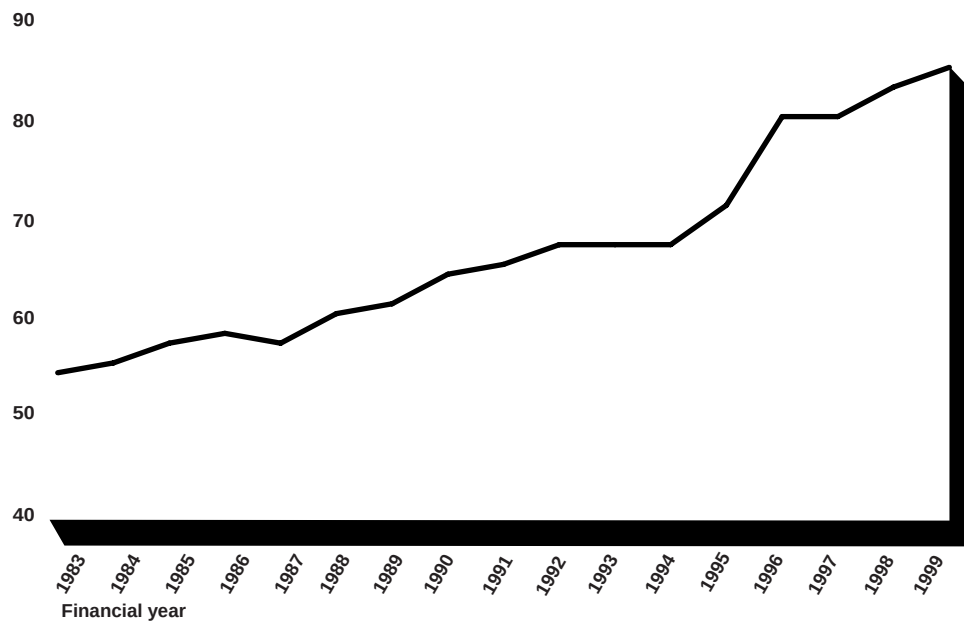
Lending Concentration, Borrowing Limits, and Arrears

As the IMF's lending has shifted exclusively to developing countries, its lending portfolio has become more concentrated among fewer borrowers. In addition, a number of borrowers have exceeded the IMF's normal limits permitting a member to borrow up to a certain percentage of the member's

quota.⁴⁵ Further, some members have been unable to meet their obligations to the Fund when due. As indicated in figure 4, the percentage of the IMF's GRA lending held by the 10 largest borrowers has grown steadily since 1983. The 10 largest users of IMF's GRA lending accounted for 55 percent of total GRA credit outstanding as of April 30, 1983. This percentage has steadily increased to 86 percent of total GRA credit outstanding as of April 30, 1999, among the highest levels in IMF history. One country, Russia, a borrower since 1993, accounted for 21 percent of total GRA credit outstanding as of April 30, 1999. See appendix IV, table 6, for a further discussion of the 10 largest GRA borrowers from 1983 to 1999.

Figure 4: Growth in Use of IMF GRA Credit by the 10 Largest Users, 1983-99

100 Percent



Source: GAO analysis of IMF annual report data.

⁴⁵Current rules governing the use of the IMF's GRA lending permit an IMF member to borrow an amount equal to 100 percent of its quota per year, with a cumulative limit of 300 percent, unless exceptional circumstances exist.

The limits as to the amount of funds that a member may borrow from the IMF were last changed in 1994, when the yearly limit on borrowing was increased from 68 percent of quota to 100 percent. In the past 4 years, the IMF has provided financing to five large developing countries that have experienced financial crises. This financing was in amounts that were all well in excess of the IMF's limit on cumulative borrowing (see table 2).

Table 2: IMF Borrowing Arrangements That Exceeded 300 Percent of Quota, as of April 30, 1999

Dollars in billions

Member	Arrangement date	Amount of arrangement	Percent of quota
Mexico	1995	\$17.9	688
Thailand	1997	3.9	500
Indonesia	1997-98	11.4	557
Korea	1997	21.0	1940
Brazil	1998	18.3	600

Source: GAO analysis of IMF data.

IMF officials have stated that the IMF has never had a lending default or write-off since its inception. However, since 1983, 15 IMF members have been unable to meet their obligations to the GRA when due.⁴⁶ Prior to this time, only Cambodia had experienced protracted arrears to the Fund. Arrears totaled about \$26 million from one member as of April 30, 1983, and reached a high of \$4.5 billion from nine members as of April 30, 1992. In response to this situation, the IMF took various measures intended to reduce arrearages, increase repayments, and protect the Fund's financial position. These measures included

- declaring members ineligible for further lending until arrears are cleared,

⁴⁶The 15 countries are Cambodia, Guyana, Vietnam, Liberia, Sudan, Peru, Zambia, Sierre Leone, Somalia, Honduras, Panama, Democratic Republic of Congo, Haiti, Bosnia/Herzegovina, and Serbia/Montenegro. See appendix IV for additional details regarding these countries' arrears.

-
- adopting a burden-sharing mechanism that created additional funds to share the cost of overdue obligations to the IMF between debtors and creditors,
 - developing a Strengthened Cooperative Strategy (including a rights accumulation program)⁴⁷ that included communications with international financial institutions if a member fails to fulfill its financial obligations to the Fund,
 - issuance of a public declaration of noncooperation⁴⁸ when a member does not actively cooperate with the Fund,
 - suspending the voting rights of members in arrears to the Fund, and
 - requiring compulsory withdrawal of members from the IMF who fail to clear their arrears.

Due to the measures taken by the IMF and through financial assistance provided by some countries, as of April 30, 1999, only five members were in arrears to the GRA, owing about \$2.8 billion.⁴⁹ In addition, none of the other 10 members formerly in arrears have incurred any subsequent arrears. The principal amount owed by these five members of about \$1.5 billion constituted less than 2 percent of the IMF's GRA credit outstanding as of April 30, 1999. Additionally, four of these members were declared ineligible for further IMF lending,⁵⁰ three were issued declarations of noncooperation,⁵¹ two have had their voting rights suspended,⁵² and one member is under consideration for compulsory withdrawal from the Fund as of April 30, 1999.⁵³

⁴⁷The rights accumulation program enables a member to accumulate rights to draw upon the IMF's resources after clearing its arrears and is limited to the 11 countries in protracted arrears as of the end of 1989. (See app. IV for a further discussion of the IMF's burden-sharing mechanism.)

⁴⁸A declaration of noncooperation is a prelude to suspending the member's voting rights.

⁴⁹The five countries are Congo (DRC), Liberia, Somalia, Sudan and the portion of the former Yugoslavia pertaining to Serbia/Montenegro.

⁵⁰The four countries are Congo (DRC), Liberia, Somalia, and Sudan.

⁵¹The three countries are Congo (DRC), Liberia, and Sudan. In August 1999, the IMF lifted the declaration of noncooperation for Sudan.

⁵²The two countries are Congo (DRC) and Sudan.

⁵³The country is Sudan.

In response to its problems with arrears, the IMF increased its reserves for potential loan losses, known as “precautionary balances,” from about \$1.1 billion as of April 30, 1983, to about \$6.2 billion as of April 30, 1999. This included the adoption of “burden-sharing” in 1986 as a system of providing resources to increase precautionary balances to share the cost of overdue obligations between debtor and creditor members.

Status of the IMF's and Its Members' Year 2000 Computer Compliance

The Year 2000 problem could affect nearly every aspect of the international financial system—from the ability of internal systems that support IMF operations to function properly to the ability of member nations to repay loans. While the IMF recognizes the importance of the impact that the problem may have on its mission-critical systems and has taken steps to mitigate potential damage, it still faces some challenges in providing more complete assurance that its internal business processes will continue to function after the date change. Further, IMF needs to complete its assessment of the impact of Year 2000 failures on the potential for increased demand for financing by its members.

IMF's Internal System Status

IMF officials stated that they have identified three systems as being mission critical⁵⁴ and believe that all three will be Year 2000 compliant by January 1, 2000. IMF is currently working on developing contingency plans for all three systems and expects to have them complete by the end of September 1999. Our Year 2000 business continuity and contingency planning guidance—also adopted by Office of Management and Budget—stresses the importance of good business continuity plans to minimize the risk of system failures on core business processes. We recommended that such plans be prepared by April 30, 1999, and tested by September 30, 1999.

While the Fund states that it is on target to test the plans by September 30, these plans may not account for all key processes. For example, Fund officials told us that the IMF has not completed assessment of its “user-developed systems” to determine which, if any of these systems, generate data for input into the mission-critical systems. However, they plan to complete this assessment and report on the results before the end of the year. By completing the assessment so late in the year, IMF will not be fully

⁵⁴These systems include the financial and administrative system, the member country account system and the payroll system.

aware of any problems until after the date change—too late to take preemptive action.

Member Nation Assessment

The IMF has only recently started to assess the Year 2000 status of its 182 member nations, and the impact that any problems faced by these members may have on IMF operations. Such problems could range from isolated failures in individual computer systems to larger, more debilitating, failures of critical infrastructure processes affecting transportation, public utilities, or financial operations. Such failures could in turn generate demand for additional financing and/or extensions in IMF repayment terms.

The IMF was slow in recognizing the potential impact and, in turn, was slow to initiate such an assessment. Officials told us that IMF delayed action because it believed that the issue was best addressed by the World Bank because it was better positioned to provide technical assistance. However, after the Fund conducted a Year 2000 seminar of the importance of member countries' compliance in April 1999, IMF officials became convinced that there were economic issues involved that could impact the Fund. Shortly afterward, an IMF-World Bank team was established to identify the countries that will not be compliant, the resulting impact on the IMF, and the contingency plans for worst-case scenarios. IMF officials do not know when the team will complete its work but do expect an interim report in the near future.

Depending on the results of the study, the late start by the IMF-World Bank team could limit the Fund's ability to effectively plan for actions that could limit the impact on its existing loan portfolio and position the IMF to offer more financial assistance to impacted nations.

Agency Comments and Our Evaluation

We requested comments on a draft of this report from the Department of the Treasury and from the International Monetary Fund. A senior Treasury official provided oral comments on behalf of Treasury and the IMF. These comments characterized our report as providing a comprehensive examination of the significant issues affecting IMF's financial condition that should be informative and useful to most readers. In addition, both the IMF and the Treasury provided technical and clarifying comments, which we incorporated where appropriate.

We are sending copies of this report to the Honorable Lawrence Summers, Secretary of the Treasury; the Honorable Madeleine K. Albright, Secretary of State; the Honorable Jacob Lew, Director, Office of Management and Budget; and the Honorable Michel Camdessus, Managing Director, IMF. Copies will be made available to others upon request.

This report was prepared under the direction of Harold J. Johnson, Associate Director, International Relations and Trade Issues, and Gary T. Engel, Associate Director, Governmentwide Accounting and Financial Management Issues. Please contact either Mr. Johnson at (202) 512-4128 or Mr. Engel at (202) 512-8815 if you or your staff have any questions about this report. Other key contacts and staff acknowledgments are in appendix VII.



Henry L. Hinton, Jr.
Assistant Comptroller General
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Jeffrey C. Steinhoff
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Accounting and Information Management Division

List of Congressional Committees

The Honorable Jesse A. Helms
Chairman
The Honorable Joseph R. Biden, Jr.
Ranking Minority Member
Committee on Foreign Relations
United States Senate

The Honorable Ted Stevens
Chairman
The Honorable Robert C. Byrd
Ranking Minority Member
Committee on Appropriations
United States Senate

The Honorable Jim Leach
Chairman
The Honorable John J. LaFalce
Ranking Minority Member
Committee on Banking and Financial Services
House of Representatives

The Honorable C.W. Bill Young
Chairman
The Honorable David R. Obey
Ranking Minority Member
Committee on Appropriations
House of Representatives

The IMF's Liquid Resources and Liquidity Position

The liquid resources of the International Monetary Fund (IMF) consist of national currencies and Special Drawing Rights (SDR).¹ Not all of the national currencies held by the IMF are usable all the time (that is, strong enough to be lent to other members). As of April 30, 1999, of the IMF's \$287 billion in resources, \$195 billion (68 percent) was considered usable by the IMF. National currencies constituted \$190 billion of usable resources, and the IMF's SDR holdings made up the remainder.² The IMF monitors the usability and actual use of the currencies through semiannual liquidity reviews and through its quarterly operational budget. Currencies are selected for the operational budget on the basis of an assessment of each member, using a range of indicators including members' balance of payments, members' reserve positions, and developments in exchange markets. As of April 30, 1999, the United States was the single largest contributor of usable resources, contributing 26 percent (about \$51 billion) of the IMF's total usable resources.

