REPORT TO CONGRESS ON WAYS TO IMPROVE THE EFFECTIVENESS OF THE IMF AND MITIGATE RISKS TO U.S. PARTICIPATION

United States Treasury

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Contents

I. Preface

The Consolidated Appropriations Act, 2016, requires the Secretary of the Treasury to report on ways to improve the effectiveness, and mitigate the risks, of U.S. participation in the International Monetary Fund (IMF). Specifically, the Act requires Treasury to provide:

1. An analysis of recent changes to the surveillance products and policies of the IMF and whether these effectively address the shortcomings of surveillance by the IMF in the periods preceding the global financial crisis and the European sovereign debt crisis.
2. A discussion of ways to better encourage countries to implement policy recommendations of the IMF including:
    - Whether implementation would improve if the IMF provided regular status reports on implementation, and
    - Whether or not IMF lending should be limited to countries that have taken steps to implement policy recommendations.
3. An analysis of the transparency policy of the IMF, ways that transparency policy can be improved, and whether such improvements would be beneficial.
4. A detailed analysis of the riskiness of exceptional access loans provided by the IMF including:
    - Whether the interest rate surcharge is working as intended to discourage large and prolonged use of IMF resources, and
    - Whether it would be beneficial for the IMF to require collateral when making exceptional access loans, and how requiring collateral would affect the make-up of exceptional access loans and the demand for such loans.
5. A description of how the classification of IMF loans has changed following the implementation of the 2010 quota and governance reforms, including the effect on the classification of outstanding exceptional access loans.
6. A discussion and analysis of lessons learned from the lending arrangements that included the IMF, European Commission, and the European Central Bank during the European sovereign debt crisis.
7. An analysis of the risk or benefits of increasing the transparency of technical assistance projects of the IMF, including:
    - The advantages and disadvantages of the current disclosure policies,
    - How IMF technical assistance could be better used to prevent crises from happening in the future, and
    - Whether and how the IMF coordinated technical assistance projects with other organizations, including the U.S. Treasury Department, to avoid duplication of efforts.

II. Executive Summary

The United States and other founding members created the IMF to promote the stability of the international monetary system. The IMF fulfills this obligation through three main functions: surveillance, financial assistance to member countries, and technical assistance. As one of the chief architects of the IMF and its largest shareholder, the United States is committed to maintaining the effectiveness of the IMF. The U.S. Treasury Department works closely with the U.S. Executive Director's office at the IMF to promote U.S. policy priorities and improve the functioning of the IMF to minimize risk to the United States and promote a stable international monetary system.

Surveillance is at the core of the IMF's mandate and is critical to the IMF fulfilling its missions of promoting economic growth, facilitating external sector adjustment, and assisting members in addressing balance of payments difficulties. Since the global financial crisis, the IMF has taken substantial steps to enhance its surveillance. It has established an Early Warning Exercise to consider tail risks facing the global economy. It has strengthened its financial sector and external sector surveillance. Looking forward, Treasury will continue to press the IMF to incorporate clear and candid assessments of the external sector into its surveillance and to keep its surveillance tightly focused on its core mandate.

The IMF can most effectively fulfill its mission when it provides relevant policy advice that has a positive influence on member country policy decisions. The IMF has taken steps to strengthen the implementation of its policy recommendations through incorporating scorecard assessments of actions taken to address past recommendations. This is done at the bilateral level through the annual country surveillance reports and on a multilateral basis through the Managing Director's semi-annual Global Policy Agenda.

The IMF provides financial assistance to countries with balance of payments needs, supporting the implementation of adjustment policies and reforms that will restore conditions for strong and sustainable growth, employment, and social investment. Before receiving a loan, a country must commit to undertake reforms to restore economic stability and sustainability. The IMF has taken steps with U.S. support to examine its lending practices by drawing lessons from previous crises to provide better targeted and flexible lending. An analysis in 2012 by IMF staff found conditionality in lending programs has become better tailored to individual country needs, more streamlined, and more tightly focused on core areas of IMF expertise than in the past. Based on reviews of the IMF's experience with crisis cases in the euro area, Treasury believes that IMF lending played an essential role in mitigating risks of spillover to the global economy, but there are a variety of lessons from the IMF's experience, including on the pace of reforms and financing contributions.

The IMF provides technical assistance and training to help member countries build capacity in key areas of economic policy-making and management, including central banking, monetary and exchange rate policy, tax policy and administration, anti-money laundering and counter-terrorist financing, and official statistics. Much of this work is financed by donors. The IMF has worked in recent years to improve the coordination of its technical assistance with that of other TA providers.

Transparency in IMF advice and practices is key to improving accountability across all three main avenues of the IMF's work (surveillance, lending, and technical assistance). IMF transparency has increased substantially over the past two decades, from publication of verbatim transcripts of Board discussions to publication of country economic data and greater sharing of IMF technical assistance reports with other donors to promote coordination. Treasury continues to look for ways to enhance transparency while preserving the candor required in IMF discussions with member states.

Implementation of the IMF's 2010 quota and governance reforms in February 2016 was an important milestone for the IMF, strengthening the IMF's core resources and the legitimacy of the IMF's governance by better reflecting current weights in the global economy. These reforms reinforced the central role of the IMF in the international monetary system, and the leadership role of the United States as the largest shareholder in the IMF. Since access to IMF resources is linked to the size of a country's IMF quota, following the quota reform, the IMF adjusted its access limits in a way that prevented any country from experiencing a decline in access.

III. Report

1. Changes to IMF Surveillance in the Aftermath of the Global Financial Crisis

The IMF's bilateral and multilateral surveillance aims to encourage policies that contribute to global growth and financial stability and discourage policies that are not sustainable or have harmful spillover effects on other countries. The IMF's economic surveillance work is comprised of country reviews (known as Article IV reviews)[1], financial sector assessments, and regional and global reviews that focus on a range of topics. The IMF periodically reviews its overall surveillance through the Triennial Surveillance Review (TSR) and through separate reviews of the Financial Sector Assessment Program (FSAP). The IMF updates and adds to the range of reports and analytic tools it uses in surveillance, as circumstances warrant. As a result of the global financial crisis, the United States and other IMF shareholder pressed the IMF to strengthen its surveillance most notably in the financial sector but in other aspects as well. Internal reviews, including a report by the IMF's Independent Evaluation Office (IEO) in 2011, and a review by the G-20 helped inform steps to strengthen IMF surveillance.

