JEB HENSARLING, TX, CHAIRMAN

United States House of Representatives
Committee on Financial Services
Washington, D.C. 20515

MAXINE WATERS, CA, RANKING MEMBER

M E M O R A N D U M

To: Members of the Committee on Financial Services

From: FSC Majority Committee Staff

Date: April 19, 2013

Subject: April 24, 2013, Monetary Policy and Trade Subcommittee Hearing on "Evaluating U.S. Contributions to the International Monetary Fund"

On Wednesday, April 24, 2013, at 2:00 p.m. in Room 2128 of the Rayburn House Office Building, the Financial Services Subcommittee on Monetary Policy and Trade will hold a hearing on "Evaluating U.S. Contributions to the International Monetary Fund." This hearing will examine the Obama Administration's request to Congress to authorize governance reforms at the International Monetary Fund (IMF) and increase the U.S. quota share by about $63 billion.

The hearing will be a one-panel hearing with one witness, Undersecretary of the Treasury for International Affairs Lael Brainard.

Overview of the IMF[1]

The IMF is an international organization whose purpose is to promote international macroeconomic stability. The IMF traces its roots to the July 1944 meeting at Bretton Woods, New Hampshire, where representatives from 45 nations gathered to discuss the postwar recovery of Europe and to create international institutions to resolve some of the economic problems—such as protectionist trade policies and unstable exchange rates—that hobbled the international economy between the two world wars. Two other international organizations also trace their origins to the Bretton Woods conference: the World Bank, whose mission is poverty reduction and economic development, and the World Trade Organization, which seeks to liberalize international trade and oversees the rules governing the international trade system. The IMF came into formal existence in 1945, and has grown to near-global membership of 188 countries today.

As the global financial system has evolved over the decades, so has the IMF. Until the early 1970s, the IMF's primary purpose was to manage the system of fixed exchange rates agreed to at Bretton Woods. The U.S. dollar was fixed to gold at $35 per ounce and all other member countries' currencies were fixed to the dollar at different rates. The IMF monitored the macroeconomic and exchange rate policies of its member countries, and helped them weather economic crises by providing them with short-term loans. The global system of fixed exchange

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[1] For more background on the IMF, see Martin A. Weiss, "International Monetary Fund: Background and Issues for Congress," CRS Report for Congress, (March 21, 2013), available at http://www.crs.gov/Products/R/PDF/R42019.pdf .

rates abruptly ended in 1973, when the United States went off the gold standard and floated its currency. After a period of instability, the modern system of floating exchange rates came into effect. The IMF adapted to the new system of floating exchange rates by promoting stable exchange rates while continuing to provide temporary financing to countries affected by economic crises.

Today, the IMF's operations can be grouped into three categories: surveillance, lending, and technical assistance:

- **Surveillance:** The IMF monitors the economic and financial policies of its member countries to identify possible risks to financial stability and to offer advice on policy adjustments.

- **Lending:** The IMF lends to countries facing balance-of-payments problems, which generally means they are having trouble paying for imports or servicing their debt. The IMF provides temporary financial assistance to enable these countries to stabilize their economies while implementing economic reforms. The IMF disburses its loans in phases ("tranches") after verifying that specified economic conditions and reforms have been met ("conditionality").

- **Technical Assistance:** The IMF provides technical assistance and training to help its member countries strengthen their capacity to design and implement effective policies. The IMF provides technical assistance in monetary and financial policies; fiscal policy and management; statistical data compilation; and economic and financial legislation.

The IMF has not been without controversy, and increased attention on its activities since the global financial crisis of 2008-2009 and subsequent Eurozone crises have revived long-standing debates about the institution's role in the global economy. Some analysts argue that with the end of fixed exchange rates, the IMF is no longer needed and it should be abolished. Others say the IMF is still vital, but needs to be restructured and refocused. Still others suggest that new functions should be added to the IMF and its role in the international monetary system should be expanded.

The Role of the United States in the IMF

Financial Commitment and Voting Power

As one of the IMF's founding members and its largest shareholder, the United States plays a major role in shaping its surveillance, lending, and technical assistance activities. The

United States has committed about $63 billion to the IMF's core source of funding, called quota.[2] The United States has the largest quota share (17.69%) of any IMF member.

