Burden Sharing at the IMF

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Abstract

The paper reviews aspects of the financial governance of the IMF, focusing on the equity implications of the manner of distributing the cost of running the Fund's regular (non-concessionary) lending operations as well as the modalities of funding its concessionary lending and debt relief operations. It is concluded that while the Fund charges borrowers roughly what it pays its creditor members for the resources used in its regular lending operations, its overhead costs (administrative budget plus addition to Reserves) are shared between the two groups of members in a less equitable manner. With the overhead costs rising inexorably to meet an increasing number and variety of responsibilities being placed upon the institution, largely at the instance of the Fund's principal creditors, by virtue of their dominant majority of voting power, the under-representation of the Fund's debtors undermines the legitimacy of its decision-making. In regard to the concessionary lending and debt relief operations, some of the funding modalities have involved a substantial contribution by Fund debtors, sometimes under pressure. While this outcome has been accepted as part of an intra-developing country burden-sharing exercise, it has also meant a significant burden-shifting away from the developed countries in the cost of meeting their responsibilities to the poorest members of the international community.

Burden Sharing at the IMF

1. Introduction:

This paper looks at one aspect of governance at the IMF, that relating to the cost of running the institution and the sharing of that cost between the industrial countries (that are the principal creditors) and low-income countries and emerging market economies (that are primarily borrowers). Much larger issues of equity are involved in respect of the distribution of quotas (or capital shares) and of voting power in the institution. This subject has received growing attention in recent years. A contribution to the literature by a retired senior IMF official who served as the Secretary of the Fund from 1977 through 1996[1] concludes that

> "The system of quotas and voting power in the IMF has, over the years, created distortions and lacks equity. A group of 24 industrialized countries controls 60 percent of the voting power, while more than 85 percent of the membership – 159 out of 183 IMF members – together hold only 40 percent of the vote. …….... The existing imbalance is seen as evidence of the lopsidedness of governance of the international monetary system. Thus a more equal distribution of quotas and voting power between the developing world and the industrial countries should enhance the IMF's governance and credibility….."

Rather than enlarging upon this theme, this paper takes the fundamental inequity in the quota distribution -- and hence in the decision making power structure -- as a given, as a fact of life under which both IMF and its sister-organization, the World Bank Group, must operate at the present time. The focus is on a much narrower issue of *financial* governance at the IMF and for purposes of the paper, burden sharing is defined to cover aspects of equity that are involved in the manner in which the cost of running the institution is distributed between the Fund's creditors and its debtors and among the different groups of debtors. This definition is meant to cover a broader set of issues than is encompassed by the existing "Burden Sharing Mechanism" in the Fund that is described in section 3 below.

2. <u>Cost of Lending through the General Resources Account (GRA)</u>

The financial operations of the Fund are conducted through several channels. The principal channel (in terms of the volume of lending) is designated as the "General Resources Account" (GRA) through which the non-concessionary transactions of the IMF take place. Borrowing countries pay interest on amounts they draw from their credit tranches [2] with the rate of interest being derived from a formula for setting the *basic rate of charge* for the use of Fund resources. That charge is based on the income that the Fund must earn in order to cover

(i) the *remuneration* that the Fund pays members whose currencies are used in lending transactions,[3] with *the basic rate of remuneration* equal to the rate of interest on the SDR;[4]
(ii) the administrative budget of the IMF and
(iii) a target level of net income for addition to reserves.[5]

Based on the net income target, the expected SDR interest rate, projected credit extension and the outlook for administrative expenses, the IMF estimates the basic rate of charge as a proportion of the SDR interest rate.[6] The decision on the rate of charge requires annual renewal, with a qualified majority of 70 percent of total voting power. For FY 2003, the basic rate of charge has been set at 128 percent of the SDR rate.

The Fund's income from charges is supplemented by *surcharges* levied on two sets of transactions. Under the Supplemental Reserve Facility (SRF) established in 1998 to provide credits to countries encountering capital account crises -- and under which there are no defined access limits -- a market-type rationing device has been adopted: there is a surcharge of 300 basis points initially (on the basic rate of charge) which rises by 50 basis points after one year from the date of disbursement and each subsequent six months to a maximum of 500 basis points. For

other GRA transactions, there are annual and cumulative access limits on purchases in the credit tranches and under the Extended Fund Facility (EFF)[7]. However, since November 2000, surcharges have also been applied to these transactions in order to discourage unduly large use of credit and to encourage prompt repayment: the surcharge is 100 basis points on credits in excess of 200 percent of quota and 200 basis points on credits in excess of 300 percent of quota. The income derived from surcharges is taken to IMF reserves directly and remains outside the net income target for the year (which enters into the calculation of the basic rate of charge). The IMF also receives income in the form of service charges, commitment fees and special charges,[8] all borne by the Fund's borrowing members.