In November 2008, G-20 Leaders called on the IMF and the Financial Stability Forum, which is now the Financial Stability Board (FSB) to collaborate in conducting Early Warning Exercises (EWE). The IMF and FSB launched the first official EWE in October 2009. The EWE is designed to strengthen assessments of systemic, low probability, high impact risks to the global outlook, and identify possible mitigating actions. The exercise integrates macroeconomic and prudential perspectives on systemic risks. It draws on analytical work, market information, and consultations with market participants, academics and country authorities. The IMF undertakes the EWE on a semi-annual basis and, following discussions by the IMF Executive Board and the FSB Plenary, presents the findings to senior International Monetary and Financial Committee (IMFC) officials during the IMF's spring and Annual Meetings.[2] Information discussed at the EWE is not made available to the public but is used to inform risk analysis and surveillance by the IMF.

IMF staff analysis of the fiscal response to the global financial crisis led to the creation of the *Fiscal Monitor,* a semi-annual publication that analyzes key public finance developments and provides medium-term fiscal projections for member countries. The *Fiscal Monitor* also examines policies to address near-term challenges as well as to put public finances on a medium-term sustainable path. The April 2016 *Fiscal Monitor*, for example, examined the use of fiscal policy to promote innovation and boost productivity growth.

The 2011 Triennial Surveillance Review (TSR) examined weaknesses in pre-crisis surveillance and suggested improvements. Recommendations to enhance surveillance included:

- Regularly analyzing spillovers and cross-country issues;
- Conducting in-depth risk assessments in bilateral and multilateral surveillance products;
- Publishing assessments of external balances; and

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[1] The obligation for IMF member countries to cooperate with the IMF on surveillance of their economies is contained in Article IV of the IMF's Articles of Agreement.
[2] The IMFC was created to advise the IMF Board of Governors. It is comprised of 24 members who represent the 189 governors of the IMF. Its structure mirrors that of the Executive Board and its 24 constituencies.

- Improving financial sector surveillance.

As a result of the 2011 TSR, the IMF Executive Board adopted a new Decision on Bilateral and Multilateral Surveillance in 2012. This decision: expanded the scope of Article IV consultations to include cross-country spillovers, including those generated by domestic policies; incorporated financial stability into the range of issues to be examined in assessing the stability of the international monetary system; and provided broader guidance on members' obligation related to domestic economic and financial policies and their spillover effects.

The IMF incorporated spillover analysis in Article IV reports and in an annual Spillover Report. The United States welcomed the integration of spillover analysis in the Article IV reports. The United States also pushed for an integration of the spillover analysis in the existing IMF publications, notably the *World Economic Outlook* (WEO). In 2015, IMF management decided to cease publication of the standalone report and began incorporating spillover analysis more systematically into the WEO.

The 2011 TSR found that the IMF's risk focus was uneven. To address this in Article IV reports, the IMF began including a risk assessment matrix that examined key domestic and global risks facing a country, the expected effects and policy recommendations to address the risks. (See Attachment 1 for an example of an Article IV risk assessment matrix.) The IMF also expanded coverage of risks in its flagship publications, the WEO and the Global Financial Stability Report (GFSR).

The United States has long pressed the IMF to improve its external sector surveillance and the transparency of its exchange rate analysis. As a significant outcome of the 2011 TSR, the IMF developed an External Sector Report (ESR) in 2012. The ESR provides much greater in-depth coverage of IMF exchange rate assessments, as well as assessments of reserves, the drivers of current account imbalances, and provides information on capital flows and measures. Consistent with U.S. recommendations, the IMF elevated the ESR in 2015 from a "pilot" to a permanent annual publication that currently covers the 29 largest economies.

As part of the development of the ESR, the IMF updated and strengthened its methodology for assessing exchange rates and current account balances on a multilateral basis. Moreover, the IMF published not only the methodology but also the data and assessments for 25 countries. This External Balance Assessment (EBA), published annually along with the ESR, was a major step forward in IMF transparency. The IMF also updated its analysis of foreign exchange reserves, developing and publishing a new methodology to assess the adequate level of reserves for emerging market and developing countries.

Given the key role the financial sector played in causing and transmitting the global crisis, the IMF has examined ways to improve its surveillance of the financial sector within and across countries. Following a 2009 review, the IMF adopted changes to strengthen the Financial Sector Assessment Program (FSAP) in response to the global financial crisis. The IMF established the FSAP in 1999 as a voluntary program providing a comprehensive and in-depth analysis of a country's financial sector. The IMF and World Bank jointly conduct FSAP assessments for emerging market and developing economies and the IMF conducts FSAPs for advanced economies. The IMF and World Bank review the FSAP program as a whole every five years. The 2009 FSAP review led the IMF to introduce a financial Risk Assessment Matrix with greater emphasis on crisis preparedness, and to develop methodologies to assess macro-prudential risks. In September 2010, the IMF Executive Board made it mandatory for jurisdictions with systemically important financial sectors to undergo FSAP assessments every five years. The 2014 FSAP review recommended ways to facilitate further integration of FSAP findings and recommendations into Article IV surveillance.