Over the past 20 years, the amounts of the IMF's usable and unusable resources have varied, as indicated in figure 5. Usable resources over the period averaged about 60 percent of total resources, with a significant portion coming from the G-10.³ During this period, the United States was the major contributor of usable resources, except during 1978 and 1979 when the dollar was not considered strong enough to be used to finance the IMF's transactions and, accordingly, was excluded from the IMF's operational budgets.⁴

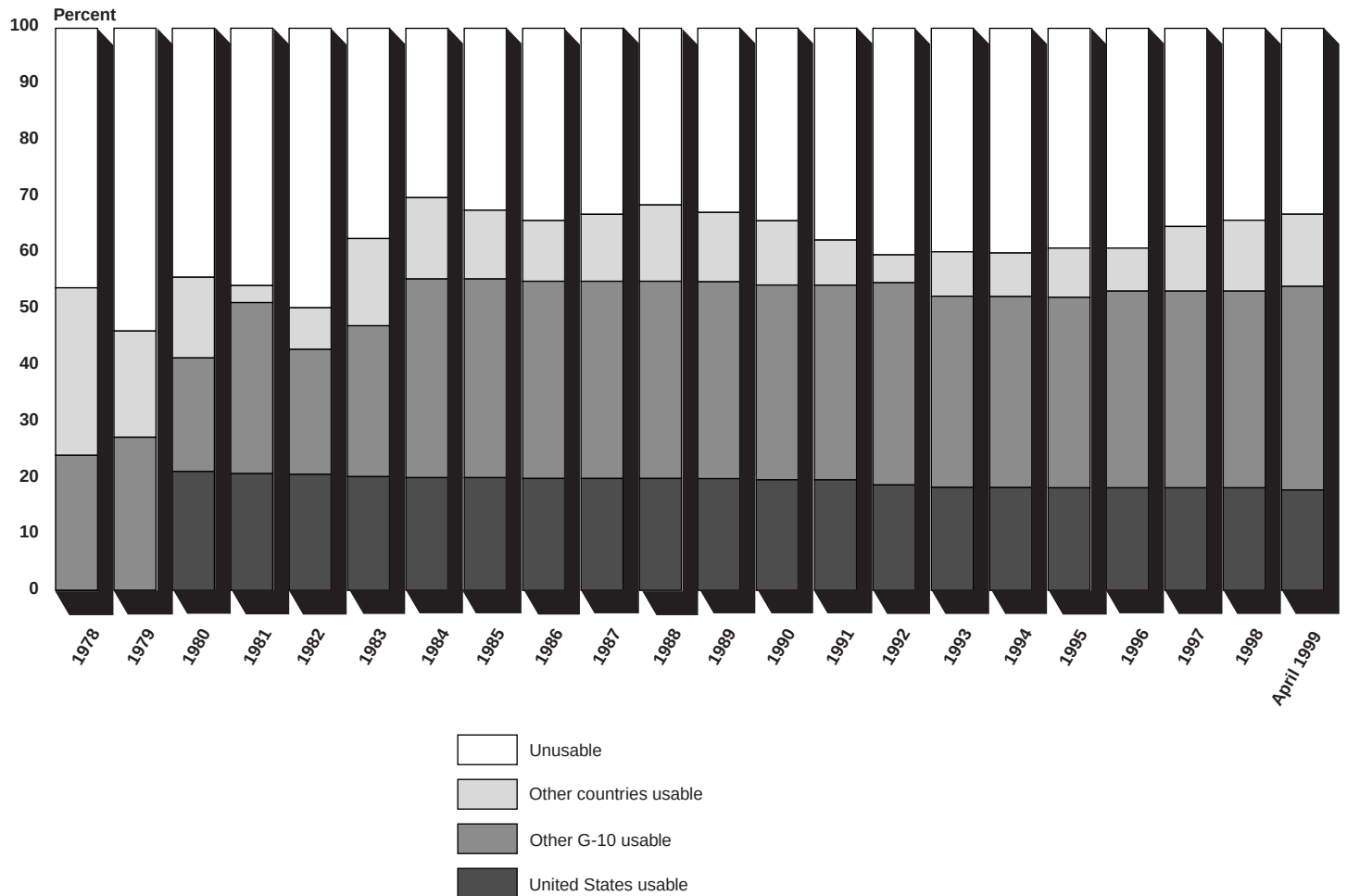
¹The SDR is a reserve asset that IMF has used since 1969. Its value comprises a weighted average of the values of four currencies: the U.S. dollar, yen, euros, and pound sterling. Because the value of the SDR relative to these currencies changes daily, the U.S. dollar value of amounts converted from SDR also changes daily. The SDR is the unit of account for the Fund.

²SDR can be held by, but not allocated to, the General Resources Account (GRA) of the IMF. The GRA receives SDR in partial payment of quotas, from charges on the use of IMF resources, and from repurchases.

³The G-10 originally comprised 10 industrialized countries: Belgium, Canada, France, Germany, Italy, Japan, the Netherlands, Sweden, the United Kingdom, and the United States. Switzerland became the 11th member in 1984.

⁴Following the depreciation of the U.S. dollar in the fall of 1978, the United States mobilized resources, including \$5 billion from the IMF, to defend the dollar.

Figure 5: The IMF's Usable and Unusable Quota Resources, End of Calendar Years 1978-98 and April 30, 1999



Source: GAO analysis of IMF data.

Members' Use of Reserve Tranche Position From the Latest Quota Increase

Table 3 identifies 92 countries that, by April 30, 1999, had withdrawn their entire \$3.6 billion of reserve tranche contributions from the January 1999, quota increase. This withdrawal reduced by about 17 percent the amount of usable resources obtained through contributions of reserve assets from the most recent quota increase.

Appendix I
The IMF's Liquid Resources and Liquidity
Position

The IMF's Eleventh General Review's quota increase of \$89 billion became effective in January 1999. As of April 30, 1999, \$84 billion had been paid by members, including 25 percent in usable currencies or SDR, totaling about \$21 billion. Included in this amount were the 92 developing countries that had paid their quota subscription of about \$14 billion, including 25 percent in reserve assets of usable currencies or SDR, totaling about \$3.6 billion. Between January 1999, when the Eleventh General Review quota became effective, and April 30, 1999, these 92 members withdrew the entire \$3.6 billion of usable currencies or SDR, replacing them with their national currencies.

Table 3: Eleventh General Review's Quota Increase and Related Reserve Tranche Drawings Through April 30, 1999, for Certain Members

Dollars in millions		
Country	Eleventh General Review's quota increase	Reserve tranche contribution and withdrawal (25 percent of quota increase)
Angola	\$107	\$27
Antigua & Barbuda	7	2
Argentina	784	196
Azerbaijan	59	15
Bangladesh	190	48
Belarus	143	36
Benin	22	6
Bolivia	61	15
Bosnia & Herzegovina	65	16
Brazil	1,169	292
Bulgaria	237	59
Burkina Faso	22	5
Burundi	27	7
Cambodia	30	8
Cameroon	68	17
Cape Verde	4	1
Central African Republic	20	5
Chad	20	5
Comoros	3	1
Congo, Republic of	36	9
Cote d'Ivoire	118	29

Continued

Appendix I
The IMF's Liquid Resources and Liquidity
Position

Dollars in millions		
Country	Eleventh General Review's quota increase	Reserve tranche contribution and withdrawal (25 percent of quota increase)
Croatia	\$ 140	35
Czech Republic	310	78
Dominican Republic	81	20
Ecuador	112	28
El Salvador	62	15
Equatorial Guinea	11	3
Eritrea	6	1
Ethiopia	48	12
Gabon	59	15
Gambia, The	11	3
Georgia	53	13
Guinea	38	10
Guinea-Bissau	5	1
Guyana	32	8
Iran, Islamic Republic of	566	141
Jamaica	98	25
Jordan	66	16
Kazakhstan	160	40
Kenya	97	24
Kiribati	2	1
Kyrgyz Republic	33	8
Latvia	48	12
Lesotho	15	4
Lithuania	55	14
Macedonia, former Yugoslav Republic of	26	7
Madagascar	43	11
Malawi	25	6
Mali	33	8
Mauritania	23	6
Mexico	1,125	281
Moldova	45	11
Mongolia	19	5
Mozambique	40	10
Myanmar	99	25
Nepal	26	7

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Appendix I
The IMF's Liquid Resources and Liquidity
Position

Dollars in millions		
Country	Eleventh General Review's quota increase	Reserve tranche contribution and withdrawal (25 percent of quota increase)
Nicaragua	\$ 46	11
Niger	24	6
Nigeria	637	159
Pakistan	372	93
Palau	1	^a
Panama	77	19
Papua New Guinea	49	12
Peru	233	58
Philippines	333	83
Romania	373	93
Russian Federation	2,206	551
Rwanda	28	7
Sao Tomé & Príncipe	3	1
Samoa	4	1
Senegal	58	14
Seychelles	4	1
Sierra Leone	36	9
Slovak Republic	135	34
Solomon Islands	4	1
South Africa	680	170
St. Kitts and Nevis	3	1
St. Lucia	6	1
Syrian Arab Republic	113	28
Tajikistan	36	9
Tanzania	70	18
Thailand	686	172
Togo	26	6
Trinidad & Tobago	120	30
Uganda	63	16
Ukraine	506	127
Uzbekistan	103	26
Vanuatu	6	2
Vietnam	118	30
Yemen, Republic of	91	23
Zambia	170	42

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Appendix I
The IMF's Liquid Resources and Liquidity
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Dollars in millions		
Country	Eleventh General Review's quota increase	Reserve tranche contribution and withdrawal (25 percent of quota increase)
Zimbabwe	\$ 124	31
Total	\$14,348	\$3,587

Continued from Previous Page

^aLess than \$1 million.

Note: SDR exchange rate = \$1.35123 as of April 30, 1999.

Source: GAO analysis of IMF's *International Financial Statistics*.

The IMF's Gold Holdings

From the IMF's inception through the passage of the second amendment to the IMF's Articles of Agreement in 1978, gold played an important role in the Fund's operations and the operations of the international monetary system. However, with the end of the gold standard in the early 1970s and the passage of the IMF's second amendment in April 1978, gold's formal role in the IMF and international currency transactions was eliminated.¹ Among other changes, the second amendment abolished the official price for gold, eliminated its use as the common denominator in the par value system,² and removed the obligatory use of gold in transactions between the IMF and its members. The second amendment anticipated a greatly diminished role for gold while seeking to promote an enhanced role for the SDR, which was intended to replace gold as the world's principal reserve asset.³

The Articles of Agreement specify that, based on an 85-percent majority vote of the total voting power of the Executive Board, the IMF may sell its gold and it may accept gold, at market prices, in discharge of members' obligations to the Fund.⁴ According to an IMF official, the Fund is not authorized to engage in any other gold transactions—including loans, leases, or use of gold as collateral—because these uses are not expressly allowed under the Articles of Agreement. More specifically, IMF documents note that the Articles of Agreement permit only the transfer of ownership rights to the gold for a price. According to IMF officials, because loans, leases, swaps, or the use of gold as collateral do not require a permanent transfer of ownership rights, they are not permitted under the Articles of Agreement.

¹In August 1971, the United States announced that it would no longer buy and sell gold at the official rate. This announcement was followed by the effective breakdown of the Bretton Woods par value system, with the devaluation of the U.S. dollar in December 1971, and by the generalized floating of exchange rates in March 1973.

²Before the breakdown of the Bretton Woods system in the early 1970s and the subsequent amendment of the Articles, the value of each member's currency was expressed in terms of gold (par value) or against the U.S. dollar, which was convertible to gold at \$35 per fine ounce.

³In the face of the development of worldwide currency exchange markets, the SDR has never achieved the preeminence anticipated by the IMF.

⁴Articles of Agreement, Art. V, Sec. 12(b)

When the IMF sells gold, the original capital value of the gold of SDR 35 per fine ounce is deposited in the GRA⁵ and becomes immediately available for the general operations of the IMF. Gold sale profits (that is, the sale price above the capital value of the gold) are generally deposited in a separate account, called the Special Disbursement Account (SDA),⁶ which provides the primary financial framework for handling such profits. Gold sale profits in the SDA may be transferred to specialized accounts (such as the Enhanced Structural Adjustment Facility-Heavily Indebted Poor Country (ESAF-HIPC) Reserve Trust Account) or they may be transferred to the GRA for use in the IMF's general operations.⁷

Specifically, the Articles of Agreement state that, based on majority votes by the Executive Board, assets held in the SDA may be used⁸

- to make transfers to the GRA for immediate use in the IMF's operations (70 percent of total voting power required);
- for operations and transactions that are not authorized by other provisions of the Articles of Agreement but are consistent with the purposes of the IMF, including balance-of-payments assistance to developing members (85 percent of total voting power required);
- for proportionate distribution of resources authorized for the purpose of providing balance-of-payments assistance to those developing members that were members on August 31, 1975, based on their respective quotas on that date (85 percent of total voting power required); and

⁵Articles of Agreement, Art. V, Sec. 12(f). Most transactions between member countries and the IMF take place in the GRA. This account handles, among other transactions, the receipt of quota subscriptions, purchases and repurchases, interest payments to members, and repayments of principal to the IMF's lenders.