Quota share is tied to voting share, and the United States also has the largest voting power of any member: 16.75%. This voting share gives the United States veto power over major policy decisions that require an 85% supermajority vote. No other single IMF member has a similar veto power. Even though quota share is in theory tied to a country's weight in the global economy, U.S. quota share (17.69%) is actually smaller than its share of global GDP (22% in 2012).[3] Over the years, the United States has let its quota share fall, to facilitate other countries joining the IMF and to reduce its financial commitment to the IMF relative to other member countries, while retaining its unique veto power.

In addition to quota, the United States has also committed resources to "supplementary" funds at the IMF. These are funds that can be tapped when demand for IMF resources is particularly strong, such as during major financial crises. The IMF has two supplementary funds: the New Arrangements to Borrow (NAB) and the General Arrangements to Borrow (GAB). The United States has committed about $103 billion to the NAB (18.67% of total NAB resources), and about $6 billion to the GAB (25% of total GAB resources). U.S. financial contributions to the IMF, including to IMF quota and the supplementary funds, are not grants. Instead, they are lines of credit extended by the United States to the IMF. The United States earns a small amount of interest when the IMF taps U.S. commitments to fund IMF programs.

U.S. Policy-Making Process

U.S. policy at the IMF is made by the executive branch and Congress. Within the executive branch, the Treasury Department has primary responsibility for managing U.S. participation in the IMF. The President appoints U.S. representatives to the IMF Board of Governors and IMF Board of Executive Directors, with the advice and consent of the Senate. The IMF's Board of Governors is the highest decision-making body at the IMF, meeting a few times each year to make major policy decisions. Every IMF member has its own representative on the Board of Governors; the U.S. representative is the Treasury Secretary.

The IMF's Board of Executive Directors manages the IMF's day-to-day operations and generally meets several times a week. The Executive Board has 24 members. Some Executive Directors represent groups of countries, while others represent individual countries. Because of its large quota share and voting power, the United States has its own representative on the Executive Board.

Congress also plays a role in formulating U.S. policy at the IMF. In addition to Senate confirmation of U.S. representatives to the IMF, Congress authorizes and appropriates all U.S. financial commitments to the IMF. The House Committee on Financial Services and the Senate

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[2] The IMF denominates values in special drawing rights (SDRs), a basket of international currencies. In this memo, dollar figures have been converted from SDRs using the exchange rate on March 28, 2013 of $1.4980/SDR (Source: IMF). Because of fluctuations in the exchange rate, the dollar amounts in this memo are approximations.

[3] International Monetary Fund (IMF), *World Economic Outlook*, October 2012.

Committee on Foreign Relations are the authorizing committees, and the Foreign Operations Subcommittees of the House and Senate Committees on Appropriations manage the relevant appropriations legislation.

Over the years, Congress has also passed several legislative mandates that have shaped U.S. policy at the IMF. Legislative mandates typically fall into three categories. First, "voice and vote" mandates direct the U.S. Executive Director to promote specific policies at the IMF and to vote for such policies. Second, directed voting mandates require the U.S. Executive Director to vote against or abstain in votes relating to certain types of programs or policies. The final type, reporting requirements, requires the Treasury Department to report to Congress on issues related to U.S. participation in the IMF.

U.S. Interests

There is disagreement about whether the U.S.'s participation in the IMF serves U.S. interests. Some argue that U.S. participation advances U.S. economic interests by reducing the impact of financial crises in other countries on the U.S. economy and promoting the development of overseas markets for U.S. exports. These supporters also maintain that the IMF promotes U.S. national security interests by fostering economic stability in fragile states, where economic instability could otherwise breed political instability. Finally, supporters also argue that U.S. leadership in the IMF allows the United States to influence IMF policy in areas deemed critical by the United States and to leverage U.S. financial commitments to promote macroeconomic stability with financial contributions from 187 other countries.