The 2014 TSR focused on areas highlighted by the 2011 TSR with particular attention to risk and spillover analysis. The 2014 TSR called for greater integration of bilateral and multilateral surveillance, recommended strengthening external sector assessments by gradually applying the EBA model to a broader set of countries, and undertaking a comprehensive assessment of the external position beyond just the exchange rate in Article IV reports. The TSR also recommended including a discussion of the contribution of domestic policies to external imbalances. Incorporating more countries into the EBA model was problematic given the lack of available data for all indicators in the model. To address this problem IMF staff developed an EBA-lite methodology that incorporates key aspects of the EBA model with a smaller set of variables. This has provided a more consistent methodology for exchange rate and current account analysis for about 150 economies. Analysis of exchange rates is now more consistently applied in the Article IV reports.

2. Encouraging Countries to Implement IMF Policy Recommendations

IMF surveillance aims to identify risks to the global and member economies as well as identify policy responses to mitigate those risks. Some multilateral surveillance incorporates a status update on past IMF policy recommendations. In the multilateral realm, the IMF's Managing Director presents a Global Policy Agenda twice a year to the Executive Board and the IMFC. This includes a scorecard of priority policy actions for advanced, emerging and developing countries undertaken in the previous six months, and where further effort is needed. The IMF also presents Surveillance Notes to the G-20 finance ministers and central bank governors meetings which includes recommendations for policy action by G-20 countries. The IMF also works closely with the FSB to identify risks, most notably through the EWE discussed above

On a bilateral basis, the Article IV process is the IMF's primary means for regular policy discussions and recommendations. IMF staff economists continually monitor members' economies. They visit member countries—usually annually—to exchange views with the government and the central bank and consider whether there are risks to domestic and global stability that argue for adjustments in economic or financial policies. Based on these discussions, staff submits an "Article IV report" for each member to the IMF Executive Board, which meets to discuss the staff's analysis and recommendations. The IMF publishes a summary of the Board's assessment on the IMF website shortly after the Board meeting. Nearly all member countries also permit publication of the Article IV report and any "Selected Issues" papers, which provide a more in-depth analysis of key issues relevant to the member's economy.

Bilateral surveillance now includes a status update of past IMF policy advice. In 2014, IMF staff began incorporating an annex in the Article IV reports on policy advice from the previous Article IV report. The annex provides the policy actions that countries have implemented in response to the IMF's policy recommendations, and highlights areas that countries have yet to address. This implementation report provides a convenient way for the IMF, Executive Board members, country authorities, and the public to examine the degree to which member countries are taking actions to implement policy advice. (See Attachment 2 for an example of an Article IV policy implementation scorecard assessment.)

The FSAP process is also a way for IMF staff to analyze potential risk factors facing a member and make policy recommendations. The FSAP provides a comprehensive and in-depth assessment of a country's financial sector. FSAPs analyze the resilience of the financial sector, the quality of the regulatory and supervisory framework, and the capacity to manage and resolve financial crises. Based on its findings, FSAPs produce policy recommendations of a micro- and macro-prudential nature, tailored to country-specific circumstances. FSAPs conclude with the preparation of a Financial System Stability Assessment (FSSA), which focuses on issues of relevance to IMF surveillance and is discussed at the IMF Executive Board together with the country's Article IV report. Each FSAP also includes a discussion of previous policy recommendations and the country's actions to implement them, both of which are then regularly included in the Article IV policy implementation annex.

IMF lending programs have built-in requirements to help compel countries to adopt policies that are consistent with IMF recommendations in return for IMF financial support. A member country borrowing from the IMF is typically required to commit to implementing a series of policies that have been negotiated between IMF staff and the country authorities, referred to as conditionality. The conditionality may involve *prior actions,* measures that a country must adopt or put into place before the Board approves the program, as well as ongoing *performance criteria* for key fiscal and monetary indicators (such as the budget balance and the stock of foreign exchange reserves) and forward-looking *structural benchmarks (*such as specific actions to strengthen public financial management or financial sector supervision). These measures help strengthen a country's economic foundation and the prospects for returning to macroeconomic health.

The IMF makes disbursements under a program in installments as countries carry out agreed economic policy actions. This approach promotes progress in program implementation, provides time for the country to adjust to economic shocks in a manner less disruptive to the country itself and the global economy, and safeguards the IMF's resources. *Program reviews* provide a framework for the IMF's Executive Board to assess quarterly or semi-annually whether the IMF-supported program is on track and whether modifications are needed to achieve the program's objectives. Reviews combine a backward-looking assessment on whether the country met the program conditions on the agreed timetable, with a forward-looking perspective (i.e., whether the program *performance criteria* or *structural benchmarks* needs to be modified in light of new developments). The IMF Executive Board reviews a country's progress on agreed policy commitments and actions and must approve any monetary disbursements under an IMF-supported program. If a program has gone off track, the IMF may require prior actions before recommending that the Executive Board conduct its review and consider disbursing the next installment.

The current framework appropriately conditions IMF lending on the implementation of policies within the country authorities' control. At the same time it maintains flexibility to provide support that is needed due to external shocks. Such support included emergency assistance and debt relief for the Ebola-affected countries in 2015, and funding for reconstruction efforts in Nepal following the 2015 earthquake. The IMF's effectiveness as the primary institution to promote global financial stability is bolstered by its ability to combine policy conditionality with appropriate flexibility.

3. The IMF's Transparency Policy

The IMF has made great strides in improving institutional transparency and in encouraging greater public sector transparency in member economies. Over the past two decades, the IMF has fundamentally changed its transparency policy, enabling the organization to contribute openly to public debates during the global financial crisis and to respond to heightened scrutiny of its increased financing activities.

Until the mid-1990s, the IMF published few of the reports prepared for the Board. With strong advocacy from the United States, the IMF's shareholders have progressively moved to expand the IMF's transparency policy. The IMF's archives were first opened up to outside persons in 1996, granting access to documents that were 30 years old, subject to certain conditions. Since then, the time lag for public access to most IMF documents has been progressively reduced and now amounts to just a few weeks for many Article IV country reports for example.