⁶Articles of Agreement, Art. V, Sec. 12(f). The Special Disbursement Account is established to receive and invest profits from the sale of IMF's gold (that is, the net proceeds in excess of the book value of SDR 35 per fine ounce); and make transfers for special purposes authorized in the Articles of Agreement. As of April 30, 1999, the balance in the SDA totaled about \$924 million.

⁷Articles of Agreement, Art. V, Sec. 12(f) (i to iii). In June 1999, the Group of Seven (G-7) countries proposed in Cologne, Germany that the IMF to sell up to 10 million fine ounces of its gold holdings and to use the investment income from those profits to help finance the IMF's contribution to poor country debt relief. The G-7 consists of the seven major industrial countries (Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States) that consult on general, economic, and financial matters.

⁸Articles of Agreement, Art. V, Sec. 12(f).

-
- to transfer SDA resources to the investment account (85 percent of total voting power required).⁹

Resources in the SDA, investment account, and specialized trust fund accounts (such as the ESAF-HIPC Reserve Trust Account) may be invested in income-producing securities of members or of international financial organizations.¹⁰

Gold Acquisition Sources and Uses

The IMF acquired almost all of its gold prior to January 1, 1974, through a variety of means. The highest amount of gold holdings occurred in the mid-1970s, when the IMF held 153 million fine ounces of gold.

Specific acquisition sources for the IMF's gold holdings include the following:

- *Quota subscriptions.* The original Articles of Agreement prescribed that 25 percent of initial quota subscriptions and quota increases were normally to be paid in gold. This represented the largest source of the IMF's gold holdings.
- *Payment of charges.* Originally, all charges, that is, interest on members' outstanding use of IMF credit, were normally payable in gold.
- *Repurchases.* Members were permitted—and in some circumstances could be required—to 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.

From 1976 through 1980, the IMF reduced its gold holdings by one-third but has not disposed of any gold since then. Sales of gold on the open market or restitution of gold to the members has been used for a variety of purposes, such as the following:

⁹Articles of Agreement, Art. V, Sec. 12(g). The IMF has never activated the investment account because, according to IMF officials, the Fund has not had the available excess liquidity allowing for the transfer of such resources to the investment account.

¹⁰Articles of Agreement, Art. V, Sec. 12(h).

- *Sales for replenishments.* On several occasions in the late 1950s and in the 1960s, the IMF sold gold to replenish its holdings of usable currencies.
- *Sales to offset operating deficits.* To generate income to offset operational deficits, the IMF sold gold to the United States and invested the proceeds in U.S. government securities. A significant buildup of reserves through income from charges to members prompted the IMF to reacquire the gold from the U.S. government in the early 1970s.
- *Gold auctions.* Between April 1976 and May 1980, the IMF disposed of 25 million fine ounces of gold to finance an IMF trust fund, which was created in 1976 to support concessional lending by the IMF to low-income countries.
- *Restitution of gold to members.* Between 1977 and 1980, the IMF restituted a total of 25 million fine ounces of gold, in four annual installments, to members in proportion to their quota shares as of August 31, 1975. For the United States, this translated into the acquisition of 5.74 million fine ounces of gold.

The IMF's Quota Reviews

Since the inception of the IMF in 1945, total quotas have grown substantially—from about \$7 billion to about \$288 billion currently. There have been 11 general reviews of quotas, as well as a special review in 1959. Of the 12 reviews, 8 have resulted in increases in total IMF quotas. IMF staff recommendations¹ for quota increases have been primarily based on formulas and have been generally significantly higher than the quota increases approved by the Board of Governors. The Executive Board has not generally relied on formulas in its decisions in prior quota reviews, but rather has primarily depended on various factors, including the IMF's liquidity and the needs of the IMF's members.

The Growth in IMF Quotas

IMF quotas have risen as a result of increased membership,² eight general quota increases since 1959, and several special and ad hoc increases in quotas of individual members outside of the general reviews. Figure 6 shows the growth in IMF quotas in constant 1998 dollars for the United States, other industrial countries, and developing countries over the period 1948 to April 30, 1999. During this period, the annual average real growth in quotas was about 2 percent. For the United States the annual average real growth was about 0.7 percent, compared to about 1.8 percent for other industrial countries and about 3.2 percent for developing countries. While inflation has eroded the purchasing power of quotas during certain periods, particularly in the 1970s and 1980s, quota increases have tended to restore the purchasing power of quotas. However, the quota increases under the sixth and seventh general reviews, each of which became effective 2 years after approval, did not restore the quota's purchasing power to the 1970 level.

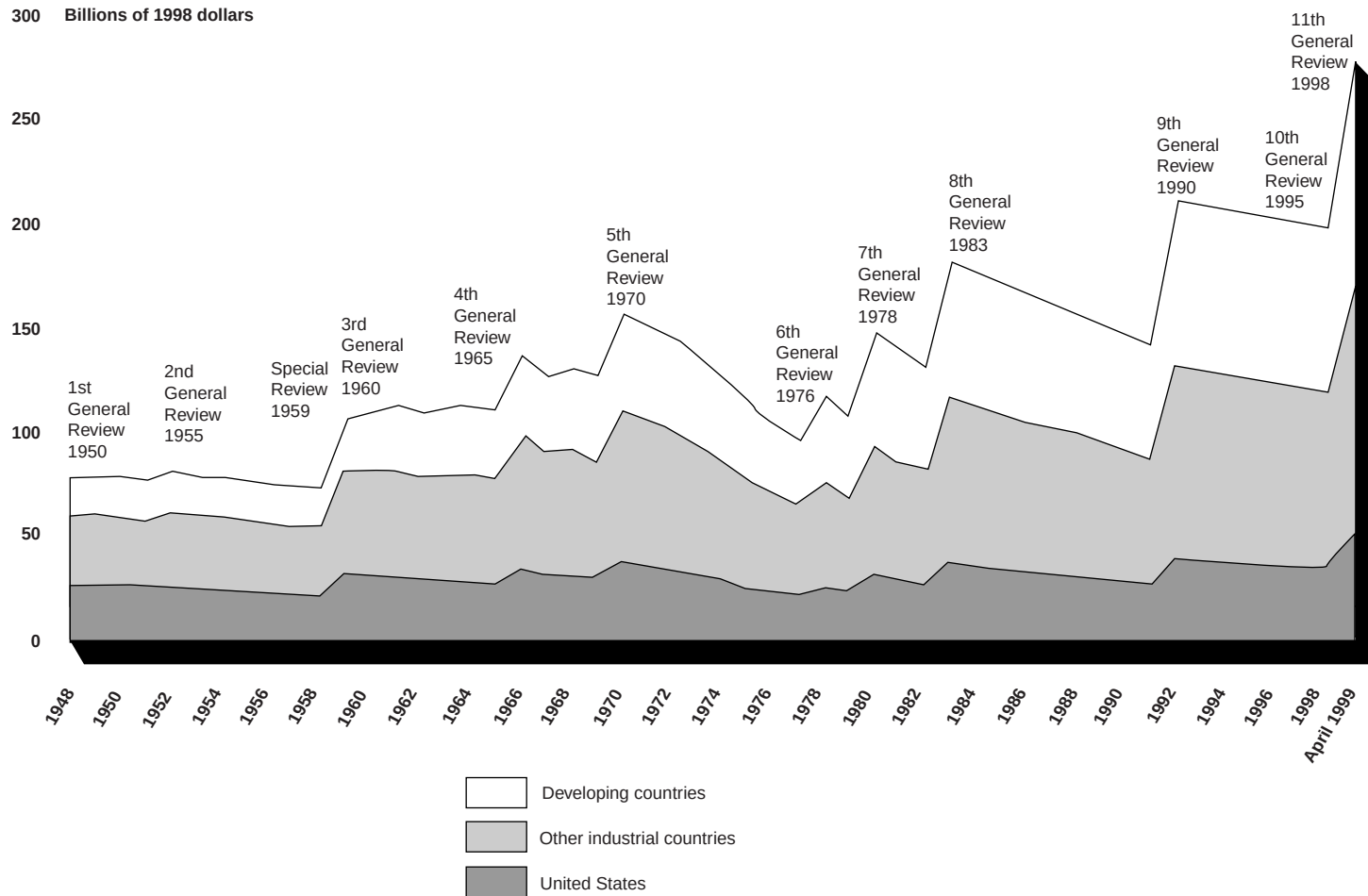
¹The IMF's staff recommendations included comments from IMF's Managing Director.

²There were 30 members of the Fund as of December 31, 1945. On March 8, 1946, the Board of Governors adopted a resolution extending the period from December 31, 1945, to December 31, 1946, in which countries could join as original members. As a result, there were 39 original members with total quotas of about \$7 billion.

Appendix III The IMF's Quota Reviews

Figure 6: IMF Quota Resources, 1948–April 30, 1999

300 Billions of 1998 dollars



Note: Quota values are expressed in 1998 dollars using the average 1998 dollar SDR exchange rate and an SDR price deflator.

Source: GAO analysis of IMF data.

Comparison of Staff's Recommendations and the Board of Governors' Approved Quota Increases

From our review of IMF documents,³ we have determined that the staff's recommendations for quota increases were generally significantly higher than the quota increases that were approved by the Board of Governors. As shown in table 4, in five reviews the staff recommended increases of as much as 100 percent, but the final approved increases ranged from zero to about 51 percent. For two reviews (the Special and Third Reviews), the Fund was not able to provide us with the staff's recommendations. In the remaining five reviews, while the staff did not always quantify the increases, its emphasis was that there should be a sizable general increase as well as selective increases to bring members' quotas more in line with their relative economic size.

The predominant factor guiding the staff's recommendations for a more enlarged IMF was the amounts derived by the quota formulas (see table 4 column 2). These formulas calculate the size of the IMF that is consistent with the growth in the world economy. However, it has been the position of executive directors that there is no single measure of the size of the world economy or indicators that are optimal for determining the size of the increase in quotas. Consequently, the results derived by the quota formulas have not had a significant bearing on the final decision on the appropriate size of the IMF.

³We did not review most official Committee of the Whole on Review of Quota's documents for prior quota reviews, as was done for the Eleventh General Quota Review. The majority of the information pertaining to the prior reviews was taken from the IMF's historical publications.

Appendix III
The IMF's Quota Reviews

Table 4: General Reviews of IMF Quotas

Review/Date	Quota increase suggested from formulas	Recommended quota increase from IMF staff	Final decision by Board of Governors^a	Percentage real growth in approved quotas^b	Some reasons cited for increase or no increase in quotas
First Review 1950	N/A	100%	0%	-24%	N/A
Second Review 1955	N/A	Graduated scale of revision ^c	0%	-4%	Quotas were considered large and had remained relatively unused.
Special General Increase 1959	N/A	N/A	60.7%	46%	Growth in the world economy. Large amount of IMF drawings and arrangements.
Third Review 1960	N/A	N/A	0%	-1%	N/A
Fourth Review 1965	N/A	50% plus selective increases to reduce disparities in the quotas of some members.	30.7%	30%	Concerns over a possible deficiency in international liquidity. Address some members' larger positions in the world economy.
Fifth Review 1970	N/A	A general increase of reasonable size.	35.4%	11%	To better reflect some members' stronger economic positions. Reduce IMF's reliance on borrowing.
Sixth Review 1976	75%	70-100%	33.6%	-14%	Emerging high balance-of-payment deficits. Better reflect some members' stronger economic positions. Reduce IMF's reliance on borrowing.
Seventh Review 1978	90%	75-100%	50.9%	31%	Many members with small quotas reluctant to ask the Fund for assistance because of their limited access to credit. Reduce IMF's reliance on borrowing.