3. The Burden Sharing Mechanism (BSM)

An upward adjustment to the basic rate of charge and a downward adjustment to the basic rate of remuneration are made to (i) offset losses of income from unpaid charges and (ii) to fund certain precautionary balances designated as Special Contingency Accounts (SCAs). The first of these Accounts , designated SCA-1, was established in FY1987 as a safeguard against potential losses resulting from an ultimate failure of members in protracted arrears on the payment of overdue obligations to the IMF. Another Special Contingency Account (SCA-2) was established in 1990 as a safeguard against possible losses resulting from purchases made through a special scheme for helping members that had accumulated arrears whereby they could get back on track under a "rights accumulation program" (RAP). The allocation of these adjustments between the debtors and the creditors of the IMF is designated as the "Burden Sharing Mechanism" (BSM).

Creditor and debtor members contribute equal amounts, in the aggregate, to the SCA-1 whereas creditors provided three-fourths of the amounts contributed to the SCA-2. However, SCA-2 was terminated in 1999 once it had it reached its target of SDR 1 billion and the amount was refunded to the contributing members after it was concluded that other precautionary balances in the GRA provided adequate protection against the risks associated with RAP-related credits. The amounts collected to offset losses of income from unpaid charges are also refunded, as and when overdue obligations are settled[9]. Resources accumulating in SCA-1 are to be refunded when there are no outstanding overdue repurchases and charges (or earlier if the IMF so decides).

The BSM raises two equity-related aspects.[10] First, members that are neither debtors nor creditors (so-called "neutral" members) do not provide contributions under the Mechanism. However, the inequity involved at the present time is not particularly onerous at the present time since the "neutral" countries account for only six percent of total quotas. Second, the distribution of the burden among members diverges sharply from quota shares. The problem has been alleviated -- though by no means removed -- as the Fund has moved since 1998 to allocate creditor participation in the financing of Fund credit according to relative quota shares for members that are deemed capable of inclusion in the Fund's quarterly financial transactions plan.

The quarterly adjustments under the BSM have been modest to date. In the last financial year (ending April, 2002), there was an increase of 14 basis points on the basic rate of charge and a reduction of 15 basis points from the basic rate of remuneration to 3.39 percent and 2.65 percent, respectively.[11] The Executive Board decided in April, 2002 to continue with the BSM.

However, it has to be recognized that the risk of loss in future could exceed the capacity of the mechanism because of a constraint mandated by the Articles of Agreement, *viz* the rate of remuneration payable to creditors cannot be reduced below 80 percent of the SDR rate of interest. And if the symmetrical sharing of costs between debtors and creditors continues to hold, the burden on debtors cannot be increased beyond whatever the creditors contribute under the BSM as currently constituted.

4. Additional Creditor Contributions to Burden Sharing:

Creditors make an additional contribution to financing the operations of the Fund by foregoing remuneration on a portion of their reserve tranche positions.[12] This unremunerated portion was equal to 25 percent of the member's quota on April 1, 1978, being that part of each country's quota that was paid in gold prior to the Second Amendment. [13] While the unremunerated reserve tranche (URT) remains fixed in nominal terms for each member, it has become significantly lower, when expressed as a percentage of quota, as a result of subsequent quota increases. The average is now only 3.8 percent of quota but the actual percentage differs widely among members as a result of the differential increases in quotas since April, 1978. Polak has pointed out that the URTs' range "from more than 6 percent of its current quota for the United Kingdom to less than 0.5 percent for Saudi Arabia"[14]

The URT has featured in past staff presentations on the equity aspects of running the Fund. In a paper on Fund Finances to be found on the IMF web-site[15], the URT is treated as a contribution by creditors on the basis that the Fund's operational expenses (its cost of raising funds) would have been higher if it had been required to pay remuneration on that portion of the

currencies of creditors used in Fund transactions.. The attached table shows the figures underlying the computation of the relative contribution of debtors and creditors, including in both cases the respective adjustments under the BSM. The table starts by excluding the Fund's cost of funds i.e, its payments to creditors, but adds back the *imputed* cost that would have been incurred if the creditors' reserve tranche positions had been remunerated. On this basis, it is calculated that the relative contribution of creditors (based on the total of actual and imputed costs) has steadily declined since FY1982 from a peak of 72.3 percent to 25.0 percent in FY2002 with a corresponding increase in the share attributed to debtors.

