

**IMPLEMENTATION OF
CERTAIN LEGISLATIVE PROVISIONS
RELATING TO THE
INTERNATIONAL MONETARY FUND**



A Report to Congress

in accordance with

Sections 1503 and 1705(a) of the
International Financial Institutions Act,

Section 801(c)(1)(B) of the
Foreign Operations, Export Financing, and Related Programs
Appropriations Act, 2001

and

Section 605(d) of the
Foreign Operations, Export Financing, and Related Programs
Appropriations Act, 1999

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Introduction

This is the ninth report prepared in accordance with Sections 1503 and 1705(a) of the International Financial Institutions Act (the IFI Act – codified at 22 United States Code sections 262o-2 and 262r-4(a)).¹ This report also covers policies set forth in Section 801(c)(1)(B) of the Foreign Operations, Export Financing, and Related Programs Appropriations Act, 2001,² as required by Section 1705(a) of the IFI Act. The report reviews actions taken by the United States to promote these legislative provisions in International Monetary Fund (“IMF” or the “Fund”) country programs. Annex 1 covers new IMF lending arrangements per section 605(d) of the Foreign Operations, Export Financing, and Related Programs Appropriations Act, 1999. Earlier reports under these provisions are available on the Department of the Treasury’s website (www.treas.gov/press/reports.html).

Treasury and the Office of the United States Executive Director (“USED”) at the IMF consistently endeavor to build support in the IMF’s Executive Board for the objectives set out in this legislation. These endeavors include meetings with IMF staff and other Board members on country programs and IMF policies, formal statements by the USED in the IMF Board, and USED votes in the Board. Treasury’s objective is to support strengthened commitments in IMF programs, policy actions by program countries, and policy decisions at the IMF itself.

Treasury’s IMF task force is charged with increasing awareness among Treasury staff about legislative mandates and identifying opportunities to influence IMF decisions in line with broader U.S. international economic policy objectives. Assessments of the overall effectiveness of the Treasury and USED’s office in promoting the legislative provisions are published annually by the GAO and are available online.³ The most recent report states that the “Treasury continues to promote the [IMF] task force as a tool for monitoring and promoting legislative mandates and other policy priorities.”

Report on specific provisions

I. Section 1503(a)

(1) Exchange rate stability

Article I of the IMF’s Articles of Agreement states that one of the purposes of the IMF is “to promote exchange stability, to maintain orderly exchange arrangements among members, and to avoid competitive exchange depreciation.” In June, 2007, as a result of U.S. leadership, the IMF adopted a new framework for exchange rate surveillance. A key feature of this framework is the concept of fundamental misalignment. A country’s exchange rate can be found fundamentally misaligned if it substantially deviates from its long run equilibrium level and if it is coupled with

¹ These provisions were enacted in Sections 610 and 613 of the Foreign Operations, Export Financing, and Related Programs Appropriations Act, 1999 (Public Law 105-277, division A, § 101(d), title VI, §§ 610 & 613). Section 1705(a) was amended by Section 803 of the Foreign Operations, Export Financing, and Related Programs Appropriations Act, 2001 (Public Law 106-429, title VIII, § 803).

² Public Law 106-429, title VIII, § 801(c)(1)(B).

³ *Treasury Has Sustained Its Formal Process to Promote U.S. Policies at the International Monetary Fund*, Government Accountability Office (GAO), June 2006.

a persistent misalignment in the current account. A finding of fundamental misalignment does not, in itself, imply a sanction by the Fund. However, it would sharpen the discussion on whether the country's exchange rate policy has a detrimental impact on the rest of the world. If a country were found to be fundamentally misaligned with the intent of increasing net exports, the Fund could find the country to be manipulating its currency in violation of its obligations under the IMF's articles of agreement.

This new framework is in the process of being implemented. Some Article IV's have been delayed, including China's, in order to incorporate the new framework into the Article IV reviews.

Treasury has urged the Fund to exercise firm surveillance over exchange rates throughout the year, as the new framework was being formulated.