Continued

**Appendix III
The IMF's Quota Reviews**

Review/Date	Quota increase suggested from formulas	Recommended quota increase from IMF staff	Final decision by Board of Governors^a	Percentage real growth in approved quotas^b	Some reasons cited for increase or no increase in quotas
Eighth Review 1983	106%	A relatively large general increase plus selective increases for many members.	47.5%	3%	Adjust members' quotas relative to their economic positions in the world economy.
Ninth Review 1990	58%	50% with a proportionate increase in IMF's borrowing authority or by about 100% if IMF's borrowing authority is not included.	50%	19%	Persistent debt problem in Latin America. Reduce IMF's reliance on borrowing.
Tenth Review 1995	34%	Selective increases based on members' shares in calculated quotas.	0%	-5%	The overall size of the IMF was considered sufficient to effectively promote its purposes.
Eleventh Review 1998	23%	100%	45%	40%	Increased demand for IMF resources. Growth in world trade and payments. Increased volatility of balance-of-payments stemming from sharp changes in private capital flows.

Continued from Previous Page

N/A = Not Available. Information was not provided by the Fund or was not available in the Fund's public documents.

Note: Table reflects reviews where some information was available on suggested increases by IMF staff.

^aPercentage increases of Board of Governors reflect overall increases at the date the quota increase was adopted.

^bA GAO-constructed SDR deflator is used to calculate real growth in approved quotas.

^cGraduated scale of revision is defined as revisions diminishing with the size of the quota, with the quota increase proportionately smaller for those countries with greater quota levels.

Source: GAO analysis of IMF data.

As shown in table 4, the IMF has cited many factors as having influenced the size of the IMF's quotas in prior reviews. In certain cases, these factors justified no change in the IMF's quota size; in other cases, they justified an increase. For example, in both the second and tenth reviews, the Board decided against any increase in quotas because the IMF's resources were considered sufficient. However, in many of the other reviews, the Board recommended increases, including the need to (1) address the possible deficiency in international liquidity, (2) reduce the IMF's reliance on

borrowing, and (3) adjust members' quotas to better reflect their relative position in the world economy.

Distribution of Quota Increases in Prior Reviews and Significance of Relative Shares

The large majority of quota increases in prior reviews were distributed equiproportionally, consistent with the strong desire of many countries to maintain the existing quota structure. Selective increases in member quotas change the relative size and voting shares of members within the IMF, increasing the quota share of some members while decreasing others. However, selective increases in quotas have taken place with the goal of bringing the quotas of members into better alignment with their relative economic size, and, in some cases, to strengthen the liquidity position of the IMF.

The overall quota structure between the two main groups of industrial and developing countries has been relatively stable over time. Figure 7 shows the history of voting shares.⁴ As of April 30, 1999, the voting share of the industrial countries was about 60 percent, as compared with about 70 percent in 1948, and the share of the developing countries was about 40 percent, as compared with 30 percent in 1948. While the United States is still the largest contributor to the IMF's resources,⁵ its voting share has fallen over time. Currently, this voting share is slightly over 17 percent, down from 31 percent in 1948.

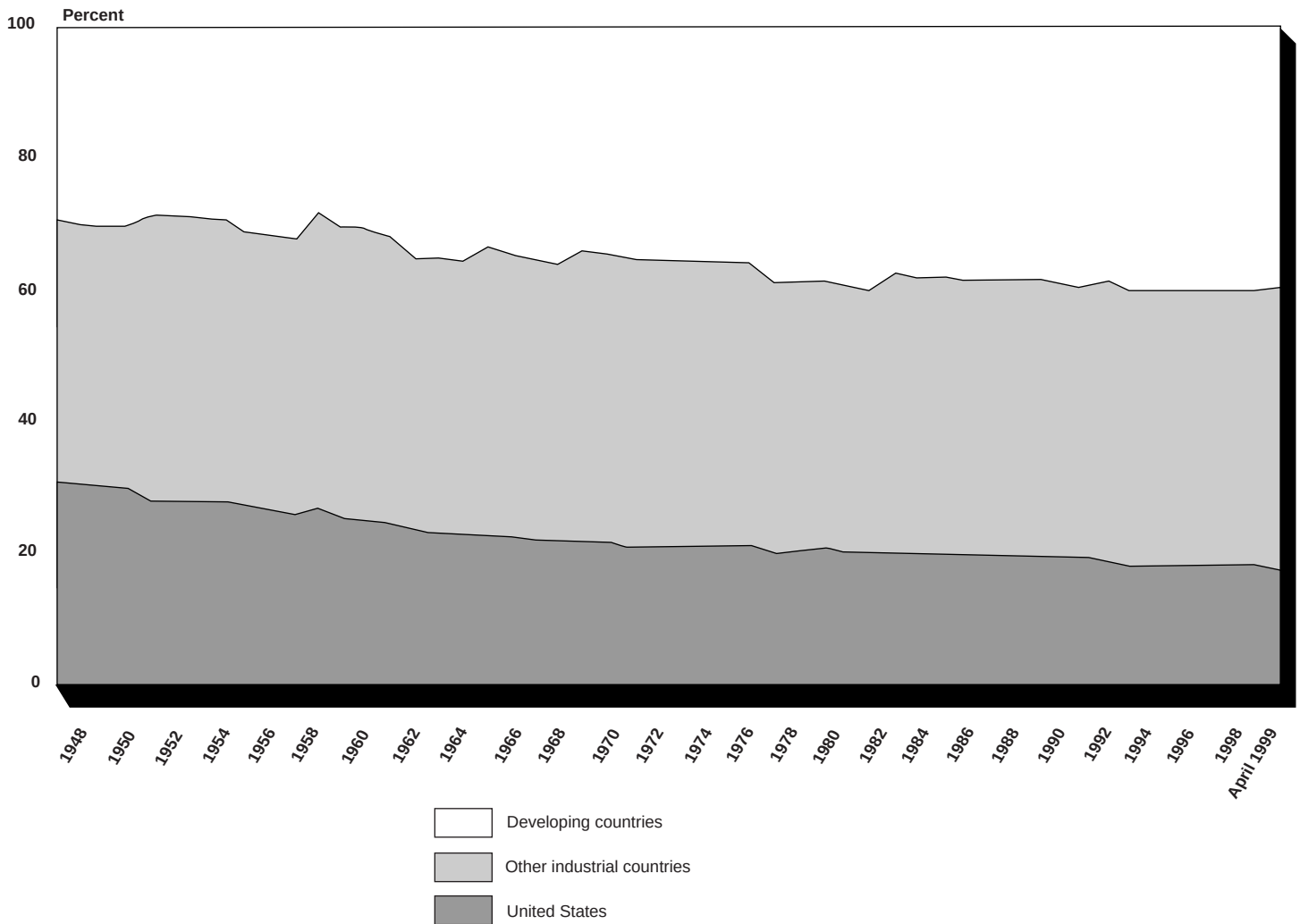
The Articles of Agreement often require 70 percent to 85 percent of the voting power of the IMF membership for approval of significant decisions. Certain decisions such as an increase in quotas or the sale of gold require an 85-percent vote of approval. Therefore, the United States can effectively veto these types of decisions based upon its voting shares. However, certain decisions, such as changing the interest rate paid by borrowers, only require a 70-percent vote of approval. The voting and quota shares of developing and transition countries have risen steadily throughout the IMF's history, increasing to 40 percent as of April 30, 1999. Thus, developing and transition countries may have sufficient voting power to

⁴In accordance with IMF's rules and regulations, the Executive Board rarely reaches decisions through formal votes, but instead works to reach a consensus among its members.

⁵The absolute size of the U.S. quota has increased from about \$2.8 billion in 1945 to the current amount of about \$50 billion. Other countries with large quotas include Japan and Germany (about \$18 billion each) and France and the United Kingdom (about \$14.5 billion each).

form a voting bloc and oppose certain decisions, such as the raising of the interest rate charged for the use of IMF resources.

Figure 7: IMF Member Voting Shares, 1948–April 30, 1999



Source: GAO analysis of IMF data.

The IMF's Lending Activities

From the IMF's first financial transaction from its GRA on March 1, 1947, through April 30, 1999, the IMF has disbursed about SDR 209 billion, or \$507 billion in constant dollars.¹ These resources were disbursed through reserve tranche drawings, 710 stand-by arrangements, and 67 extended arrangements. Since 1947, the IMF's lending has involved successively larger amounts of financing and reached about \$82 billion as of April 30, 1999. Additionally, the composition of industrial and developing country borrowers had changed so that by 1988, industrial countries were no longer users of IMF credit. As the IMF's lending shifted exclusively to developing countries, 15 members since 1983 have been unable to meet their obligations to the GRA when due.² In response to these arrears, the IMF has increased its reserves to consider potential loan losses and adopted a mechanism to share the cost of overdue obligations between debtor and creditor members. As of April 30, 1999, five members were in arrears to the GRA.

The Expansion of GRA Lending Arrangements and Facilities

Since 1947, the IMF has expanded the types of GRA lending arrangements and facilities to respond to demands by its members for increased credit and generally longer repayment terms. These lending arrangements and facilities consisted of the following nine types:

- *Stand-by arrangements*, used from 1952 to the present, are the most common form of IMF lending. Under these arrangements, members purchase currency primarily for short-term balance-of-payments assistance. Repayment terms were up to 5 years. Interest rates ranged from zero percent for the first 3 months to about 9.67 percent per year in 1985.
- *The Compensatory Financing Facility (CFF)* was available from 1963 to 1988 and was expanded in 1988 to the Compensatory and Contingency Financing Facility (CCFF). These facilities provided members experiencing shortfalls in export earnings or increased costs of cereal and oil imports with resources to purchase currency. Repayment terms were up to 5 years. Interest rates ranged from zero percent for the first 3 months to about 9.67 percent per year in 1985.

¹The IMF's reported amounts have been adjusted to 1998 dollars using an SDR price deflator and the average 1998 dollar/SDR exchange rate.

²An additional two members, Iraq and Afghanistan, are also in arrears to IMF's SDR Department.

- *The Buffer Stock Financing Facility (BSFF)* was available from 1969 to 1984. The BSFF provided currency purchases for members to reduce the variability of export earnings. Repayment terms were up to 5 years. Interest rates ranged from zero percent for the first 3 months to about 9.67 percent per year in 1985. All of these loans were repaid by 1988.
- *The Oil Facility* was available for one year in 1974 and again in 1975 to finance members' purchases of oil during the 1974-75 worldwide oil crisis. The IMF borrowed funds from several industrial and oil-producing members to finance this facility. Repayment terms were up to 7 years. Interest rates ranged from about 6.88 percent to 7.88 percent per year from 1974 to 1983. All of these loans were repaid by 1983.
- *The Extended Fund Facility (EFF)*, established in 1974, provides financing to members experiencing structural balance-of-payment problems. Under these extended arrangements, repayment terms are up to 10 years. Interest rates ranged from about 4 percent to 6.88 percent per year from 1977 to 1981. In 1983, the EFF interest rate became the same as that for regular facility loans, which have ranged from about 3.42 percent per year in 1999 to about 9.67 percent per year in 1985.
- *The Supplemental Financing Facility (SFF)* was available from 1979 through 1984 to provide financing for developing country members. The IMF borrowed resources from several industrial and developing members to fund the SFF. Repayment terms were up to 7 years. The SFF was phased out after other facilities, such as the SAF and the ESAF became available. Interest rates were up to about 0.33 percent higher than regular facility loans until 1984, when the SFF interest rate became the same as that for regular facility loans. All of these loans have been repaid except for countries in arrears as of April 30, 1999.
- *The Enlarged Access to Resources (EAR)* facility was available from 1981 to 1992 to provide additional financing to developing country members. The IMF borrowed resources to fund this facility from several industrial and developing members. Repayment terms were up to 7 years. This facility was phased out after other facilities, such as the SAF and the ESAF, became available. Interest rates were up to about 0.20 percent higher than regular facility loans until 1984, when the interest rate for the EAR facility became the same as regular facility loans.

-
- *The Systemic Transformation Facility (STF)* was available from 1993 to 1995 to provide funding to 28 countries to transition³ from centrally planned economies to market economies. Repayment terms were up to 10 years. Variable interest rates ranged from about 3.42 percent per year in 1999 to about 6.33 percent per year in 1993.
 - *The Supplemental Reserve Facility (SRF)* was created in 1997 in response to the Asian financial crisis. The SRF provides assistance to members experiencing exceptional balance-of-payment problems that could threaten the international monetary system. Repayment terms are very short-term as amounts are due from 1- to 2-½ years. Interest rates have been about 7 percent in 1998 and 8 percent in 1999.

As the GRA lending facilities have evolved, their repayment terms have expanded from up to 5 years for stand-by arrangements, the CFF, and the BSFF; to up to 7 years for the oil and EAR facilities and the SFF; and finally, up to 10 years for extended arrangements and the STF. The recent exception is the 1- to 2-½ year repayment terms of the SRF. Of the approximately \$82 billion of outstanding GRA credit as of April 30, 1999, 45 percent was under 5-year facilities, 32 percent was under 10-year facilities, 21 percent was under the 1- to 2-½ year SRF facility, and 2 percent was under 7-year facilities.