The table does not take account of supplementary charges that are being levied on the larger users of Fund resources. It takes the debtors' contribution as equivalent to *ordinary c*harges in excess of net operational expenses i.e., in excess of the amounts needed to cover remuneration based on the SDR interest rate (and the cost of any Fund borrowing). These amounts are not trivial: in FY 2002, for example, as much as SDR 314 million of income from surcharges was transferred to the General Reserve;[16] this compares with SDR 577 million of regular income from charges (in excess of net operational expense) that is included in the calculation of the debtors' contribution in the table

However, the particular approach to measuring and distributing the cost of operating the Fund that is reflected in the table has also been criticized on other grounds. The distribution between the two groups depends on assumptions of how to treat the interest foregone by the creditors on part of their credits. If this is seen as a "burden" accepted by the creditors, it must also be counted as a deduction from the "burden" of the debtors. It can also be argued that

measuring the debtors' burden on the basis of the excess of the rate of charge over the SDR interest rate overstates the debtors' burden in two respects: (i) it fails to consider their opportunity cost (i.e., the interest rate at which they could obtain credits in the private markets, assuming that such credits were available at all) and (ii) the SDR rate on which currently a premium of 28 percent is applied to determine the basic rate of charge happens to be a composite of short-term rates on the official paper issued by four of the most highly credit-worthy financial authorities in the world. The creditors' share, as calculated in the Table, declines in part because of the decline in the SDR interest rate in recent years.

5. Rising Cost of Running the Fund:

Notwithstanding the conceptual issues involved in calculating the distribution of the burden, there is no gainsaying the fact that the costs of running the Fund have risen over time and will continue to increase under two heads -- administrative expenses and the build up of precautionary balances. The Administrative Budget in U.S. dollar terms (in which such expenses are incurred) has risen from $ 583 million in FY 2000 to $ 677 million in FY 2002 or by 16 percent over the two year period. If the cost of capital projects is added, the increase in the same period is 18.6 percent. The projected increase for FY 2003 is 10.2 percent, without accounting for capital projects which jump from $ 61.5 million to $ 215 million, but the latter amount is meant to be disbursed over three years. Measured in SDR terms and using International Accounting Standards (which include depreciation of some capital budget projects and account for employee benefits differently), the increase over the three year period ending FY 2003 is 30.6 percent. The annual increases in the administrative budget (even excluding capital projects) is likely to continue in order to meet an increasing number and variety of responsibilities placed

upon the institution by the major shareholders, by virtue of their dominant majority of voting power in the institution. Among the new mandates are the intensified emphasis on financial surveillance; extensive work launched on the formulation and monitoring of Standards and Codes; growing involvement in anti-money laundering measures and controlling the financing of terrorism etc. In each of these areas, and under the rubric of poverty alleviation, improving governance and fostering civil society participation in the development and implementation of adjustment programs, the Fund is constantly expanding its technical assistance, expenditures on which begin to approach one-third of its administrative budget.[17]

A second factor in raising the cost of running the Fund is the imperative to build up its precautionary balances in the face of the increased risks confronting the institution. Among these risks in that associated with the growing concentration and volatility of Fund credit, as well as the frequency with which the Fund is being called upon to assist members facing capital account crises. Of particular significance is the amount of credit extended to a very few borrowers, with just three members – Argentina, Brazil and Turkey – accounting for almost two-thirds of total credit outstanding in the GRA at the end of 2002 and itself a reflection of the inadequacy of Fund resources to deal with capital account crises.[18]. There will need to be a substantial addition to the present level of reserves and other precautionary balances, now totaling SDR 5 billion.[19] In fact, there is general support for a doubling of that level and for the maintenance of the present system of accumulating these balances, under which surcharge income and regular net income are placed to reserves and only a fraction is financed – or for that matter, can be financed, given the 80 percent floor on the rate of remuneration – through the existing burden sharing mechanism.[20]

How to deal with these rising costs without placing an inordinate burden on debtors in the GRA becomes the principal burden sharing issue for the Fund in the coming years.

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6. Gold and the GRA:

Turning next to ideas for meeting the growing cost of running the Fund, one proposal that has been put forward is the mobilization of Fund gold. The Fund currently carries 103 million ounces of gold on its balance-sheet, valued on the basis of historical cost, at a book value of SDR 5.9 billion. There is a "hidden reserve" element attached to this asset when compared to prevailing market-prices (of SDR 26-27 billion). There has been a marked reluctance to tap this hidden reserve in the period following the mobilization that occurred in 1976-80 when 25 million ounces were auctioned to finance the establishment of the Trust Fund to support concessionary lending by the IMF to low-income countries.