- In its Board statement at the September 2007 Article IV discussions on the Republic of Korea, the USED underscored Korea's strong growth in a flexible exchange rate regime and the role of exchange rate appreciation in mitigating inflationary pressures.
- In its July 2007 statement on the Article IV review of Brazil, the USED noted that heavy intervention resulted in substantial reserve accumulation. It stated that given the Central Bank of Brazil's high level of reserves, intervention is more costly than the alternative options for preventing the development of an overvalued real exchange rate and that concerns about exchange rate overshooting could be better addressed through countercyclical fiscal policy.
- In its December 2006 board statement on the Article IV review of India, the USED noted that India's flexible exchange rate regime will support the economy's adjustment as well as encourage the recognition and hedging of foreign exchange risk. It also emphasized that there is scope for additional flexibility in the application of the exchange rate policy which is particularly important as India moves toward greater integration with the global economy.
- In its Board statement at the October 2006 Article IV discussions on Russia, the USED noted that heavy intervention in the foreign exchange market has led to significant money supply growth and that negative real interest rates have helped fuel an asset price boom. The USED highlighted that given that Russia now has the world's third largest foreign exchange reserves and a current account surplus of 11 percent of GDP, the authorities should cease intervening in the foreign exchange market and rather focus monetary policy directly on steadily reducing inflation.

(2) Policies to increase the effectiveness of the IMF in promoting market-oriented reform, trade liberalization, economic growth, democratic governance, and social stability through:

(A) Establishment of an independent monetary authority

With the support of the United States, the IMF has been a consistent advocate of greater independence of monetary authorities across a range of countries. IMF conditionality frequently includes measures to strengthen central bank autonomy and accountability. The IMF also provides technical assistance to help countries achieve these goals. In addition, the Fund promotes these objectives through assessments of compliance with internationally-agreed upon standards and codes, as well as rules for safeguarding the use of IMF resources. Examples of United States activities in the last year with regard to these issues include the following:

- In its Board statement at the July 2007 Article IV discussions, the USED urged that the Brazilian Central Bank be granted full autonomy, especially given Brazil's recent success in anchoring the market's inflation expectations.
- In its statement on Pakistan's November 2006 Article IV review, the USED noted that a strong and independent central bank will continue to be a key to macroeconomic stability.

(B) Fair and open internal competition among domestic enterprises

Though the World Bank has the lead mandate on these issues, with United States support the IMF encourages member countries to pursue policies that improve internal economic efficiency. These measures may include ending directed lending (or other relationships between government and businesses based on favoritism), improving anti-trust enforcement, and establishing a sound and transparent legal system. For example,

- In a January 2007 Board Statement on Swaziland's Article IV review, the USED urged authorities to remove legal, regulatory, and administrative barriers to business establishment and operation in an effort to promote private sector-led economic development.

(C) Privatization

The IMF has made privatization a component of country programs where significant distortions and government ownership of business enterprises have created substantial inefficiencies in the allocation of resources and the production of goods. Collaborating with the World Bank, the Fund has supported the use of competitive and transparent means of privatization so that borrowing countries might achieve gains in economic efficiency and improve their fiscal positions. Examples of IMF programs and surveillance discussions in which the USED has advocated privatization include the following:

- In an August 2007 board statement for the Iraq Article IV, the USED commended the liberalization of fuel imports and encouraged Iraqi authorities to push for quick passage and implementation of a suite of hydrocarbons laws to encourage private investment in oil production.
- In a December 2006 Board statement on the second review of Cameroon's Poverty Reduction and Growth Facility, the USED urged the government to move forward with the privatization

of the government-owned airline, telecom company and water parastatal, noting that further delay would require additional government subsidization.

- In an April 2007 Board statement on a Poverty Reduction and Growth Facility for Burkina Faso, the USED encouraged Burkina Faso authorities to continue efforts for the government to reduce the government's ownership stake in SOFITEX, the country's largest cotton company and a central player in the critical cotton sector.

(D) Economic deregulation and strong legal frameworks

Markets are distorted and entrepreneurship is stifled without strong property rights, enforcement of contracts, and fair and open competition. While these issues are often addressed as part of the World Bank's mandate, the IMF periodically includes such policy advice in its programs or surveillance on measures considered critical to the member country's macroeconomic performance. Examples of United States' efforts to encourage these reforms include the following:

- In the August, 2007 Article IV review for Uruguay, the USED urged Uruguayan authorities to support increased financial intermediation through promoting banking sector competition, reforming state-owned banks, and strengthening bank supervision and regulation.
- In the December, 2006 Article IV review for India, the USED emphasized that an inefficient dispute resolution system, the lack of binding international arbitration and the backlogged domestic court system remain major deterrents to foreign investment in critical infrastructure projects.