Some Members Have Been Regular Users of IMF Credit

Of the IMF's 182 member countries as of April 30, 1999, 137 members have made currency purchases and 45 members have never used IMF credit. Table 5 identifies 11 members that have been regular users of IMF credit for 20 years or more since 1947. The number of years and the period are noted for the longest and second longest periods of continuous borrowing. No industrial country has had currency purchases since 1985.

³The IMF considers 28 of its member countries to be countries in transition, consisting of 11 countries that comprised the former Soviet Union, 16 former Soviet bloc countries in Eastern or Central Europe, and Mongolia.

Table 5: IMF Members With 20 or More Years of IMF GRA Lending, Calendar Years 1947-98

Dollars in millions

Number	Country	Number of years of purchases	Cumulative purchases	Longest period	Second longest period
1	Philippines	30	\$9,870	12 (1970-81)	7 (1983-89)
2	Pakistan	25	7,906	12 (1972-83)	8 (1991-98)
3	Argentina	24	20,928	13 (1985-97)	5 (1959-63)
4	Turkey	24	8,374	7 (1978-84)	6 (1966-71)
5	Chile	23	7,625	7 (1983-89)	7 (1963-69)
6	Haiti	23	518	7 (1961-67)	5 (1980-84)
7	Sri Lanka	23	3,053	21 (1965-84)	1 (1988)
8	Jamaica	21	3,064	15 (1981-95)	4 (1976-79)
9	Mali	21	405	9 (1964-72)	5 (1982-86)
10	Bolivia	20	916	8 (1956-63)	3 (1971-73)
11	Sudan	20	2,879	7 (1978-84)	6 (1964-69)
Subtotal of 11 countries above		254	65,538		
Total all borrowers		1,219	\$394,159		

Note 1: Total does not include years of borrowing from the SAF/ESAF.

Note 2: Total of all borrowers includes purchases by Cuba, which is no longer an IMF member, and purchases by the former Yugoslavia that the IMF has allocated to the five successor countries, four of which have become IMF members. Serbia/Montenegro will owe the portion that the IMF has allocated to it when it becomes an IMF member.

Source: GAO analysis of IMF's *International Financial Statistics*.

The Evolution of Yields on Periodic Charges and Remuneration

A member borrowing funds from the IMF pays various charges to cover the IMF's operational expenses, including remuneration paid to the member whose currency is being borrowed. Presently, a borrower typically pays a service charge of one-half of 1 percent of the amount of each transaction at the time of disbursement, a commitment fee of one-quarter of 1 percent of an amount estimated to be drawn down annually,⁴ and periodic charges for interest. Under procedures in effect since May 1, 1981, the basic periodic charge rate is determined at the beginning of each financial year. The rate

⁴The commitment fee is payable upon agreement on an arrangement, but the fee is refundable as purchases are made.

includes an amount designed to allow the IMF to meet its annual administrative expenses and net income target and to remunerate members whose currencies have been purchased by other IMF members.

On May 1, 1989, the basic periodic charge rate was modified to be based on a proportion of the SDR interest rate and changes weekly with fluctuations in the SDR interest rate.⁵ For the fiscal year ended April 30, 1999, the proportion was set at 107 percent of the estimated SDR rate of 3.43 percent, or 3.67 percent. Added to this amount is a rate of 0.13 percent to cover potential loan losses under burden-sharing,⁶ for a total rate⁷ of 3.80 percent for all lending facilities except the SRF. When the first purchase is made under the SRF, an annual rate of charge of 300 basis points⁸ above the regular rate of charge for other IMF lending is assessed on purchases, as adjusted for burden-sharing. The rate increases by 50 basis points at the end of the first year and every 6 months thereafter, until it reaches 500 basis points.

Remuneration was not paid on gold tranche deposits prior to adoption of the second amendment of the Articles on April 1, 1978. Subsequently, the IMF established an unremunerated reserve tranche for each member that was equal to 25 percent of the member's quota before the second amendment.⁹ For countries that became members after April 1, 1978, an unremunerated reserve tranche position amount was fixed. This amount was based on the weighted average of the unremunerated reserve tranche to the quota of all other members on the date that the member joined the

⁵The SDR interest rate is determined by reference to a combined market interest rate, which is a weighted average of yields or rates of 3 month, short-term instruments in the capital markets of the five members whose currencies comprise the SDR.

⁶The additional charge to borrowers and lower remuneration paid to countries providing the funds is known as "burden-sharing." It was adopted by the IMF in 1986, and it is discussed further at the end of this appendix.

⁷While the yields for periodic charges and remuneration have been identified for each year, historical data was not available for calculating the weighted average of interest rates on the Fund's outstanding loan portfolio for each year since its first loan in 1947.

⁸100 basis points equal 1 percent interest.

⁹The IMF computes a remunerated reserve tranche position, which is effectively the complement of the unremunerated reserve tranche position. A detailed description of the methodology and an example is found in IMF, *Financial Organization and Operations of the IMF*, Pamphlet Series No. 45, fifth edition (Washington, D.C., IMF, 1998).

IMF. The IMF then pays interest on that part of a member's reserve tranche position in excess of the unremunerated reserve tranche position.

As quotas increase, the ratio of the unremunerated reserve tranche position to quota declines. For example, the unremunerated portion of the United States of about SDR 1.7 billion represented 25 percent of the U.S. quota subscription prior to April 1, 1978. This percentage has declined with subsequent quota increases. After the 1999 quota increase, the unremunerated portion of the United States represented about 4.5 percent of the U.S. quota. Since the IMF only pays remuneration to members on their remunerated reserve tranche position, some members have foregone significant amounts of interest income on such balances. For example, using the IMF's average remuneration rates, the United States has foregone about \$2.7 billion since 1980, or almost \$150 million annually on its unremunerated reserve tranche position.

The Evolution of Periodic Charges

A summary of GRA periodic charges paid by IMF members as a percentage of outstanding purchases since March 1947 follows.

- From 1947 to 1974, periodic charges were fixed at zero percent, for amounts outstanding less than 3 months, to a maximum of 5 percent for all borrowing.
- For 1975 to 1976, periodic charges ranged from a fixed amount of zero percent for amounts outstanding less than 3 months to 6 percent. Higher rates were charged by type of loan facility, to a maximum of about 7.88 percent for Oil Facility loans with a 7-year term.
- From 1977 to 1981, periodic charges were fixed from 4 percent to about 6.38 percent. Higher rates were charged by type of loan facility, to a maximum of about 7.88 percent for Oil Facility loans with a 7-year term.
- For 1982, periodic charges were fixed at 6.25 percent, and 1983 rates became variable, from about 6.60 percent to about 8.52 percent. Other rates were charged by type of loan facility, to a maximum of about 7.88 percent for Oil Facility loans with a 7-year term.
- Since August 1983, periodic charges from a low of about 3.42 percent for 1999 to a high of approximately 9.67 percent for 1985 have been determined weekly for all facilities based upon a proportion of the SDR interest rate, unadjusted for burden-sharing. Periodic charges for the SRF loans were about 7 percent in 1998 and 8 percent in 1999.

The Evolution of Remuneration

A summary of remuneration paid to members as a percentage of their remunerated reserve tranche position follows.

- From 1947 to 1969, remuneration was not paid to members.
- From 1970 to 1974, remuneration of 1.5 percent was paid.
- For 1975 and 1976, remuneration from a low of 1.5 percent to a high of about 5 percent was paid.
- From 1977 to 1981, remuneration from a low of about 3.5 percent for 1977 and 1978 to a high of about 9.79 percent for 1981 was paid quarterly, based upon 90 percent of a high SDR interest rate of about 10.88 percent.
- For 1982 and 1983, remuneration from a low of about 7.20 percent to a high of about 11.93 percent was paid quarterly, based upon 85 percent of a high SDR interest rate of about 14.03 percent.
- Since 1984, remuneration from a high of about 9.32 percent for 1990 to a low of about 3.43 percent for 1999 has been determined weekly, based upon 85 percent to 100 percent of the SDR interest rate, unadjusted for burden-sharing. The financial year 1999 average remuneration rate was set at the estimated SDR rate of 3.43 percent, less 0.15 percent to cover potential loan losses under burden-sharing, for a rate of 3.28 percent.

The Concentration of Fund Credit Has Increased Since 1983

As discussed in our letter, the share of the 10 largest users of IMF's GRA resources has steadily increased to 86 percent of total GRA credit as of April 30, 1999, the highest level since 1970. Table 6 identifies 25 members that have been among the 10 largest GRA borrowers from 1983 through 1999. Besides those remaining among the 10 largest borrowers as of April 30, 1999, 9 members have partially paid off their balances, and 6 members have fully paid off their balances. Additionally, 6 members have been among the 10 largest borrowers during this 17-year period for 9 or more years, or over half of the time.

Appendix IV
The IMF's Lending Activities

Table 6: The 10 Largest GRA Borrowers, 1983-99

Dollars in billions

Member	Number of years among the 10 largest borrowers	10 largest balances outstanding as of April 30, 1999	Members with partially paid-off balances as of April 30, 1999	Members with fully paid-off balances as of April 30, 1999
Algeria	6	\$1.8		
Argentina	17	4.9		
Brazil	11	9.5		
Chile	7			X
Czechoslovakia ^a	2		X	
Hungary	7			X
India	15		X	
Indonesia	2	9.2		
Korea	7	13.2		
Mexico	16	7.2		
Morocco	7			X
Pakistan	6		X	
Peru	5		X	
Philippines	12	1.6		
Poland	1			X
Romania	5		X	
Russia	7	17.5		
South Africa	1			X
Sudan	4		X	
Thailand	3	3.2		
Turkey	5		X	
Ukraine	4	2.7		
Venezuela	9		X	
Yugoslavia, SFR ^a	7		X	
Zambia	4			X
Total		\$70.8	9	6

Note: SDR exchange rate = \$1.35123 as of April 30, 1999.

^aThese member balances have accrued to successor countries.

Source: GAO analysis of IMF annual reports.

Arrears by Country Since 1983

Since 1983, there were 15 IMF members¹⁰ that were 6 months or more in arrears to the GRA. The arrears to the GRA started with 1 member in 1983, reached a high of 11 members in 1989, 1990, and 1993, and has decreased to 5 members from 1996 through April 30, 1999. Further, the IMF has determined members in arrears to be ineligible for additional GRA lending until their arrears have been cleared. As of April 30, 1983, one member was ineligible for additional GRA lending. The number of members in arrears that were ineligible for GRA lending increased to a high of 10 members by April 30, 1990. From 1996 through April 30, 1999, the number of ineligible members decreased to four. How these arrears developed, subsequent IMF actions, and the resolution of the arrears or its status as of April 30, 1999, are discussed in the following paragraphs:

- *Cambodia* (formerly Democratic Kampuchea before 1990) is a low-income developing country that began to experience protracted arrears in May 1975. The country also was experiencing political and civil unrest, and the government was operating under the auspices of the United Nations. In December 1978, the IMF's Executive Board, in accordance with the Articles of Agreement, declared the country ineligible for additional IMF lending. As of April 30, 1993, the country had arrears to the GRA totaling about \$34 million. In October 1993, Cambodia paid all of its arrears with assistance from a support group co-chaired by France and Japan, and according to the IMF, then became eligible for additional IMF credit.
- *Guyana* is a low-income developing country that began to experience protracted arrears in May 1983. In May 1985, the IMF's Executive Board declared the country ineligible for additional IMF lending. As of April 30, 1990, the country had arrears to the GRA totaling about \$125 million. In June 1990, Guyana paid all of its arrears with assistance from a support group chaired by Canada, and then became eligible for additional IMF credit.
- *Vietnam* is a low-income developing country that began to experience protracted arrears in February 1984. The country also faced bilateral economic sanctions from the United States. In January 1985, the IMF's Executive Board declared the country ineligible for additional IMF lending. As of April 30, 1993, the country had arrears to the GRA totaling about \$74 million. In October 1993, Vietnam paid all of its arrears with

¹⁰Includes remaining amounts of the former Yugoslavia pertaining to Serbia/Montenegro, which is not an IMF member.

assistance from a support group co-chaired by France and Japan and then became eligible for additional IMF lending.