In 2004, the IMF revised its policy to call for the publication of the vast majority of IMF documents (subject to country consent for country papers), institute regular reporting on ongoing trends on publication, and undertake periodic reviews of the transparency policy itself. Countries retain the right to request deletion of highly market-sensitive material prior to a document's release. Publication of annual Article IV staff reports is "voluntary but presumed." This means that these reports are published except in the rare cases when the country issues an objection. Release of country program documents is also "voluntary but presumed," but the Managing Director historically has not recommended approval of an exceptional access program unless the country has agreed to publish the related staff report.

In 2014, 92 percent of member countries agreed to publication of their respective IMF Article IV country report. Only four countries have never allowed Article IV report publication – Bahrain, Brunei, Oman, and Turkmenistan. At the Board, the United States continues to press countries to publish their Article IV reports.

In 2014, 97 percent of member countries under an IMF program agreed to publish their letters of intent, memoranda on economic and financial policies, and technical memoranda of understanding. Over the past decade the IMF has published all exceptional access program proposals and program reviews. Most of these are available within a few weeks of the Board meeting.

The IMF also publishes all policy papers, typically following the Board discussion. The publication of policy papers is presumed but is subject to Board approval, while the publication of multi-country documents requires consent either from the Board or the relevant members depending on the type of document. In 2014, the Board reduced the lag for public access to most Board meeting minutes from five to three years. The IMF has retained the five-year lag for discussions that involve IMF lending or a Policy Support Instrument. Board minutes include verbatim transcripts of the meeting. The United States has supported these changes and will continue to look for ways for the IMF to increase its transparency.

The IMF also publishes, on a timely basis, information regarding each member country's financial positon in the IMF. IMF financial data are updated weekly and available on the IMF's website. These data include a summary of financial assistance to member countries in support of their policy programs, available IMF resources, arrears, and key IMF rates.

The IMF established the Special Data Dissemination Standard (SDDS) in 1996 to guide members that have, or might seek, access to international capital markets in providing their economic and financial data to the public. For member countries with less developed statistical systems, the IMF established the General Data Dissemination Standard (GDDS) in 1997 as a framework for evaluating their needs for data improvement and setting priorities. In 2012, the IMF created SDDS Plus as an upper tier of the IMF's Data Standards Initiatives to help address data gaps identified during the global financial crisis. The United States was one of the first adherents to the SDDS Plus.

In 2015 the enhanced GDDS (e-GDDS) replaced the GDDS. More than 97 percent of IMF member countries participate in the e-GDDS, SDDS, or SDDS Plus. There are currently 110 participants in the e-GDDS, 66 SDDS subscribers, and 8 SDDS Plus adherents.

Based on the results of a March 2015 review of the IMF's Data Standards Initiative, IMF management decided to focus greater attention on helping GDDS countries graduate to SDDS. The United States strongly supports the IMF's push to focus technical assistance resources on GDDS countries and to use surveillance reviews to call attention to priorities for filling data gaps and improving data dissemination. Notably, in October 2015 China subscribed to SDDS, which will help provide better information across a number of data categories, including China's reserve holdings.

4. Risks of Exceptional Access Loans – Surcharges and Collateral

The IMF can provide lending above normal access limits to countries in crisis, subject to the IMF's exceptional access framework. While such lending inevitably involves risk, the unique nature of IMF lending, including the IMF's ability to attach policy conditions to its lending, and the IMF's status as the world's "preferred creditor" (whereby countries routinely prioritize payment to the IMF ahead of payment to other creditors), substantially mitigates this risk. For example, as part of an IMF program, the country and the IMF may agree to permit the exchange rate to depreciate, which can reduce outflows of foreign exchange, improve export revenues, and strengthen a country's external sustainability, ultimately strengthening the country's ability to repay the IMF. In addition, because the international community recognizes the IMF as the world's "preferred creditor," failure of a country to repay the IMF effectively cuts a country off from other sources of finance, amplifying the consequences of a failure to repay and making it far less likely to happen. That is why of the 24 cases of IMF exceptional access lending since the global financial crisis began in 2008, there was only a single instance of a country not repaying in full and on time, and in that case (Greece in June 2015) the country quickly remedied the delay in its repayment to the IMF. Indeed, a number of countries that have received exceptional access from the IMF have made early repayments to the IMF. From an institutional perspective, the IMF's balance sheet is rock solid, with precautionary balances of over $23 billion and gold holdings worth about $102 billion at current market value (carried on the balance sheet at $4.5 billion), relative to credit outstanding of $67 billion.

In addition, the IMF's exceptional access framework includes a set of four criteria that borrowing countries must meet, which are designed to provide clarity and predictability for borrowers and the markets and to further safeguard IMF resources. The criteria are: (1) balance of payments pressure on the capital account that cannot be met within existing financing limits; (2) a high probability that debt will remain sustainable, based on a rigorous and systematic analysis; (3) good prospects for regaining private capital market access while IMF resources are outstanding; and (4) a strong adjustment program and a reasonably strong prospect of success, considering the member's adjustment plans and its institutional and political capacity to carry them out.

The IMF uses both level and time based surcharges to further mitigate risks (by generating income to boost precautionary balances) and create incentives for countries to avoid large and prolonged use of IMF resources. Level based surcharges were introduced in 2000 to discourage unduly high access but are set so as not to discourage countries with need from seeking assistance. In 2009, level based surcharges were set at 200 basis points above the normal borrowing rate on credit outstanding over 300 percent of quota. In February 2016, the Board approved a reduction in the threshold for level based surcharges from 300 percent to 187.5 percent of quota. The surcharge was kept at 200 basis points.

The IMF introduced time-based surcharges in 1997 to provide an incentive for early repayment. When credit outstanding exceeded the threshold for level-based surcharges for more than 36 months, a time-based surcharge of 100 basis points was added. In February 2016, the Board decided to differentiate between SBAs and EFFs. SBAs, the main non-concessional facility, are typically 12 to 24 months in duration and cannot extend beyond 36 months. In contrast, EFFs are intended for countries with more prolonged difficulties, including underlying structural problems, and generally last 36 months with a possible extension to 48 months. The repayment period for an EFF is also longer, 4 ½ to 10 years compared to 3 ¼ to 5 years for the SBA. IMF staff maintained that it takes longer on average for a country with an EFF to regain markets access, namely 39 months, compared to 15 months for a country with an SBA. Based on IMF staff advice, the Board kept the time-based threshold at 36 months for the SBA but increased it to 51 months for the EFF.