During 1999-2000, the IMF conducted two off-market transactions in gold that left its holdings unchanged in order to generate resources to help finance its participation in the HIPC Initiative. It sold the equivalent of SDR 2.7 billion ($ 3.7 billion) at ruling market prices to two countries: Mexico and Brazil. After each sale, the gold was immediately accepted back by the IMF *at the same market price* in settlement of financial obligations of these members to the IMF. The gold so accepted was included in the IMF balance-sheet at the market price of the transaction instead of at the original book value of SDR 35 per fine ounce. However, the equivalent of that original price was retained in the GRA and the proceeds in excess of this amount (SDR 2.2. billion or about $ 2.9 billion) were held in the Fund's Special Disbursement

Account (SDA)[21] and invested, with the income from these investments being made available for financing the IMF contribution to the HIPC Initiative.[22]

The rationale for the off-market transactions was to avoid causing disruption to the functioning of the gold market but it resulted in a recurring increase in the cost of Fund operations. The IMF holdings of usable currencies in the GRA were lower, and reserve tranche positions were higher (on which remuneration must continue to be paid), *than they would otherwise have been* by the amount of the profit (SDR 2.2 billion). This is because Brazil and Mexico paid in gold instead of paying in the usable currencies that would have allowed the Fund to reduce the reserve tranche positions of creditor members. The effect on IMF net income was estimated at SDR 94 million in FY 2001, the first year in which the full income effect of the gold transactions was felt. While the off-market gold sales were "one-off" transactions, their consequences for the Fund's income would be of long duration. The relatively large increase in cost would have resulted in a higher rate of charge under normal procedures but the effect has been mitigated for debtors through the existing BSM i.e., by requiring members to contribute the amount of SDR 94 million to SCA-1. The decision to protect the Fund's non-concessionary borrowers from carrying the full brunt of the negative income-effect of the off-market gold transactions (they still bear one-half the cost under the BSM) is indicative of a recognition that the burden of helping the poorest member-countries (i.e., those eligible under the HIPC Initiative) ought not to be shouldered exclusively by other borrowing members who might be only less poor. It does enable creditor countries to shift one-half of the burden that they should bear in meeting their obligations to the world's poorest.

The negative consequences for the Fund's income position of the off-market transactions rule out any chance of resorting to this technique for helping GRA debtors; undertaking straightforward sales in the market would evoke even greater resistance from the interest groups that forced the Fund to choose the off-market route, when the objective was to benefit the poorest countries. Moreover, any transaction involving gold requires an 85 percent qualified majority of total voting power which gives the United States veto power and any small group of large quota countries could presumably assemble the votes required to block a decision.

7. Other Proposals for Improving Burden-Sharing in the GRA

If gold transactions are ruled out, the sharing mechanism already in place could be modified. The Fund staff paper cited earlier suggests an alternative on the following lines:

> "….. the rates of charge and remuneration would initially be set equal to the SDR interest rate and then adjusted, as under burden-sharing, so as to distribute the burden of financing the Fund's remaining expenses (administrative expense and its additions to precautionary balances, less the effect of the Fund's interest-free resources) on the basis of the aggregate quota shares of debtor and creditor members, respectively"…..[23]

The proposal would shift from a 50:50 sharing of costs to 60:40 on the basis of current quota shares between the industrialized members and all other countries or even a higher share could be assigned to creditors when account is taken of the fact that some major non-industrialized members are also Fund creditors. It will be recalled that Fund creditors had accepted a 75:25 sharing ratio in the case of SCA-2.

However, the proposal cannot deal with the problem that the downward adjustment to the rate of remuneration cannot fall below the 80 percent floor on the SDR rate of interest set in the Fund's Articles. There is, of course, nothing in the Articles to prevent the SDR interest rate itself

being lowered below that currently set at 100 percent of the weighted composite of short-term rates of interest on the currencies in the SDR basket; this option has been rejected in the past on the grounds that it would diminish the attraction of the SDR as a reserve asset.

A more equitable solution would provide for the portion of the reserve tranche that would be free of remuneration to be expressed as a uniform proportion of members' current quotas. The proportion would be adjusted periodically to generate an amount of interest-free resources that would permit the rate of charge to remain equal to the rate of remuneration, and the latter, in turn to remain equal to the market (SDR) interest rate. Thus creditors and debtors would both receive and pay the market interest rate on their positions in the Fund and the proposal would be robust in the sense that the distribution of the burden of the non-remunerated cost would not be affected by fluctuations in the SDR interest rate or the level of Fund credit.

However, this proposal cannot be implemented without amending the Articles. Once the possibility of amendment is accepted, other solutions could also be considered, such as repealing the 80 percent floor noted earlier. Another possibility would be to apply to the meeting of budgetary costs in the Fund's General Department (of which GRA is a part) the principle already applied in the SDR Department, namely, an annual assessment to cover the cost of operating the Fund charged in proportion to quotas.

8. Concessionary Lending

This section looks at another aspect of Fund operations that bears on issues of burden-sharing, namely the effort made by the international community to provide highly concessionary

financing, outside its quota-funded resources, to the poorer countries in the Fund membership. The basic rationale for this effort was that Fund support for the adjustment efforts of its low-income member-countries should be made available on financing terms consistent with their debt-servicing capacity.