- *Liberia* is a low-income developing country that began to experience protracted arrears in December 1984. In January 1986, the IMF's Executive Board declared the country ineligible for additional IMF lending. The country was also experiencing political instability and a civil war since 1989. Further actions by the IMF under its Strengthened Cooperative Strategy included issuance of a declaration of noncooperation in March 1990. As of April 30, 1999, the country had arrears to the GRA totaling about \$562 million and arrears to IMF's SDR Department and Trust Fund of about \$65 million. IMF's Executive Board has decided not to implement the next step of the strategy to suspend Liberia's voting rights because of the country's efforts to make regular monthly payments and to implement economic reforms.
- *Sudan* is a low-income developing country that began to experience protracted arrears in July 1984. The country has been experiencing political and internal instability and a civil war since 1983. In February 1986, the IMF's Executive Board declared the country ineligible for additional IMF lending. Further actions by IMF under its Strengthened Cooperative Strategy included issuance of a declaration of noncooperation in September 1990 and a suspension of the country's IMF voting rights in August 1993. A procedure for compulsory withdrawal of Sudan from the IMF was initiated in April 1994. However, this action has been deferred in light of Sudan's regular monthly payments and continued satisfactory implementation of a program of economic adjustments. As of April 30, 1999, the country had the largest and most protracted arrears to the GRA totaling \$1.4 billion and arrears to IMF's SDR Department and Trust Fund of about \$105 million. In August 1999, the IMF lifted the declaration of noncooperation and is considering reinstatement of the country's IMF voting rights.
- *Peru* is a middle-income developing country that began to experience protracted arrears in September 1985. The country was also experiencing political and internal instability. In August 1986, the IMF's Executive Board declared the country ineligible for additional IMF lending. As of April 30, 1992, the country had arrears to the GRA totaling about \$853 million. In March 1993, Peru paid all of its arrears with assistance from a support group co-chaired by Japan and the United States and bridge loans from both sponsors. Peru then became eligible for additional IMF lending.
- *Zambia* is a low-income developing country that began to experience protracted arrears in April 1985 due to adverse economic conditions. In September 1987, the IMF's Executive Board declared the country

ineligible for additional IMF lending. As of April 30, 1995, the country had arrears to the GRA totaling about \$1.3 billion. In December 1995, Zambia paid all of its arrears with the help of bridge loans from several IMF members and then became eligible for additional IMF lending.

- *Sierra Leone* is a low-income developing country that began to experience protracted arrears in January 1985. In April 1988, the IMF's Executive Board declared the country ineligible for additional IMF lending. The country was also experiencing political and internal instability and a civil war since 1992. As of April 30, 1993, the country had arrears to the GRA totaling about \$110 million. In March 1994, Sierra Leone paid all of its arrears with assistance from an informal donor group of major industrial nations and international financial institutions, and then became eligible for additional IMF lending.
- *Somalia* is a low-income developing country that began to experience protracted arrears in July 1985. The country was also experiencing political instability, a prolonged civil war, and a virtual cessation of a functioning government. In May 1988, the IMF's Executive Board declared the country ineligible for additional IMF lending. As of April 30, 1999, the country had arrears to the GRA totaling about \$250 million and arrears to IMF's SDR Department and Trust Fund of about \$20 million. According to the IMF, the Executive Board has not taken any further actions as political and economic conditions in the country are so disrupted that it has not been possible for IMF staff to conduct an assessment of the country's position.
- *Honduras* is a low-income developing country that began to experience protracted arrears in November 1987 due to adverse economic conditions. In November 1989, the IMF's Executive Board declared the country ineligible for additional IMF lending. As of April 30, 1990, the country had arrears to the GRA that totaled about \$29 million. In June 1990, Honduras paid all of its arrears with assistance from a consultative group chaired by the World Bank, and then became eligible for additional IMF lending.
- *Panama* is a middle-income developing country that began to experience protracted arrears in December 1987. In June 1989, the IMF's Executive Board declared the country ineligible for additional IMF lending. The country was also experiencing political and internal instability, including the December 1989 U.S. intervention in Panama (Operation Just Cause). As of April 30, 1991, the country had arrears to the GRA totaling about \$243 million. In early 1992, Panama paid all of its arrears with assistance from a support group chaired by the United States and through contributions from several governments, and then became eligible for additional IMF lending.

- *Congo, Democratic Republic of* (DRC, formerly Zaire before May 17, 1997) is a low-income developing country that began to experience protracted arrears in June 1988 and again in November 1990. Arrears of about \$141 million as of April 30, 1989, were cleared in 1990. However, arrears continued and in September 1991, the IMF's Executive Board declared the country ineligible for additional IMF lending. Further actions by the IMF under its Strengthened Cooperative Strategy included issuance of a declaration of noncooperation in February 1992 and a suspension of the country's IMF voting rights in June 1994. The country was also experiencing political and internal instability and a civil war since 1996. As of April 30, 1999, the country had arrears to the GRA totaling about \$477 million, and its arrears to IMF's SDR Department were about \$11 million. The IMF is considering initiating the procedure for compulsory withdrawal from the IMF unless the country resumes cooperation with IMF policy implementation and payments to the Fund.
- *Haiti* is a low-income developing country that began to experience various periods of protracted arrears in May 1988, November 1988, and November 1991. The country also faced international economic sanctions. As of April 30, 1994, the country had arrears to the GRA totaling about \$24 million. In December 1994, a support group contributed \$65 million in grants to clear Haiti's arrears to the Fund and other multilateral institutions. Haiti then became eligible for additional IMF lending.

In 1992, the Socialist Federal Republic of Yugoslavia was dissolved in the midst of conflict and the IMF allocated its Fund debts and resources to its five successor countries: Bosnia/Herzegovina, Croatia, Macedonia, Slovenia, and Serbia/Montenegro. As of April 30, 1999, the first four countries had become IMF members. In September 1992, Bosnia/Herzegovina and Serbia/Montenegro began to experience protracted arrears. Subsequently

- *Bosnia/Herzegovina* had protracted arrears to the GRA of about \$31 million as of April 30, 1995. In December 1995, Bosnia/Herzegovina cleared its arrears to the Fund with the help of a bridge loan from another IMF member.
- *Serbia/Montenegro* had protracted arrears to the GRA of about \$100 million, and arrears to IMF's SDR Department of about \$24 million as of April 30, 1999.

Additionally, two other members were in arrears to IMF's SDR Department for amounts owed for quarterly charges on their allocation of SDRs:

- *Iraq* has not made payments to the IMF due to international economic sanctions under United Nations Security Council Resolution No. 661, adopted August 6, 1990. As of April 30, 1999, this amounted to \$50 million.
- *Afghanistan* has not made payments of \$5 million as of April 30, 1999.

Precautionary Balances

International and U.S. accounting standards require lending institutions to estimate a provision for loan losses that reduces the amount of outstanding lending projected to be collectable, with a corresponding amount charged to operations as an expense. The IMF is not required to follow international, U.S., or the accounting standards of any country. According to the IMF, it has never established a provision for potential loan losses because the Fund

- technically does not make a loan as members purchase currencies from the IMF with an equivalent amount of their national currency;
- determined that it could not write off any currency holdings while a country is an IMF member;
- determined that potential losses were neither probable nor estimable;
- extends lending only to members; and
- had no losses historically, even for members that have left the IMF such as Cuba.

Rather than establish provisions for potential loan losses, the IMF decided to create the following accounts that it refers to as “precautionary balances,” which the Fund believes can be used to absorb any potential loan losses.

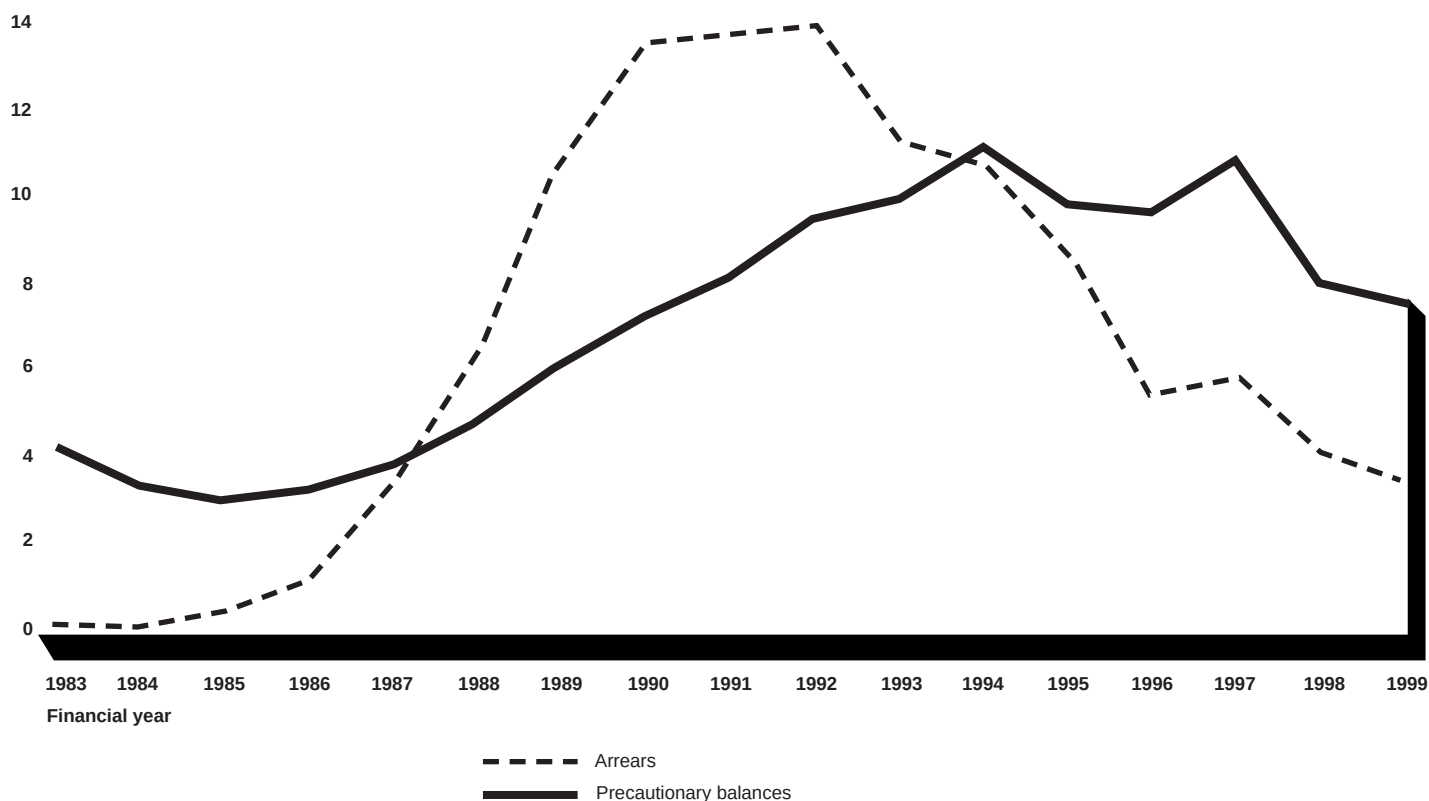
- *General and Special Reserves* are provided for in the Articles of Agreement. These reserves reflect the IMF's accumulated net income. General and Special Reserves totaled approximately \$1.1 billion in 1983 and increased to about \$3.5 billion as of April 30, 1999. No loan losses have been charged against these reserves.
- *Special Contingent Accounts* 1 and 2 (SCA-1, SCA-2) were established in 1987, and 1990, respectively. The amount in the SCA accounts totaled about \$2.7 billion as of April 30, 1999.

Precautionary Balances and Arrears

Since 1983, IMF's precautionary balances and arrears have experienced significant growth as a percentage of total GRA outstanding credit but have declined in recent years as indicated by figure 8.

Figure 8: IMF's Precautionary Balances and Arrears as a Percentage of Total GRA Outstanding Credit, 1983-99

16 Percent of outstanding GRA credit



Source: GAO analysis of IMF annual reports.

Specifically

- from 1988 through 1993, total arrears exceeded IMF's precautionary balances as a percentage of total GRA outstanding credit, until various IMF measures and financial support from certain countries reduced those amounts in arrears and

-
- the establishment of the SCAs contributed to the increase in total precautionary balances as a percentage of total GRA outstanding credit to absorb potential loan losses.

The Burden-sharing Mechanism

In 1986, the IMF developed a burden-sharing mechanism to share the potential cost of loan losses between borrower and creditor members. Under this mechanism, the IMF generated resources to (1) provide the Fund with interest revenue that was not paid by members in arrears to the GRA and (2) increase the balance of the two SCAs. For borrowers, the IMF increased the quarterly periodic charge for interest to include a calculated amount for the burden-sharing portion. For creditor members, the IMF calculated a reduction in the quarterly remuneration paid on such members' reserve tranche position, subject to a specific floor, for their burden-sharing portion.