(E) Social safety nets

While growth is an essential ingredient for poverty reduction, investment in human development and basic social services is also critical. Cost effective social safety nets can play an important role in building domestic support for economic reform, and in alleviating the direct impact of poverty.

The IMF does not lend directly for budget support to build social safety nets. However, the Fund's policy advice and its focus on macroeconomic stability encourage domestic policy makers to develop fiscal strategies that address the needs of the poor. Reducing generalized subsidies while protecting pro-poor spending, for example, is a common theme. In the poorest countries, IMF advice is developed within a country-specific poverty reduction strategy (PRS) that encourages accountability between donors and recipients.

- In the June 29, 2007 Board review of Paraguay's Stand-by Arrangement, the USED advocated increased expenditure on poverty reduction in Paraguay, financed by increased revenues from reforms to broaden the tax base.

(F) Opening of markets for agricultural goods through reductions in trade barriers

The IMF encourages a multilateral, rules-based approach to trade liberalization across all sectors of the global economy, including, but not limited to, the agricultural sector. The IMF has played a supportive role in promoting trade liberalization, particularly in the context of the WTO trade negotiations under the Doha Development Agenda (DDA). In April 2004, the Fund approved the Trade Integration Mechanism (TIM) to provide financial support to countries facing balance of payments problems resulting from trade adjustment. The proposal represents a concrete response to developing country concerns about the potential negative impacts from multilateral trade liberalization. The IMF is prepared, along with the World Bank, to provide transitional assistance to member countries experiencing payment imbalances arising from the passage of trade reform.

(3) *Strengthened financial systems and adoption of sound banking principles and practices*

The joint IMF-World Bank *Financial Sector Assessment Program* (“FSAP”) has emerged as a critical instrument for financial sector surveillance and advice. As of end-September 2007, 116 countries have completed FSAP assessments and 24 countries have completed FSAP update assessments. Twenty-eight reviews are underway or planned.

Results from the FSAP are used to generate assessments of compliance with key financial sector standards such as the Basel Committee’s *Core Principles for Effective Banking Supervision*, the International Organization of Securities Commission’s *Objectives and Principles of Securities Regulation*, and the IMF’s own *Code of Good Practices on Transparency in Monetary and Financial Policies*. The FSAP assessment results are summarized in *Financial System Stability Assessments* (“FSSA”) which are often provided to the public. Some key examples of where the USED has supported the strengthening of financial systems are:

- In its May, 2007 Board statement on Turkey’s 6th review of its Stand-by Arrangement the USED noted that Government of Turkey supervisory capacity has improved substantially, while the legislative framework is being modernized with the new Banking Law, the Mortgage Law, and prospective legislation on insurance and capital markets.
- In its statement on Japan’s Article IV review in July 2007, the USED called for greater focus on consumer and investor protection, based on information disclosure, and risk management measures. The USED emphasized the need for such efforts to respond to Japanese investors’ increased appetite for risk and investment abroad, and the need to increase the return on savings for retirement.
- During the IMF Board discussion on Brazil’s Article IV review in July 2007, the USED supported policies that would foster financial intermediation, further reductions in directed lending, gradual phase out of the financial transactions tax, phase-out of credit quotas to specific sectors, and reorientation of the state-owned development bank toward market-oriented lending.

(4) *Internationally acceptable domestic bankruptcy laws and regulations*

The IFIs have continued to build upon work started after the Asian financial crisis to promote more effective insolvency and debtor-creditor regimes. While the World Bank normally leads reviews of domestic insolvency laws, the IMF actively supports this agenda. Both the UN Commission on International Trade Law (UNCITRAL) and the World Bank have worked to compile recommendations in this area covering, respectively, insolvency law and sound insolvency/creditor rights regimes. At the urging of the United States, staff from the World Bank, IMF and UNCITRAL worked together to develop a standardized, unified assessment methodology to assess implementation of those recommendations. The Financial Stability Forum, also with strong U.S. support, has called on World Bank and UNCITRAL staff to continue this cooperation and complete a concise, unified international standard for insolvency and creditor rights.