The first effort was made through the establishment of the Trust Fund, using the proceeds of gold auctions in the period 1976-80 to provide low-conditionality loans at an interest rate of one-half of one percent, repayable over a ten-year period, with five and a half years of grace.[24] In 1986, the Fund established the Structural Adjustment Facility (SAF) to recycle the resources that were being repaid by Trust Fund beneficiaries. However, these resources were limited in amount and it was felt that stronger adjustment and reform measures than those under the SAF would call for an augmentation of SAF resources. An Enhanced Structural Adjustment Facility (ESAF) was launched in 1987 (and enlarged and made permanent in 1994) with the funds raised from bilateral contributors. Resources amounting to SDR 11.5 billion have been raised through September 2001 from 17 loan-providers -- central banks, governments and official institutions -- generally at market-related interest rates, and on-lent on a pass-through basis through the ESAF Trust (re-designated in October 1999 as the PRGF Trust) to 54 of 77 eligible countries.[25] In FY 2002, SDR 4.4 billion in new loan resources were made available to finance future PRGF operations, raising the total loan funds availability to SDR 16 billion[26].

While most loan-providers are remunerated at a six-month SDR interest rate, ESAF/PRGF borrowers are charged a concessionary rate of one-half of one percent, which has required the Fund to find additional resources on a grant basis or by way of deposits or

investments placed in the Subsidy Account of the Trust at below-market interest rates. At the end of FY 2002, the Subsidy Account of the PRGF Trust had received bilateral contributions amounting to SDR 2.5 billion.

With the launching of the HIPC Initiative in 1996 and its enlargement in 1999, it was decided to establish a HIPC Trust and followed in September 2001 with the PRGF-HIPC Trust in order to (i) enable the IMF to provide assistance in the form of grants or interest-free loans to HIPC eligible countries and (ii) to permit the transfer of subsidy resources from the PRGF-HIPC Trust to the Subsidy Account of the PRGF Trust to subsidize the continuation of PRGF lending after subsidy resources currently available in the PRGF Trust are fully utilized. The total subsidy resources required for these two purposes are estimated at SDR 7.5 billion of which SDR 2.2 billion are needed for the HIPC Initiative and the cost of subsidies for PRGF lending is estimated at SDR 5.2 billion. Bilateral pledges for meeting these requirements amount to about SDR 3.8 billion and come from a wide cross-section of the IMF membership, demonstrating the broad support for the HIPC and PRGF Initiatives. Altogether 93 countries have pledged support: 27 advanced countries, 57 developing countries and 9 countries in transition.[27] It is to be noted, however, that most of the contributions from the developing countries derive from the refunds they received from the liquidation of the SCA-2 (referred to earlier) and the contributions of some of them may have been elicited by the exercise of considerable pressure from the powers-that-be in the institution.

The IMF's "own" contributions amounting to SDR 2.6 billion are derived from several sources: (i) the net proceeds generated from the 1976-80 gold transactions mentioned above;

(ii)one-time transfers from Trust Fund/SAF reflows into the SDA; (iii)foregoing compensation for the administrative expenses related to the PRGF operations for the financial years 1998 through 2004 from the Reserve Account of the PRGF Trust and (iv) part of the income from surcharges levied on SRF transactions in 1998 and 1999. These flows are to be supplemented by investment income earned on these contributions. Of these, item (iii) has a bearing on charges paid by GRA borrowers as a reduction in re-imbursements for PRGF operations increases net administrative expenditures that enter into the determination of the basic rate of charge. There have been proposals for improved cost recovery for expenses incurred by the GRA initially for running the SDR Department and for the Fund's concessionary ESAF/PRGF programs. While the costs for the former are trivial, the same cannot be said for the latter; these are projected at SDR 52 million or about 10 percent of the total administrative expenses in FY 2000-2001. Hence the decision not to seek re-imbursement for PRGF Trust expenses represented a steep increase in administrative expenses that directly raised the charges paid by GRA borrowers.

As noted above, the Fund has already raised the loan resources it needs to maintain a lending rate of roughly SDR 1 billion per annum for the next four years through what has come to be known as the "Interim PRGF". Beyond the four-year period, it is expected that sufficient funds will have been released from the "Reserve Account" of the PRGF Trust[28] to establish the "self-sustaining" PRGF at a level of about SDR 0.7 billion per annum in perpetuity.

Less assured is the ability of the Bretton Woods institutions to "top-up" the relief to be made available to the eligible HIPC countries to assure sustainability of their remaining debt at the "completion point" of their poverty reduction and growth efforts. A further mobilization of

the Fund's "hidden reserves" in the shape of its gold holdings has been suggested.[29] But this would require actual sale, not the technique used in 1999-2000, and neither approach is considered likely for reasons cited in a preceding section.