While surcharges have become more prevalent following the global financial crisis, the current system of price-based incentives appears to achieve its objective of discouraging members' prolonged use of IMF resources. Since 2008, five members with high levels of credit outstanding—Iceland, Latvia, Hungary, Ireland and Portugal—have made large early repurchases. Iceland and Latvia had pre-existing arrangements with the IMF and were exempted from the 2009 surcharge policies, while Hungary, Ireland, and Portugal were subject to the system of level- and time-based surcharges. Early repurchases made by Hungary, Ireland, and Portugal appear to coincide with regained market access and a reduction in the cost of market borrowing. Ireland made early repurchases so as to reduce its credit outstanding to just below the surcharge threshold as market access became relatively cheaper; this suggests that eliminating the surcharge was a motivation for making the early repurchases.

The IMF did not consider introducing collateral during the 2016 review of access and surcharges. Collateral would add an additional safeguard for IMF resources but could also act as a disincentive to approach the IMF in the early stages of a crisis, resulting in the need for greater financing. Further, the insistence on collateral for exceptional access programs could undermine market confidence in the country and delay a return to market access. Treasury believes that current safeguards are sufficient to protect the IMF from incurring losses, as demonstrated by the IMF's very strong balance sheet after more than 70 years of operation.

5. Classification of Loans Following the Implementation of the 2010 Quota Reforms

The IMF links the amount of most borrowing from the IMF to a member country's quota. The IMF sets access limits at levels intended to meet member's balance of payments needs and provide members with confidence regarding the scale of possible financing, while preserving the IMF's liquidity and the revolving nature of its resources. The IMF Executive Board reviews these limits every five years to ensure their continuing adequacy relative to potential need and capacity to repay. In 2009, the Board approved an increase in normal access limits for borrowing under the Stand-by Arrangement (SBA) and Extended Fund Facility (EFF) to 200 percent of quota on borrowing in a 12-month period and a 600 percent of quota cumulatively, net of scheduled repurchase obligations.

The IMF Executive Board postponed the 2014 review pending the implementation of the 2010 quota reforms. These reforms became effective in February 2016 and doubled country quotas on average. IMF staff proposed reducing access limits to 140 percent of quota over a 12-month period and 420 percent of quota cumulatively for the SBA and EFF. Staff argued that these levels would result in a rise in average nominal access consistent with the growth in global GDP, trade, and external liabilities (excluding foreign direct investment) since 2009. Treasury supported the proposed changes but some Board members pushed for higher access limits, with several opposing an outcome where nominal access for some countries would decline. The Board reached a compromise whereby access limits were reduced to 145 percent of quota over a 12-month period and 435 percent of quota cumulatively for the SBA and EFF. This resulted in an average increase in access of 45 percent in special drawing rights (SDR) terms.[3] The increase ensures that no country's access declines in nominal terms and that access relative to key economic indicators was maintained. Since the quota increase was not distributed equally across all countries (but rather weighted in favor of dynamic countries whose weight in the global economy had grown), the impact on IMF access of individual countries varies.

The adjustments to access limits have not resulted in any reclassification of country programs. There are no active programs that were approved as exceptional access, but would now fall within normal limits. Currently, Ukraine is the only active exceptional access program; other exceptional access programs have already concluded, and are in the process of being repaid. As indicated in the table below, the Ukraine program exceeds normal access thresholds under both the current cumulative threshold (435 percent) and the former cumulative threshold (600 percent). Similarly, member countries that were not subject to the exceptional access framework prior to the entrance into effect of the modifications to overall access limits would be grandfathered. No countries, however, met this threshold.

Ukraine EFF approved March 2015:

SDR billion (US$ billion)	Percent of pre-reform quota	Percent of current quota
12.348 billion ($17.5 billion)	900 percent	614 percent

[3] The SDR is a basket of currencies used as a unit of account by the IMF.

The SBA and the EFF are the main non-concessional lending facilities of the IMF. The IMF also reduced access under other facilities both non-concessional and concessional, as shown in the table below. The Flexible Credit Line, a short-term facility reserved for countries with very strong fundamentals, policies, and a good track record of policy implementation, has no preset access limit.

Annual and Cumulative Normal Access Limits by Facility
as a percent of quota

	Current Limits		Previous Limits	
	Annual	Cumulative	Annual	Cumulative
Non-Concessional				
SBA/EFF	145	435	200	600
RFI	37.5	75	75	150
PLL	200	500	500	1000
Concessional				
SCF/ECF	75	225	150	450
RCF				
Normal	18.75	75	37.5	150
Shocks	37.5	75	75	150

Note: Access limits for the concessional loan facilities and the Rapid Financing Instrument (RFI) were rasied by 50 percent in July 2015 with the understanding that they would be halved once the 2010 quota reforms were effective.

6. Lessons Learned from Lending Arrangements that Involve the Troika

There have been a series of opportunities for the IMF staff, management and shareholders to reflect on the lessons learned from IMF lending to the euro area crisis countries: Ireland, Greece, Portugal and Cyprus. The IMF conducted self-evaluations through ex post country evaluations of the Ireland and first Greece program, and two broad reviews of crisis programs (including euro area countries) in 2011 and 2015. The IMF's Independent Evaluation office (IEO) also reviewed the IMF's crisis lending programs in 2014. Forthcoming are self-evaluations of the Portugal, second Greece, and Cyprus programs, and an IEO review focused on the euro area countries.