Deferred Charges

Under the burden-sharing mechanism, IMF members have generated resources for deferred charges that totaled about \$1 billion as of April 30, 1999. Deferred charges represent foregone interest revenue for loans 6 months or more in arrears to the IMF. When all arrears are settled, this amount can be distributed to members that received reduced remuneration or paid higher charges.

SCA-1

Since the initial placement of about \$35 million in SCA-1 in 1987, the IMF has annually decided the size of SCA-1 additions before the beginning of each financial year. Under the burden-sharing mechanism, additions have amounted to 5 percent of the IMF's reserves at the start of each financial year. Balances in the SCA-1 are to be distributed to the members that shared the cost of financing when there are no outstanding overdue charges and repurchases, or at any earlier times, as the IMF may decide. As of April 30, 1999, the SCA-1 amounted to about \$1.3 billion.

SCA-2

On July 1, 1990, the Executive Board established a new cooperative strategy for burden-sharing that involved accumulating resources in SCA-2. This mechanism provided the IMF with additional liquidity to finance the

encashment¹¹ of rights following the completion of the rights accumulation program¹² by 11 eligible members. It also provided a safeguard against the risk of loss arising from currency purchases made in connection with the encashment of rights. As part of this new strategy, the IMF established a target to accumulate SDR 1 billion and further adjusted its rates of charge and remuneration whereby creditor and debtor countries contributed at a ratio of three to one. The SCA-2 account was fully funded at SDR 1 billion during 1997, for a total of about \$1.4 billion as of April 30, 1999. Refunds of SCA-2 contributions are to be made after all repurchases under the rights approach have been made (or at an earlier date as the IMF may decide.)

Burden-sharing Contributions by Members

As of April 30, 1999, the IMF reported that its members' burden-sharing contributions, net of refunds, had been about \$3.7 billion. The contributions have (1) strengthened the IMF's financial position by funding the foregone income it has not received from members with overdue obligations and (2) augmented its liquid resources by increasing IMF's precautionary balances. The quantitative effect of burden-sharing on IMF members is that creditor members, including the United States, have contributed about 60 percent through reduced remuneration, while debtor members have contributed about 40 percent through increased charges. The G-7, including the United States, are all creditor members. As of April 30, 1999, the G-7 had contributed a cumulative amount of about \$1.5 billion, or 41 percent of the net burden-sharing contributions. The United States had contributed about \$657 million, or about 18 percent of the net burden-sharing contribution, which was the largest percentage of all IMF members. Debtor members' cumulative burden-sharing contributions as of April 30, 1999, totaled about \$1.5 billion, which equaled the G-7 contributions.

The levels of protracted arrears in 1989 have declined steadily since the implementation of the rights accumulation programs and the SCA-2. As of April 30, 1999, 8 of the 11 members then in protracted arrears were current with the IMF due to their participation in the rights accumulation program and financial assistance from support groups.

¹¹To provide liquid resources when the members are considered eligible to receive the funds.

¹²This program allowed a member to accumulate rights to draw upon future Fund resources after clearing its arrears and is limited to the 11 members that were in protracted arrears to the Fund at the end of 1989.

Refunds of Burden-sharing Adjustments

Under the burden-sharing mechanism, it is the practice of the Executive Board to refund burden-sharing adjustments when countries in arrears settle amounts owed. These refunds have ranged from a low of zero for several quarters in the late 1980s to a high of about \$370 million for the quarter ended January 31, 1996, in nominal dollars. Through April 30, 1999, the United States had received remuneration refunds of about \$214 million, or about 33 percent of all remuneration refunds made by the IMF. The United States is still due a refund of about \$657 million for its total burden-sharing contributions, while other IMF members are due a total of almost \$3 billion.

The IMF's Borrowing and Credit Lines

The IMF has relied mainly on quota resources as its primary source of financing but has used borrowing and its credit lines from official sources¹ to supplement quotas when the level of its liquid resources were low. The IMF's Articles of Agreement permit borrowing from both official and private sources; however, as a matter of policy, the IMF has borrowed only from official sources. According to the IMF, this policy reflects the nature of the Fund as a cooperative, intergovernmental institution whose basic purpose is to facilitate the overall adjustment process by using some countries' surpluses to offset other countries' deficits in their balance-of-payments.

History of IMF Borrowing and Credit Lines

Borrowing has played an important role in providing temporary supplemental resources to the IMF since the early 1960s, particularly during the period of large payment imbalances that persisted from the early 1970s to the mid-1980s. Table 7 shows the relative share of borrowed resources used in financing IMF assistance to member countries from the time of its first borrowings in 1964 through April 30, 1999.

Table 7: IMF Outstanding Borrowing as a Percent of Outstanding IMF Credit 1964–April 30, 1999

1998 dollars in billions			
Year-end December	Outstanding IMF borrowing		
	Amount of outstanding IMF credit	Amount	As a percent of outstanding IMF credit
1964	\$10.1	\$ 2.8	27.7
1965	20.6	6.3	30.6
1966	20.0	7.8	39.0
1967	15.0	4.7	31.3
1968	22.5	7.9	35.1
1969	23.3	5.6	24.0
1970	17.8	4.1	23.0
1971	7.0	0	0

Continued

¹The official sources have included member countries and their central banks, one country that was not a member at the time the funds were borrowed (Switzerland) and its central bank, and the Bank for International Settlements.

Appendix V
The IMF's Borrowing and Credit Lines

1998 dollars in billions			
Year-end December	Outstanding IMF borrowing		
	Amount of outstanding IMF credit	Amount	As a percent of outstanding IMF credit
1972	5.4	0	0
1973	4.8	0	0
1974	15.9	7.1	44.7
1975	28.3	17.5	61.8
1976	44.1	22.9	51.9
1977	42.2	25.8	61.1
1978	30.7	19.1	62.2
1979	21.7	10.6	48.8
1980	20.9	10.4	49.8
1981	30.4	14.6	48.0
1982	41.3	17.6	42.6
1983	61.2	26.6	43.5
1984	68.6	27.7	40.4
1985	66.7	26.7	40.0
1986	61.3	24.8	40.5
1987	51.5	18.5	35.9
1988	43.1	11.5	26.7
1989	37.3	6.0	16.1
1990	33.3	5.8	17.4
1991	36.1	6.2	17.2
1992	35.8	5.2	14.5
1993	36.7	4.7	12.8
1994	36.7	4.2	11.4
1995	50.5	1.5	3.0
1996	50.2	0	0
1997	63.8	0	0
1998	82.0	5.9	7.2
April 30, 1999	81.6	0	0

Continued from Previous Page

Source: GAO analysis of IMF data.

Table 7 illustrates the continuous role of quotas in providing resources to the IMF. Borrowing and credit lines provided temporary financial support to IMF's operations during four periods.

- From 1964 to 1970, the IMF financed between approximately 23 percent and 39 percent of its outstanding GRA credit with borrowed resources from the General Arrangements to Borrow (GAB).
- From 1974 to 1986, the IMF financed between approximately 40 percent and 62 percent of its GRA credit with borrowed resources from the GAB and other agreements.
- The IMF's GRA credit financed with borrowed resources from the GAB and other agreements declined from 36 percent in 1987 to none in 1996 and 1997.
- In 1998, about 7 percent of the IMF's GRA credit was financed with borrowed resources from the GAB and the New Arrangements to Borrow (NAB). This amount was fully repaid in March 1999.

Since its inception, the Fund has entered into 11 borrowing arrangements or agreements, as shown in table 8.

Table 8: IMF Borrowing Arrangements and Agreements, 1962-98

Dollars in billions

Borrowing arrangement or agreement	Number of countries or central banks	Total amount of borrowing authority
Current borrowing arrangements:		
The GAB (1983) ^a	11	\$23.0
Associated borrowing agreement with Saudi Arabia (1983) ^b	1	2.0
The NAB (1998)	25	23.0
Past borrowing agreements:		
The GAB (1962-83) ^a	10	6.4
Oil facility (1974) ^c	7	3.4
Oil facility (1975) ^c	12	3.5
Supplemental Financing Facility (SFF) (1979-84)	14	10.1
Enlarged Access to Resources (EAR): Medium term (1981-87)		
Saudi Arabian Monetary Agency (SAMA)	1	9.4
Short term (1981)		
Bank for International Settlement (BIS) and others	19	1.5
Short term (1984)		
SAMA, BIS, Government of Japan, and National Bank of Belgium	4	6.2
Government of Japan (1986-91)	1	3.5

^aThe GAB was revised and enlarged in 1983.

^bUnder the associated borrowing agreement, Saudi Arabia will stand ready to lend Saudi riyals to the IMF up to an equivalent of about \$2 billion. These funds are to assist the IMF in the financing of currency purchases by members for the same purposes and in the same circumstances as are prescribed in the GAB

^cThe first Oil Facility was created in 1974 and was funded by seven entities. A second Oil Facility was created in 1975 and funded by 12 entities.

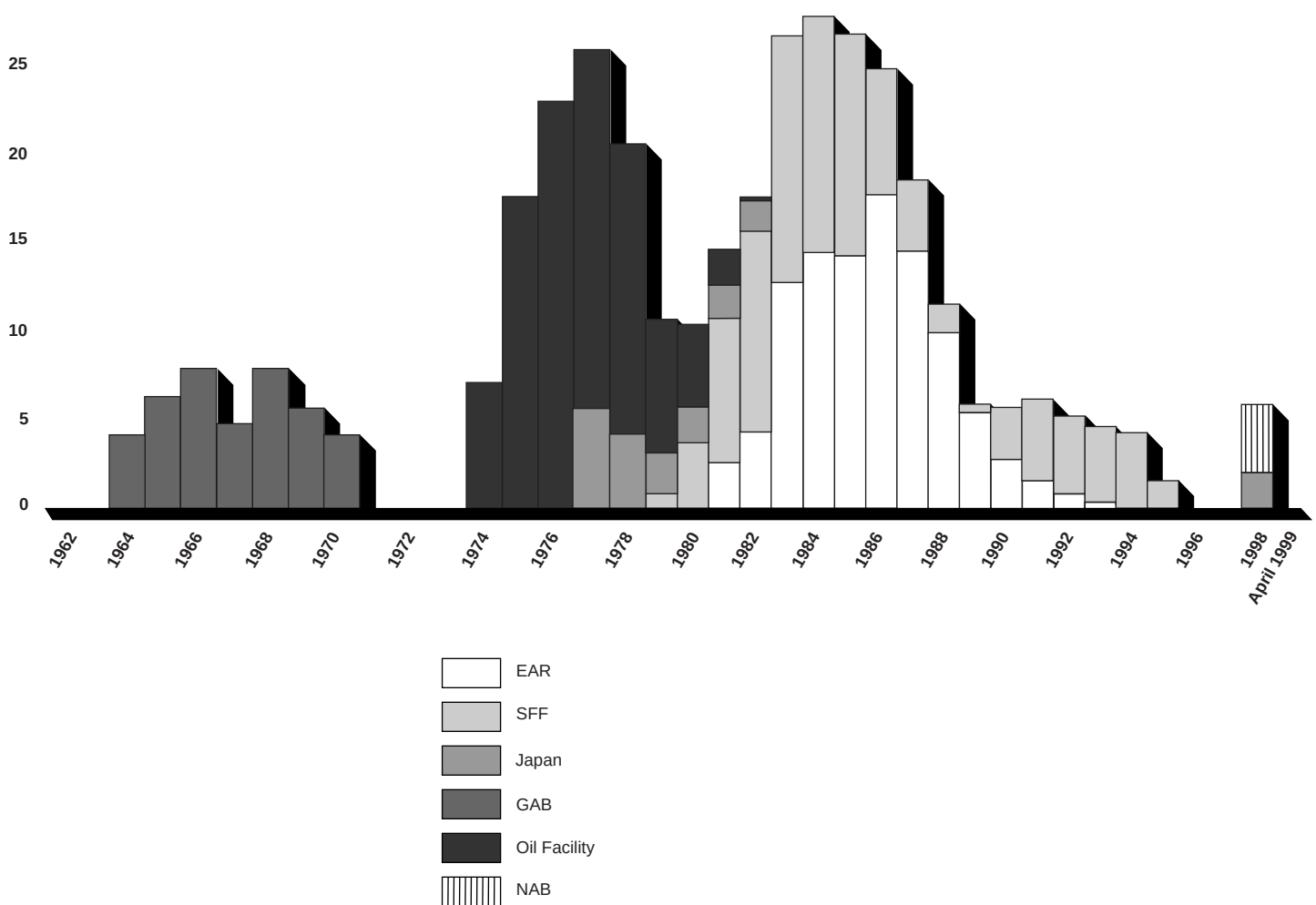
Source: GAO analysis of IMF data.