The IFIs also provide technical assistance to help emerging market economies develop efficient insolvency regimes. The IMF and the World Bank have supported adoption of the Model Law on Cross-Border Insolvency developed by the UN (the UNCITRAL Model Law) to facilitate the resolution of increasingly complex cases of insolvency where companies have assets in several jurisdictions. With the support of the United States, the IMF has worked with the World Bank to promote improved insolvency regimes in a number of countries.

(5) Private sector involvement

The United States continues to work to ensure that the private sector plays an appropriate role in the resolution of financial crises. Over the past several years, the IMF, with the support of the United States, has taken important steps towards strengthening crisis prevention and resolution. The IMF has strengthened its surveillance of member countries and instilled more discipline in the use of official sector financing, especially through the establishment of rules and procedures governing exceptional access to Fund resources. Additionally, the use of collective action clauses (see Section C, below), supported by the IMF as an accepted contractual, market-based approach to sovereign debt restructurings, should help a sovereign restructure its debt when under financial distress. The IMF recognizes the need to preserve the fundamental principles that (a) creditors should bear the consequences of the risks they assume, and (b) debtors should honor their obligations.

In particular, the United States has advocated policies that include:

(A) Increased crisis prevention through improved surveillance and debt and reserve management

The United States has urged the IMF to strengthen further its surveillance function and crisis prevention capabilities. In May 2007, the Board discussed an IMF staff paper on strengthening debt management which provided a stocktaking of the IMF and World Bank's experience in helping middle- and low-income countries in strengthening debt management practices. The Board noted that the development of clear operational frameworks to identify, monitor, and manage balance sheet and market risks would be helpful for middle- and low-income countries and the USED supported a four-year pilot project for providing technical assistance to three to

four low-income countries per year to help them build the capacity to develop and implement an effective medium-term debt management strategy.

The USED has also supported the balance sheet approach to measure vulnerabilities in emerging markets and has called for greater focus on debt sustainability in both low-income and emerging market countries.

- In its October, 2006 Article IV Board statement, the USED commended Colombia's performance in reducing its debt ratio to a predicted 40% or less of GDP by 2010, and encouraged continued debt reduction and prudent fiscal policies.
- In its January 26, 2007 review of the Peru Stand-By Arrangement, the USED welcomed authorities' efforts to re-balance the currency denomination of debt towards domestic currency, reducing the government's vulnerability to exchange rate volatility.
- In its July 18, 2007 Article IV response, the USED supported Indonesia's fiscal stance which aims to reduce public debt, and noted that this goal remains appropriate.

The IMF continues to encourage, with strong United States support, member countries to make their economic and financial conditions more transparent. Countries are urged to provide additional information to private market participants by publishing Article IV assessments and program documentation as well as by regularly releasing data consistent with the IMF's Special Data Dissemination Standard (SDDS).

- Fund members subscribing to either the General or Special Data Dissemination Standards (SDDS) increased from 75% of all members in 2005 to 82% in 2006, and 83% in 2007.
- In its October 2006 statement on Burma's September 2006 Article IV review, the USED noted that economic data continues to not be transparent to outside observers and the Burmese public and found that IMF surveillance and formulation of policy recommendations are hindered by questionable transparency and data shortcomings.
- In its November 2006 statement on India's Article IV review, the USED encouraged the Indian authorities to adopt the methods outlined by SDDS and to publicize current statistics.
- In its Board statement at the September 2007 Article IV discussions on the Republic of Korea, the USED emphasized that that it would welcome a greater degree of transparency from Korean authorities regarding the timing and magnitude of their foreign exchange interventions.

(B) Strengthening of emerging markets' financial systems

The IMF continues to work with other IFIs to promote stronger financial systems in emerging market economies (see Section 3). The IMF and the World Bank reviewed coordination of their assistance efforts and the results of this review were set forth in the Malan Report which was published in February 2007. This report notes that the IMF and the World

Bank are the only IFIs with near universal membership, and that both of these institutions play an important role in helping emerging economies address the challenges of globalization, and obtain its benefits. The report recommended that future cooperation be based on the comparative expertise of the two institutions, with the IMF taking the lead in instances where there are significant issues of domestic or global economic stability, and the World Bank leading in instances where financial sector development issues are paramount.