The IMF's participation in the euro area programs was essential and substantial, and there is much to learn from what went right and what went wrong. The IMF's technical skills and experience in program design were critical to the credibility of the euro area lending arrangements. At the time that the euro area programs were implemented, particularly with respect to the Greece programs, there was a real risk of severe European and global contagion from a potential euro area exit. This contagion would have had very severe and damaging consequences for the global economy and the U.S. economy. The United States believes that the IMF Board made the right choice in approving the IMF's participation in these programs.

Nevertheless, important lessons can be learned from an evaluation of the individual programs and the interaction the IMF with the euro area institutions to guide future exceptional access programs and engagement with regional financial arrangements. On the program side key lessons include:

- ***Exchange Rate Adjustment/Internal Devaluation***: Depreciation of the exchange rate can aid adjustment of an economy by easing the adverse effects on output. The euro area programs, however, faced a common challenge: because they were in a currency union, they were constrained from using exchange rate policy as a tool, and had to rely on "internal devaluation". Internal devaluation which relies on domestic price adjustment proved difficult, slow and painful. Low inflation and weak external demand further complicated the process. The longer-term nature of adjustment through internal devaluation emphasizes the importance of finding the right balance between requiring upfront adjustments and a more gradual approach.
- ***Structural Reforms:*** Structural reforms are particularly important for countries requiring an internal devaluation and hence may need to be more extensive than in other programs. However, some structural reforms turned out to have a stronger drag on near-term growth than the IMF expected. As a result, the capacity of authorities to implement reforms is critically important and program assumptions need to account for the potential short-term drag on growth from reform implementation. Structural measures also need to be sequenced to favor growth-enhancing measures particularly in the early stages of a program. The IMF's analysis indicated that staff assumed near-term positive growth effects from supply-side reforms in both Greece and Portugal programs, a result that was at odds with the empirical literature on the effects of such reforms.
- ***Fiscal Consolidation:*** Many of the euro area countries had high levels of public debt requiring fiscal consolidation. The prescribed fiscal consolidation, however, often proved too large and too fast to support a recovery in growth. In Ireland's program a more even distribution of fiscal adjustment, rather than a more front-loaded approach, helped limit the contraction in demand. As with structural reforms, program design needs to take into account the effects of fiscal consolidation on output. In Greece, the greater than expected effect of consolidation on output under the first program and the consequent rise in the debt to GDP ratio led IMF staff to push for a more gradual approach to consolidation in the follow on programs. To help address these issues, the IMF should consider additional financing to accommodate a more gradual consolidation as well as timely debt restructuring.

The IMF's experience with euro area crisis programs also provides lessons with respect to the role of the European institutions in financing and program design.

- ***Importance of Institutional Arrangements in a Monetary Union:*** The Greek crisis highlighted the shortcomings of the euro area architecture that did not provide for adequate risk sharing and crisis response. The establishment of firewalls through the creation of the European Financial Stability Facility and the European Stability Mechanism helped reduce the threat of contagion. By the time of the Cyprus program in 2013, the ability to limit contagion allowed for a deeper restructuring. The European efforts to move to a banking union and the creation of a Single Supervisory Mechanism should help prevent future crises and limit the spread of crises.

- ***Financing Arrangements:*** Membership in a currency union constrains the policy options that the IMF would normally pursue (i.e. exchange rate adjustment) and lengthens the period of adjustment, while the IMF's financing remains short-term in nature. Thus, the United States has strongly supported an approach in which the currency union typically bears the bulk of financing costs and IMF financing plays a secondary and catalytic role.
- ***Currency Union Conditionality:*** Regarding program design, a key insight is that currency union-level policies can matter critically for country outcomes, and thus currency union-level conditionality can and should be used. The IMF's policy dialogue with the currency union could have been strengthened in areas such as ECB monetary and supervisory policies, construction of European firewalls, and intra-European economic imbalances that compressed demand in the periphery countries. In addition, more of the euro areas dimensions could have been included in euro area country surveillance and program reviews.

The upcoming IEO evaluation of euro area programs is an important opportunity to delve more deeply into these issues so the IMF and international community can continue to learn from this experience and incorporate lessons into future crisis response.

7. Transparency and the IMF's Technical Assistance (TA)

Many countries rely on the IMF's technical expertise and request technical assistance from the institution in areas including macroeconomic policy, monetary and exchange rate policy, financial stability frameworks, fiscal policy and debt management, public financial management, tax policy and administration, and official statistics.

In June 2013, the IMF rolled out an updated version of its official policy on dissemination of TA information. The report encapsulating this policy, entitled *Staff Operational Guidelines on Dissemination of Technical Assistance Information*, is available on the IMF website. Governing this policy is the principle that countries, in requesting TA from the IMF, consent to dissemination of information about that TA unless they explicitly object. In addition to the organization receiving TA from the IMF, other recipients of TA information may include Executive Directors (EDs) and their staff, donors and other TA providers with a legitimate interest, and/or the general public. Prior to revision of the policy in 2008, a patchwork of overlapping practices for specific situations led to a lack of clarity, further inhibiting wider sharing of TA information. As a result, before 2008, the general practice was to treat most TA information as confidential.

The current policy states that TA information can be shared per the following guidelines.

- General TA information is considered not-confidential, unless otherwise requested by the recipient country. The IMF makes such non-confidential TA information available to EDs and their staff, donors, and the general public, upon request.
- Final TA advice is considered confidential, but if such information is requested by EDs and their staff, donors, or other TA providers with a legitimate interest, the IMF makes such information available upon absence of objection from the recipient country. When making such information available, the IMF requires that recipients maintain the confidential nature of the information.

These guidelines seek to strike a balance among: the IMF's role as a confidential advisor to the authorities, the public value of IMF transparency, and the importance of information sharing among TA providers to promote coordination and reduce overlap.