Others are more skeptical and see the IMF as an enabler of moral hazard. They are concerned that taxpayer dollars are being used to fund IMF programs to bail out governments that have implemented irresponsible fiscal and monetary policies. They argue that the availability of funding from the IMF reduces incentives for governments to adopt difficult, but prudent, economic policies. Opponents also point out that the IMF is often unpopular in countries receiving IMF assistance, typically because of the conditions attached to IMF loans which often require recipients to adopt unpopular austerity measures. In some cases, public anger is also directed towards the United States, which is seen by some citizens of borrowing countries as responsible for the policy prescriptions imposed by the IMF as a condition for receiving funds.

Governance and Quota Reform at the IMF[4]

In December 2010, the IMF's Board of Governors agreed to a reform package that would make two major changes: (1) it would nearly double the size of the IMF's quota resources; and (2) it would increase the representation of emerging and developing economies at the IMF. The reform package cannot go into effect until a supermajority of IMF countries formally approve the reforms.

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[4] For more details on the 2010 reform package, Rebecca M. Nelson and Martin A. Weiss, "IMF Reforms: Issues for Congress," CRS Report for Congress (Feb. 1, 2013), available at http://www.crs.gov/Products/R/PDF/R42844.pdf.

Although the IMF's rules do not require that all of its member countries approve the reform package, the United States must approve the package for it to become effective because its voting share is necessary to reach the required 85% supermajority for the reforms to be implemented. Although most other IMF member countries have formally approved these reforms, the United States has not yet approved them. Under U.S. law, the Obama Administration cannot do so without specific congressional authorization.

Depending upon how the Congressional Budget Office (CBO) scores the change, Congress may also need to appropriate funds for these reforms to become effective because they increase U.S. quota resources by about $63 billion, even though they cut the equivalent amount from the New Arrangements to Borrow (NAB). Even with the increase in U.S. voting share, the share of U.S. voting power at the IMF would fall slightly, but the United States would still maintain its unique veto power over major policy decisions. The United States would also likely retain its own representative on the Executive Board.

Proponents of the reform package argue that it is necessary for maintaining the effectiveness and legitimacy of the IMF as the central institution for international macroeconomic stability. Proponents argue that the IMF's core funding needs to be increased to give it the resources that it needs to respond effectively to financial crises in a globalized economy. They also maintain that the under-representation of emerging economies at the IMF is broadly perceived as unfair and reduces the support of several member countries for IMF programs and initiatives. They suggest that it is better to encourage emerging powers—like Brazil, China, India, Russia, and South Africa (the BRICS)—to participate in existing international organizations, rather than run the risk that these nations establish their own institutions, which may pursue policies that are not consistent with U.S. interests.

Opponents of the reform package maintain that because the IMF has found other ways to supplement its resources during economic crises, particularly through the NAB, the IMF's core funding does not need to be increased. They also argue that the IMF could be more judicious in its lending programs, and that recent IMF programs in the Eurozone have been ill-advised, because advanced Eurozone economies have the resources they need to resolve their crises. Opponents are also skeptical that emerging economies support the existing norms and values of international financial institutions. They are concerned that giving countries like China and Brazil a greater voice in the institution may result in financial and trade policies that are less aligned with U.S. interests.

Although the IMF's Board of Governors agreed to the reform package in 2010, the Administration did not request the $63 billion quota increase in its FY2012 or FY2013 budget requests. News reports indicate that the Administration was holding off on the request until after the 2012 elections. [5] In March 2013, the Administration approached the House and Senate about including the reform package in the continuing resolution. The IMF legislation was not included in the House or Senate version of the legislation, nor was it included in the final bill that was

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[5] Lesley Wroughton and David Lawder, "Senate Rebuffs Obama Request to Shift Funds for the IMF," Reuters (March 12, 2013), available at http://www.reuters.com/article/2013/03/12/us-usa-imf-reforms-idUSBRE92B04K20130312.

passed into law. President Obama also declined to request legislation in his FY2014 budget request, instead noting "the required authorization requests, including for mandatory funding for the IMF quota increase and NAB rollback, will be submitted separately."[6]

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[6] U.S., Department of the Treasury, "Justification for Appropriations: FY 2014 Budget Request, U.S. Department of Treasury, International Programs" (March 2013), at p. 45, available at http://www.treasury.gov/about/budget-performance/Documents/FY2014_Treasury_International_Programs.pdf.