9. Summary and Conclusions

The paper has reviewed aspects of the financial governance of the IMF, focusing on how the cost of running the Fund is distributed between its creditors and debtors in the non-concessionary lending operations of the institution through its General Resources Account (GRA) and how the concessionary lending by the Fund has been funded.

There are two elements of GRA cost: (i) interest expenses by way of remuneration payments to creditors and (ii) "other expenses" that include the administrative budget and a net income target for building up its reserves. The basic rate of remuneration is equal to the SDR rate. The Fund covers this element of its cost of funds by setting a basic rate of charge to be paid by debtors on their outstanding borrowing from the Fund as a proportion of the SDR interest rate (e.g., 128 percent in FY 2003). The "other costs" are covered by an addition embedded in the basic rate of charge and through a contribution made by creditors in the form of an interest-free portion of the quota resources they provide to the Fund, designated as the unremunerated reserve tranche (URT). However, the URT, being fixed to a historical base, has meant that the creditor contribution remains constant (or changes with the SDR interest rate) while the Fund's "other expenses" rise steadily, and along with that, the share paid by the Fund's debtors.

Special provisions under the Burden Sharing Mechanism (BSM) have been made to offset losses of Fund income from unpaid charges and to accumulate precautionary balances in Special Contingency Accounts (SCA) additional to the Fund's General and Special Reserves. These contributions are refundable to members who made them when overdue obligations are settled. One of these Accounts (SCA-1) has been built up with creditors and debtors contributing equal amounts through adjustments to the basic rate of charge and the basic rate of remuneration. However, the capacity of the BSM to achieve a more equitable sharing of the rising costs of running the Fund is constrained by the 80 percent floor on the rate of remuneration payable to creditors set under the Articles. Unless new sharing mechanisms can be devised, these costs will add ineluctably to the burden on the Fund's GRA (or non-concessionary) debtors. Much of the increase in costs results from an increasing number and variety of mandates imposed upon the institution by the Fund's major shareholders by virtue of their dominant majority of voting power. The corresponding disproportion in the representation of the Fund's debtors (mostly developing and transition countries) tends to undermine the legitimacy of the Fund's decision-making. The paper reviews alternative mechanisms and finds that robust proposals for improving burden sharing will require an amendment of the Fund's Articles.

Turning to the Fund's concessionary lending, the paper describes the various efforts made to find the necessary resources for this purpose. These efforts have included two – quite distinct -- episodes of gold mobilization in 1976-80 and 1998-99 and a series of approaches from 1987 onwards to garner bilateral official funding to which developing countries have also contributed, sometimes under pressure. The Fund's debtors have provided support directly by way of voluntarily turning back the refunds received by them from the termination of one of

the Special Contingency Accounts (SCA-2) and indirectly through agreeing to decisions to forego re-imbursements for the cost of administering the PRGF Trust. The artifice used to protect the interests of gold market participants in the last set of "off-market" gold sales has also involved a contribution by Fund debtors -- through the BSM -- for covering the *continuing* higher level of remuneration expenses that this particular "one-off" transaction has entailed. While many of the Fund's debtors have accepted these efforts as part of an intra-developing country burden-sharing exercise, it has also meant a certain burden-shifting away from the developed countries in the cost of meeting their responsibilities to the poorest members of the international community.

End Notes

[1] Leo Van Houtven: Governance of the IMF – Decision Making, Institutional Oversight, Transparency and Accountability (Pamphlet Series No. 53), IMF, Washington, D.C. 2002. See also Ariel Buira: Reforming the Governance of the Bretton Woods Institutions in Financing for Development, OPEC Pamphlet Series 33, Vienna, Austria, (August 2002) being proceedings of a Workshop of the G-24 held in New York (September 2001).

[2] There is no charge if a member draws out its "reserve tranche" (previously known as the "gold tranche") which is not considered as a credit from the Fund but rather as the use of the member's own reserves.

[3] In addition to remuneration, the Fund must cover interest paid on any sums it borrows from member governments under the General Arrangement to Borrow (GAB) or under the New Arrangements to Borrow (NAB). For an explanation of these Arrangements, see IMF Pamphlet No 45 (revised) titled Financial Organization and Operations of the IMF (2001), pp. 72-78. There are no outstanding borrowings at the present time.

[4] The SDR interest rate is a weighted composite of market-determined rates on short-term official paper denominated in the currencies in the SDR basket, namely, the U.S. dollar, the euro, the Japanese yen and the pound sterling.