The IMF's 11 borrowing arrangements include 3 current credit lines from which it can borrow, with the 2 largest being the GAB, initially established in 1962, and the NAB, established in 1998. Amounts available under these credit lines have expanded from \$6 billion under the GAB in 1962 to the combined total of the GAB and the NAB of about \$46 billion as of April 30, 1999. Additionally, another \$2 billion is available under an associate credit agreement with Saudi Arabia.

The IMF's eight past borrowing agreements were used to finance lending under the GAB in 1962 and the Oil Facility, SFF, and EAR facilities, as discussed in appendix IV. In addition, the IMF borrowed from the government of Japan under an agreement that began in 1986, with drawings terminating in 1991. Figure 9 illustrates the IMF's borrowing sources and trends since the establishment of its first borrowing arrangement in 1962 through its most recent borrowings under the GAB and the NAB in 1998.

Figure 9: Outstanding IMF Borrowing, 1962–April 30, 1999

30 Billions of 1998 dollars



Source: IMF's International Financial Statistics.

The GAB

The GAB was originally conceived and designed as an arrangement whereby 11 of the main industrial countries agreed to strengthen the IMF's financial position by standing ready to loan the Fund up to specified amounts of their respective national currencies. These loans could be made when the IMF needed supplemental resources to help forestall or cope with an impairment of the international monetary system.

The potential amount of credit under the GAB totaled about \$6 billion (in lenders' currencies) from its inception until December 1983. In response to the growing pressure on the IMF's usable currencies caused by the Latin America debt crisis in mid-1982, the amount of credit available under the GAB was enlarged to about \$23 billion, with an additional \$2 billion associate credit agreement with Saudi Arabia. Table 9 shows a listing of current GAB participants and credit amounts.

Table 9: GAB Participants and Credit Amounts, as of April 30, 1999

Dollars in millions	
Participant	Amount
United States	\$5,743
Deutsche Bundesbank	3,216
Japan	2,871
France	2,297
United Kingdom	2,297
Italy	1,493
Swiss National Bank	1,378
Canada	1,206
Netherlands	1,149
Belgium	804
Sveriges Riksbank	517
Total	\$22,971
Associate credit agreement with Saudi Arabia	\$2,027

Note: SDR exchange rate = \$1.35123 as of April 30, 1999.

Source: IMF.

At the time of the GAB's enlargement in 1983, the interest rate was raised from below market levels used in the earlier GAB, to 100 percent of the

SDR interest rate. Since its inception, the GAB has been activated 10 times, with total drawings of about \$7.2 billion.

- From 1964 through 1970, the GAB was activated six times, primarily for drawings by the United Kingdom for balance-of-payments assistance. Total amounts borrowed by the IMF under the GAB activations were about \$2.2 billion. All of these borrowings have been repaid.
- In 1977, the GAB was activated twice for drawings by the United Kingdom and Italy, and once in 1978 by the United States for reserve tranche purchases for balance-of-payments assistance. Total amounts borrowed by the IMF under the GAB activations were about \$3 billion. All of these borrowings have been repaid.
- In July 1998, the GAB was activated for the 10th time for about \$2 billion drawn as part of an extended arrangement with Russia totaling about \$8.4 billion. This was the first activation of the GAB in 20 years, and the first time it has been used for a non-participant. This activation was canceled in March 1999 when the IMF repaid the \$2 billion shortly after it received funds from the recent Eleventh General Review's quota increase.

The NAB

Following the Mexican financial crisis in 1994-95, IMF members were concerned that substantially more resources might be needed by the IMF to respond to future financial crises. This concern prompted the G-10 and other financially strong countries to develop financing arrangements that would double the amount available under the GAB. The NAB is a set of credit arrangements between the IMF and 25 members and institutions established in November 1998. The NAB is available to provide supplemental resources to the IMF to forestall or cope with an impairment of the international monetary system or to deal with an exceptional situation that poses a threat to the stability of that system.

Funds available under the GAB are also available under the NAB, and together they constitute a combined credit line of about \$46 billion available for lending. The NAB can be activated when eligible participants representing 80 percent of the total credit arrangements determine there is a threat to the international monetary system and agree to the request. The NAB became effective in November 1998 for 5 years and may be renewed. A list of NAB participants and their credit arrangements is shown in table 10.

Appendix V
The IMF's Borrowing and Credit Lines

Table 10: NAB Participants and Credit Amounts, as of April 30, 1999

Dollars in millions	
Participant	Amount
United States	\$ 9,070
Deutsche Bundesbank ^a	4,807
Japan ^a	4,807
France ^a	3,482
United Kingdom ^a	3,482
Saudi Arabia ^a	2,405
Italy ^a	2,394
Swiss National Bank ^a	2,104
Canada ^a	1,887
Netherlands ^a	1,778
Belgium ^a	1,307
Sveriges Riksbank ^a	1,161
Australia	1,095
Spain	908
Austria	557
Norway	518
Denmark	501
Kuwait	466
Finland	459
Hong Kong Monetary Authority	459
Korea	459
Luxembourg	459
Malaysia	459
Singapore	459
Thailand ^a	459
Total	\$45,942

^aAlso a participant in, or associated with the GAB.

Note: SDR exchange rate = \$1.35123 as of April 30, 1999.

Source: IMF.

The activation requirements for the NAB are not as strict as the requirements for the GAB. Specifically, the credit arrangements under the NAB may be activated for the benefit of an IMF member that is a participant or non-participant in the NAB, under circumstances similar to

those specified in the GAB. However, under the NAB, activation for a non-participant is not subject to more stringent criteria related to the IMF's liquidity situation. Nevertheless,

- the maximum combined amount drawn under the GAB and the NAB cannot exceed SDR 34 billion (about \$46 billion as of April 30, 1999); and
- the NAB will be the facility of the first and principal recourse in the need to provide supplementary resources to the IMF except that (1) in the event of a request for drawing on the IMF by a participating member (or a member whose institution is a participant) in both the GAB and the NAB, a loan request may be made under either the GAB or the NAB and (2) in the event that a loan request under the NAB is not accepted, the request may be made under the GAB.

In December 1998, the NAB was first activated for about \$4 billion drawn on an extended arrangement with Brazil totaling about \$18.3 billion. This activation was canceled in March 1999 when the IMF repaid the \$4 billion shortly after it received funds from the recent Eleventh General Review's quota increase.

Objectives, Scope, and Methodology

As required under the Omnibus Appropriations Act for fiscal year 1999, we are reporting on several matters relating to the IMF's financial operations. In this report, we reviewed the IMF's

- liquidity position as of April 30, 1999, including the Fund's experience with borrowed resources to meet its members' financing needs;
- gold holdings and its role in the IMF's financial operations; and
- process for determining the amount of quota contributions required from its members.

We also included information on how the IMF's lending activities have evolved since the Fund was founded in 1945. In addition, we discussed the status of preparedness of the IMF's mission-critical and key computer systems for the year 2000.

The scope of our work had the following limitations:

- Although we obtained the U.S. Executive Director's position papers pertaining to quota reviews, we did not have access to nonpublic statements of the other IMF executive directors, the Executive Board minutes, or information on how final quota decisions were reached by the IMF's Executive Board.
- With the agreement of Committee staff, our review of the IMF's lending did not include facilities for low-income members and administered accounts that included various trust accounts that operated from 1976 to 1986, the Structural Adjustment Facility that was established in 1986, and the Enhanced Structural Adjustment Facility that was established in 1987. Outstanding loans under these facilities amounted to about \$8.8 billion as of April 30, 1999, and were discussed in a previous GAO report.¹
- Historical data was not available for calculating the weighted average of interest rates on the Fund's lending portfolio for each year since the Fund's inception, as the Omnibus Appropriations Act requested.
- An evaluation of the IMF's efforts and related management structure and processes to address the year 2000 problem was not within the scope of our work.

¹See *Developing Countries: Status of the Heavily Indebted Poor Countries Debt Relief Initiative* (GAO/NSIAD-98-229, Sept. 30, 1998).

Our work also included numerous interviews with IMF officials and U.S. Treasury officials and a meeting with the Fund's certified public accounting firm. Much of the information reported is as of April 30, 1999, the end of the IMF's financial year, and to the extent possible, we used data audited by the IMF's auditors. Additionally, to meet our objectives, we did the following:

- To review the IMF's liquidity position as of April 30, 1999, we reviewed the IMF's approach for calculating and reporting on its liquid resources and analyzed the reported amount of its liquid resources to determine whether adjustments the IMF made to the reported amount were practical and relevant. This included reviewing the various components that have evolved to determine the IMF's liquidity position as of April 30, 1999; the IMF's quarterly operational budgets and semiannual review papers on the Fund's liquidity and financing needs; and the IMF's methodology used in its reviews of liquidity and financing needs. In addition, we reviewed the Fund's documentation to determine if there was an analytical basis to support the liquidity ratio threshold that the IMF uses to determine when it is imprudent to lend. We also queried IMF officials about their rationale for the liquidity ratio percentage used as a minimum threshold for its lending activities.

We also analyzed the IMF's experience with borrowed resources, including its use of credit lines, to identify the amounts and periods, financing arrangements, and participants. This analysis included a ratio and trend analysis of the circumstances that led the IMF to borrow from its GAB, NAB, and other financing arrangements and agreements. In our work, we (1) reviewed the Fund's annual reports, which included its audited financial statements, books on the history of the Fund, and papers on the IMF's financing needs and (2) analyzed the IMF's data base of *International Financial Statistics* on outstanding borrowing.

- To review the IMF's gold holdings and its role in IMF's financial operations, we reviewed the history of IMF's acquisition and use of gold from 1946 to the present period, and conducted a detailed review of the Fund's governing principles and explanations for holding gold. We compared the Fund's policies to evolving gold management practices by several other official holders of gold and analyzed gold acquisition and use data over the history of the Fund's operations. We reviewed historical accounts and related IMF documentation that described the evolution of gold management practices. We also reviewed published reports on alternative uses for gold and the evolving nature of gold management practices. Finally, we discussed all of these issues with

Fund staff from the Treasurer's office and gold experts from the U.S. Treasury, two U.S. mining companies, the World Gold Council, and the Gold Institute.

- To review the IMF's process for determining quota contributions from members, we obtained and reviewed the Fund's policies and procedures supporting its quota increase from the Eleventh General Review in 1999. We also reviewed information on the quota review and more general information on 11 other quota reviews since 1950. In our review, we gained an understanding of the quantitative and qualitative factors the IMF takes into consideration to determine a quota increase. These factors included (1) if and when a quota increase is needed, (2) the size of a quota increase, (3) how the quota increase was distributed among member countries, and (4) what formulas were used to calculate members' quotas. In doing so, we reviewed the U.S. Executive Director's position papers pertaining to quota reviews. We also reviewed the IMF's (1) documents on the official Committee of the Whole on Review of Quotas for the Eleventh General Review, (2) semiannual review papers on liquidity and financing needs, (3) annual reports, (4) the IMF pamphlet, *Financial Organization and Operations of the IMF*, and (5) historical publications. In addition, we queried IMF officials and the U.S. Executive Director to obtain their comments on the IMF's quota review process.
- To review the evolution of the IMF's GRA lending activities since the first transaction in 1947, we identified the types and terms of lending facilities, regular users of IMF credit, and the 10 largest users of IMF credit. We also reviewed the evolution of yields on periodic charges and interest remuneration, members in arrears, the funding of precautionary balances, and the effect of the burden-sharing mechanism on the Fund's financial operations and on its members. To conduct our review, we analyzed the IMF's (1) data base of *International Financial Statistics*; (2) annual reports from 1947, which included audited financial statements; (3) key publications, including its *Articles of Agreement of the International Monetary Fund* and *Financial Organization and Operations of the IMF*; (4) various policy documents and staff position papers; and (5) data on financial transactions for member countries. We also discussed the Fund's lending activities with IMF officials, the U.S. Executive Director, and the Fund's certified public accounting firm to gain an understanding of the GRA lending activities.
- To review the status of preparedness of the IMF's mission-critical computer systems for the year 2000, we reviewed information from IMF's web site and held discussions with Fund officials and the IMF's certified public accounting firm. We met with IMF's Management

Information Systems specialists and discussed the Fund's status for testing its mission-critical computer systems and developing and testing its contingency plans. We also queried other IMF officials about the status of its members' year 2000 readiness and the potential impact on the IMF's operations if the members were not compliant. Additionally, we met with the Fund's certified public accountants for their assessment of the IMF's year 2000 readiness.

We conducted our review between December 1998 and August 1999 in accordance with generally accepted government auditing standards.

GAO Contacts and Staff Acknowledgments

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Appendix VII
GAO Contacts and Staff Acknowledgments

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