The IMF's TA can help in crisis prevention by strengthening public sector institutions and policies. Experience suggests that helping economies develop resilient and deep capacity, with sufficient buffers to dull the effects during onset, represents the biggest opportunity to prevent crises. In providing for greater capacity, the IMF's Monetary and Capital Markets department has seen an increase in interest for more advanced TA, specifically dealing with crisis management, systemic issues, central bank operations, banking regulation and supervision, and monetary frameworks. Although financial crises are likely to remain difficult to predict and efforts to prevent crises may not always succeed, TA can still be beneficial in amelioration of crisis effects. The IMF and Treasury's Office of Technical Assistance (OTA) have worked together to employ a wide range of TA interventions to stem the effects of crises and resolve failing institutions. Given downside risks to the global economy, deep capacity building engagements are needed.

The IMF does not have capacity to meet all country requests for TA, and can leverage its TA resources by partnering with other TA providers including OTA. As in all donor-related endeavors, coordination is critical to effectiveness, and the IMF seeks to minimize duplication of effort and maximize complementarity. The IMF employs a range of coordination mechanisms depending on the country situation, from a formal Steering Committee, to joint participation under single project management, to discrete activities under a consolidated work plan, to regular communication about complementary projects.

Bilateral and multilateral donors are playing an increasingly important role in financing the IMF's technical assistance, with their contributions now financing nearly half of the IMF's effort. Strong partnerships between the IMF and other donors also help improve the quality and content of the IMF's technical assistance.

Recognizing the value of these partnerships, the IMF is taking steps to engage with donors and other TA providers on a broader, longer-term and more strategic basis. For example, the IMF is seeking to pool donor resources in multi-donor trust funds on a regional and topical basis to supplement the IMF's own resources for technical assistance while leveraging the IMF's expertise and experience. The IMF has already established topical trust funds in the areas of anti-money laundering/combating the financing of terrorism; management of natural resource wealth; tax policy and administration; and debt management.

The IMF and Treasury's Office of Technical Assistance (OTA) have complementary models of operation, with the IMF engaged in a broader set of countries with more intermittent support, while OTA provides deeper engagement in a particular issue area (often with resident advisors) in fewer countries. This provides opportunity for OTA/IMF collaboration. For example, OTA and the IMF have worked together to help the Central Bank of Myanmar strengthen its framework for anti-money laundering and counter terrorist finance (AML/CFT), with OTA assisting with outreach events to engage the private sector, and the IMF focusing on examination procedures. When the IMF was unable to complete its work during its shorter-term engagement, the IMF coordinated with and handed off to OTA to finish the project. The IMF's coordination spans both bilateral and multilateral donors. In Iraq, the IMF is assisting the central bank with legal regulatory work to strengthen its AML/CFT regime, while the World Bank is providing training sessions on the basics of bank supervision, and OTA will be complementing these efforts through one-on-one assistance to supervision staff on practical implementation.

In recent years, OTA has also assisted the IMF with development of its Tax Administration Diagnostic Assessment Tool (TADAT), which the IMF rolled out in November 2015. TADAT is the IMF's toolset for diagnosing gaps and opportunities in a country's tax administration. OTA provided feedback during development of the tool to improve its accuracy and practicality. Treasury's OTA is now the only external organization trained, licensed, and authorized by the IMF to use TADAT to help countries identify areas for tax administration improvements. Examples of recent IMF-OTA engagement are provided in the box below.

Technical Assistance Partnerships between the IMF and Treasury's Office of Technical Assistance

Mongolia – The IMF and OTA are engaged in a jointly run tax administration project to improve collection and management of tax revenue. The IMF/OTA partnership on the project has benefitted from a single leadership strategy and a unified set of goals.

Guinea Bissau and Burma – The IMF and OTA have worked in partnership in these countries, among others, to jointly assess and address local needs in the area of tax administration. Often times, work on the project will be split between IMF and OTA to leverage each organization's comparative advantage– given the local context.

Ukraine – In the immediate aftermath of the Euromaidan crisis, the IMF and OTA's Banking & Financial Services Team worked together to address the needs of the distressed banking sector. OTA brought specific and deep experience with resolving failing institutions, allowing for insured depositors to be paid out, and working with the National Bank.

Appendix 1: Sample Article IV Risk Assessment Matrix

Brazil: Risk Assessment Matrix[1]

Nature/Source of Threat	Likelihood	Expected Impact on Economy	Policy Responses
		Domestic Risks	
Delays in the resolution of the Petrobras corruption probe	***M***	***H.*** Firms under investigation, including Petrobras, could see their access to funding diminished and their investment programs at risk. The infrastructure concession program could be hampered by the ineligibility of construction companies. Pressure would rise to use public funds, possibly through public banks, to support Petrobras' investment.	Strengthen governance standards and anti-corruption safeguards in procurement procedures to ensure the success in attracting private sector participation in the infrastructure program. Ease the requirement that Petrobras' participate in all new oil developments, and domestic content requirements.
Drought and power rationing	***H***	***H***. Growth slowdown from electricity rationing accompanied by inflationary pressures as consumers will have to bear the additional energy cost in the absence of energy subsidies. Water rationing could affect manufacturing as well as agriculture, including in Sao Paulo state.	Keep policies tight to contain spillovers into inflation and refrain from introducing additional Treasury subsidies which will weaken the fiscal outturn. Make sure that prices reflect scarcity to promote the efficient use of resources, while protecting basic level of access for vulnerable households.
Falling short of the fiscal target	***M***	***H***. Fiscal balances would continue to disappoint and fail to stabilize debt. Further loss of confidence would result in lower investment and growth. Inflationary pressures would remain elevated. Brazil could lose its investment grade, which would further dampen confidence and growth, weakening the primary balance and increasing sovereign borrowing costs and public debt. Corporates could be vulnerable to capital flow reversals and exchange rate depreciation. The strains would worsen if banking system soundness deteriorated owing to an increase in NPLs.	Additional fiscal consolidation measures should be identified to restore credibility in the fiscal framework and to ensure debt stabilizes. Focus efforts on boosting competitiveness and productivity. If the sovereign loses its investment grade, triggering economic side-effects, additional policy actions would be necessary, possibly including monetary policy tightening.
Intensified inflationary pressures	***M***	***H***. Worsening inflation expectations and further erosion to the inflation targeting framework.	Further monetary tightening to preserve the credibility of the inflation framework and ensure the convergence of inflation towards the target.