[5] The annual increase in reserves was set at 3 percent of reserves at the beginning of the financial year for the years 1981-84, 5 percent for financial years 1985-99, 3.9 percent for financial year 2000 and 1.7 percent for financial years 2001-02.

[6] A mid-year review is undertaken to establish whether an adjustment to the basic rate of charge is required in view of developments during the year. At the end of the financial year, if net income exceeds the amount projected at the beginning of the year, the basic rate of charge is reduced retroactively; if it falls short of the target, the rate of charge is increased in the next financial year to make up for the shortfall.

[7] Access is subject to an annual limit on gross purchases currently set at 100 percent of quota and a cumulative limit on credit outstanding currently set at 300 percent of quota.

[8] A one-time service charge of 0.5 percent is levied on each loan disbursement from the GRA. A refundable commitment fee is charged on Stand-By and Extended Fund Facility (EFF) credits, payable at the beginning of each

12-month period on the amounts that may be drawn during that period, including amounts available under the SRF; the commitment fee is refunded when the credit is used in proportion to the drawing made. The IMF also levies special charges on overdue principal payments and charges that are overdue by less than six months.

[9] Cumulative charges that have been "deferred" since 1986 to the end of April 2002 have resulted in adjustments to charges and to remuneration amounting to SDR 865 million; the cumulative refunds over the same period, resulting from the settlement of deferred charges, have amounted to SDR 994 million. Vide IMF Annual Report for FY2002).

[10] See Box 7, Pamphlet # 45, op.cit

[11] Ibid

[12] In addition to the URT, the Fund's Reserves and other precautionary balances (now totaling SDR 5 billion) have the effect of lowering operational expenses because they allow the Fund to reduce the amount of currency obtained from creditor members for providing financial assistance to other members. Lower expenses allow the net income target to be met with less income from charges. The rate of charge can therefore be lower than if there were no interest-free resources.

[13] As explained in Pamphlet No. 45 (revised) "The gold tranche was never remunerated historically, so it was natural to set aside this same amount in terms of SDR on this date as the unremunerated reserve tranche".(URT). For countries joining the IMF after April 1, 1978 the URT was calculated as the average, relative to quota, applicable to all existing members on the date that the new member joins the Fund.

[14] J.J.Polak: Streamlining the Financial Structure of the IMF (Princeton Essays in International Finance, No 216), September 1999.

[15] See paper titled Financing the Fund's Operations – Review of Issues (04/11/2001)

[16] Annual Report, FY 2002 (p.67)

[17] Most technical assistance is provided on a grant basis, even though it is no longer meant exclusively for poorer members.

[18] If Brazil were to make all purchases under the arrangement approved in September 2002, the Fund's exposure to a single country, Brazil, would rise to SDR 25 billion, or about 40% of total credit outstanding. .

[19] The very recent rollover of large Argentine payments obligations raises questions in regard to this policy.

[20] See Concluding Remarks by Acting Chair on the Fund's Policy on Precautionary Financial Balances (11/18/02)

[21] Funds deposited in the SDA belong to the IMF exclusively, not being part of quota resources.

[22] The material in this and the next paragraph draws verbatim from Pamphlet # 45 (p. 53), *op.cit*.

[23] Staff Paper cited in fn # 13 *supra*

[24] Of the $ 4.6 billion in profits from the gold sales, $ 1.3 billion was distributed to developing member-countries in proportion to their quotas, while $ 3.3 billion was made available for concessionary lending through the Trust Fund.

[25] The change from ESAF to PRGF is claimed to be more than a change in nomenclature. There is now "an explicit focus on poverty reduction in the context of a growth oriented economic strategy."(Annual Report, FY 2002) p.61

[26] It is notable that with the exception of two developing countries (China and Egypt) all loan resources were provided by developed countries, including five of the G-7 countries (the USA and the UK being non-contributors).

[27] Annual Report, FY 2002, p.62-63 are quoted extensively for the numbers in this and the next paragraph.

[28] The Reserve Account was set up to provide security to bilateral lenders to the PRGF Trust and to cover the cost of administering PRGF operations. The balance in this Account is projected to be sufficient to cover all outstanding PRGF Trust obligations to lenders by around 2007. Once that point is reached, Reserve Account balances are freed to help subsidize the continuation of PRGF operations.

[29] See study by Nancy Birdsall and John Williamson (with Brian Deese) titled Delivering on Debt Relief From IMF Gold to a New Aid Architecture (Center for Global Development, Institute for International Economics0 April 2002.The study proposes mobilizing IMF gold to cover the IMF share of the cost of deepening and including additional countries in the Initiative ($ 9 billion) and the establishment of a contingency facility ($ 5 billion).