[1] The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood of risks listed is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly.

Brazil: Risk Assessment Matrix (Concluded)

Nature/Source of Threat	Likelihood	Expected Impact on Economy	Policy Responses
		External Risks	
Protracted period of low growth	*M*	*H*. Employment destruction would lead to a deterioration of households' balance sheet and income resulting in a rise in delinquencies on consumer loans. Increased financial vulnerabilities among banks with portfolio concentrated in consumer/housing loans. Potential knock on effects on public finances. For example, Caixa extends housing loans to low-income families with a government guarantee. Lower corporate profits may expose some highly leveraged corporates	Monitor for signs of emerging domestic financial and corporate vulnerabilities. Take measures to strengthen the fiscal framework including public debt, and refrain from adding further demand stimulus. Impose targeted prudential measures to reduce risks in weak financial institutions. Smooth out the employment loss by relying on strategies such as reduced hours. Accelerate efforts to improve the business environment and foster investment.
Abrupt surges in global financial market volatility	*H*	*H*. Increasing Brazil's risk premiums, pressures on the real and reversal of capital flows. Increasing yields in domestic bond markets. In particular corporates lacking FX hedging could be exposed.	The flexible exchange rate remains an important capital flow shock absorber. Recourse to FX intervention if FX volatility becomes excessive. Provide FX liquidity and support individual banks if dollar shortages appear. Increase policy rate to ensure adequate external financing. May also need to tighten fiscal policy to further strengthen policy credibility and avoid sell-offs of Brazilian domestic bonds.
Financial imbalances from protracted period of low global interest rates	*M*	***M.*** Building-up vulnerabilities as some corporates may further increase leverage.	Monitor highly leveraged corporate; consider CFMs to discourage shorter-term borrowing. Tighten monetary policy further if financial risk taking becomes excessive.
Protracted period of slower global growth in advanced and emerging economies	*H*	*H*. Worsening current account deficit and weaker growth. Highly indebted corporates could see their profits decline. A sharp decline in commodity prices would have a direct impact on the exporting sector.	Use the exchange rate as first shock absorbers. Limited room for monetary and/or fiscal policy stimulus to smooth shock. Instead, prioritize structural reforms to boost potential growth.
Sharp rise in world oil prices	*M*	***L.*** Mild negative impact on the trade balance in the short-term, but improving current account in the medium term, when Brazil is expected to become a net oil exporter. In the near term, an adverse impact on the finances of Petrobras if domestic fuel prices are not adjusted sufficiently.	Domestic pricing policies should ensure Petrobras obtains an adequate return from commercialization of imported fuel.

Appendix 2: Sample Article IV Implementation Scorecard

United States 2015 Article IV -- Responses to Past Policy Advice

Fiscal policy. Over the last few years staff has emphasized the importance of fixing long standing fiscal problems to slow entitlement spending and normalize the budget process. Cost saving measures that were part of the Affordable Care Act appear to be lowering health care inflation. A continuing resolution for the rest of FY2015 that was passed in December 2014, subsequent extension of funding for the Department of Homeland Security, as well as bipartisan support for passing a reform package that ends automatic Medicare payment cuts to doctors –the so-called "Doc-Fix" were positive steps that lessened fiscal uncertainties. Staff also advocated adopting a medium-term fiscal consolidation plan to restore long-run fiscal sustainability, stressing that early action is needed to slow entitlement spending. Anchored by such a plan, staff called for expanding the near-term budget envelope through specific measures—including front-loaded infrastructure spending, a better tax system, active labor market policies, and improving educational spending, with these measures funded by offsetting savings in future years. The prospects for progress in these areas remain unfavorable, given the lack of political consensus.

Monetary policy. Given continued economic slack and expectation of muted inflationary pressures, staff supported maintaining policy rates at zero for longer (past mid-2015) than foreseen by markets at the time of the last consultation. Staff also stressed the importance of a well communicated normalization of U.S monetary policy conditions, in the context of robust U.S growth, and pointed to scope for enhancements to the Fed's communications toolkit. The Fed continues to maintain a supportive monetary policy and has made significant efforts—in FOMC statements, press conferences, and speeches—to strengthen its communication and prepare markets for normalization.

Financial policies. Based on the 2010 FSAP and subsequent work, staff has recommended several steps to tackle financial sector risks, particularly those related to activities in nonbank intermediaries. Substantial progress has been made on the national and global financial reform agenda over the last few years, and many of the policy suggestions have been implemented. These include enhanced capital and liquidity buffers, strengthened underwriting standards in the housing sector, greater transparency to mitigate counterparty risks, as well as progress in collecting more comprehensive information to assess risks. Still, several reforms emphasized by staff, such as addressing remaining vulnerabilities of the money market funds and the tri-party repo market, allowing for the orderly resolution of too-important to-fail financial institutions, and reforms to increase the resilience of the insurance sector remain to be completed.

Structural policies. Staff has recommended several structural measures to counter the slowdown in potential growth and high poverty rates, including expand the EITC, increasing the minimum wage, investing in infrastructure and education, improving the tax system, using active labor market policies, implementing a broad, skills-based approach to immigration reform and capitalizing on the gains from rising U.S. energy independence. The Administration has taken measures to increase wages for some workers and several states and localities have increased minimum wages. Building political consensus on a reform of the tax system in the direction envisaged by staff (a less complex system with a broader tax base and lower rates) has made little progress. Support for immigration reform is elusive and there is no plan to raise the gas tax or to introduce a VAT or a carbon tax.

Housing finance. Staff has stressed policy measures to encourage greater availability of mortgage credit, while clarifying the future role of government in housing finance. Administrative measures have been taken to lessen regulatory uncertainties and to transfer risks from the agencies to private investors through market transactions. Legislative proposals to more fundamentally reshape housing finance have made little headway in Congress.