Table 1. Relative Burden on Members of Financing the Fund's Administrative Expenses, Precautionary Balances, and Imputed Interest Costs, FY 1982-2002 1/

(in millions of SDRs and percent)

	Items in Excess of Remuneration Expense and Cost of Borrowing						Debtors' Share			Creditors' Share			Relative Contribution (in percent) 4/	
FY	Administrative expenses	Net income	Deferred charges	SCA-1	SCA-2	Total actual cost	Charges in excess of net operational expenses 2/	Burden-sharing contributions	Sub-total	Imputed costs - NRT 3/	Burden-sharing contributions	Sub-total	Debtors	Creditors
1982	153.3	92.1	0.0	0.0	0.0	245.4	245.4	0.0	245.4	641.4	0.0	641.4	27.7	72.3
1983	191.4	65.4	0.0	0.0	0.0	256.8	256.8	0.0	256.8	497.0	0.0	497.0	34.1	65.9
1984	192.8	73.0	0.0	0.0	0.0	265.8	265.8	0.0	265.8	436.4	0.0	436.4	37.9	62.1
1985	224.2	(29.8)	0.0	0.0	0.0	194.4	194.4	0.0	194.4	478.2	0.0	478.2	28.9	71.1
1986	223.4	78.1	0.0	0.0	0.0	301.5	301.5	0.0	301.5	411.9	0.0	411.9	42.3	57.7
1987	190.9	86.0	182.2	26.5	0.0	485.6	276.9	117.7	394.6	349.3	91.0	440.3	47.3	52.7
1988	175.1	49.1	153.7	60.4	0.0	438.3	224.2	107.1	331.3	340.0	107.0	446.9	42.6	57.4
1989	172.7	54.2	224.8	62.9	0.0	514.6	226.9	144.0	370.9	413.6	143.8	557.4	40.0	60.0
1990	188.6	85.5	235.3	65.0	0.0	574.4	274.1	150.2	424.3	502.0	150.1	652.1	39.4	60.6
1991	189.4	69.9	210.3	69.8	142.3	681.7	259.3	181.6	440.9	500.9	240.8	741.7	37.3	62.7
1992	232.2	89.9	190.0	73.4	156.3	741.8	322.1	189.3	511.4	398.0	230.4	628.4	44.9	55.1
1993	263.3	70.6	139.4	78.3	177.0	728.6	333.9	172.1	506.0	342.7	222.6	565.3	47.2	52.8
1994	318.0	74.1	94.1	82.0	161.2	729.4	392.1	139.6	531.7	271.1	197.7	468.8	53.1	46.9
1995	288.3	85.1	96.0	85.2	130.3	684.9	373.4	101.4	474.8	293.8	210.1	503.9	48.5	51.5
1996	301.3	89.3	64.4	92.0	174.2	721.2	390.6	92.0	482.6	271.4	238.6	510.0	48.6	51.4
1997	316.8	93.8	47.4	94.8	58.6	611.4	410.6	82.8	493.4	251.2	118.0	369.2	57.2	42.8
1998	368.5	98.5	48.7	99.4	0.0	615.1	467.0	74.6	541.6	266.3	73.5	339.8	61.4	38.6
1999	392.1	106.7	42.4	107.4	0.0	648.6	498.8	74.8	573.6	243.2	75.0	318.2	64.3	35.7
2000	448.4	267.7	42.4	128.5	0.0	887.0	716.1	85.9	802.0	239.8	85.0	324.8	71.2	28.8
2001	384.6	166.6	48.7	94.0	0.0	693.9	551.2	71.5	622.7	292.1	71.2	363.3	63.2	36.8
2002	530.8	46.2	35.0	94.0	0.0	706.0	577.0	64.0	641.0	148.6	65.0	213.6	75.0	25.0

1/ This table is based on the following assumptions: (a) the Fund's "cost of funds," i.e., its payments to creditors, are excluded, and the table attempts to quantify the relative contributions of debtor and creditor members to financing the Fund's "other costs," which are defined to be equal to the total of the first five items (administrative expenses, net income, deferred charges, SCA contributions) plus the imputed cost of the non-remunerated reserve tranche position; (b) debtor members are assumed to finance administrative expenses and net income (because of the method of determining the rate of charge); and (c) creditor members pay for the imputed cost of the nonremunerated reserve tranche positions (i.e. the table assumes zero holdings of nonremunerated reserve tranche positions by debtor members).

2/ Contribution by debtors through charges in excess of the amount needed to cover remuneration expense and the cost of borrowing. This is equivalent to the total of administrative expenses and net income, excluding income derived from surcharges starting in FY 98, and certain windfall gains from the introduction of a new accounting standard in FY 2000.

3/ Cost of holding the nonremunerated reserve tranche (NRT) is calculated at the average rate of remuneration in effect each year.

4/ Based on the total of actual and imputed costs.