The IMF is also actively involved with the World Bank in monitoring the implementation of the Basel Core Principles for Effective Banking Supervision. The IMF, with United States support, has increased its cooperation with the World Bank in this area, through the joint Financial Sector Assessment Program (FSAP) and in assessing countries' observance of other standards and codes.

Some key examples of where the USED has supported a strengthening of emerging market financial systems are:

- In its statement during the December 2006 IMF Executive Board discussion on India's Article IV consultations, the USED urged the removal of restrictions on banking sector assets, divestiture of government ownership of financial institutions, elimination of the obstacles to development of securitization markets, and improving reporting standards.
- The IMF Board discussed Turkey's Article IV review in May 2007. Welcoming Turkey's recent participation in the FSAP, the USED called for bolstering the bank resolution framework, supported authorities' commitment to bank privatization. The USED's statement encouraged ongoing human capital investment so that bank supervisors can respond effectively to still high levels of deposit dollarization, the large stock of foreign currency loans, and the thin inter-bank markets.
- In its Board statement at the February 2007 Article IV discussions, the USED noted that although Guatemalan authorities made progress in upgrading the bank supervisory framework and implementing the Basel Core Principles, the supervisors still lack sufficient legal authority to conduct effective consolidated supervision, and need to take immediate steps to bolster the crisis management framework, initiate comprehensive special inspection of banks, and recapitalize the deposit insurance fund with public money.
- In its December, 2006 review of the Uruguay Stand-By Arrangement, the USED urged the passage of a financial sector law, along with capitalization of the central bank, as a means of reducing financial sector vulnerabilities.

(C) Strengthened crisis resolution mechanisms

The United States, in cooperation with the IMF and the broader international financial community, has promoted a strengthened framework for crisis resolution through use of collective action clauses (CACs), application of the lending into arrears policy, and clear limits on the use of official finance.

(i) Collective Action Clauses

Sovereign bonds governed by New York law conventionally had not included provisions which would permit modification of key payment terms by less than unanimous consent. This restriction made these bonds harder to restructure when a sovereign experienced financial distress. The United States has worked actively with the IMF and the private sector to promote the market's adoption of CACs in order to improve debt restructuring processes. CACs have now become the market standard for sovereign bonds issued under New York law.

As of August 2007, CACs are included in 66 percent of the stock of external sovereign bonds issued by emerging markets. The IMF, encouraged by the United States, has made CACs an important element of its crisis resolution agenda. The IMF has indicated it will continue to encourage future issuers to follow this trend.

(ii) Lending into Arrears

The IMF lending into arrears policy permits the Fund to provide financial support for policy adjustments, despite the presence of actual or impending arrears on a country's obligations to private creditors, where: (i) prompt IMF support is considered essential for the successful implementation of the member's adjustment program; and (ii) the member is pursuing appropriate policies and is making a good faith effort to reach a collaborative agreement with creditors. IMF efforts in recent years have focused on applying the "good faith" criterion to specific cases, including Argentina, the Dominican Republic, Iraq, and Dominica.

(iii) Clear Limits on Official Finance

The United States continues to press the IMF to improve its lending selectivity. In 2002 explicit criteria were developed for extending loans to countries seeking to borrow beyond normal limits ("exceptional access"). These include: (i) the member must be experiencing "exceptional balance of payments pressures on the capital account" which cannot be addressed with normal resources, (ii) an analysis of sustainable debt levels, (iii) reasonable prospects exist that the member will regain access to private capital markets during the program term, and (iv) the member's policy program can reasonably be expected to succeed. In addition, procedures were introduced to require: (i) a "higher burden of proof in program documentation", (ii) early consultation with the Board on sovereign creditor negotiations, (iii) the issuance of a staff note specifically outlining all of the relevant considerations, and (iv) an ex-post evaluation of such a program within twelve months of its completion.

(6) Good governance

The IMF's commitment to promoting good governance is outlined in its 1996 *Declaration on Partnership for Sustainable Global Growth* and its 1997 *Guidelines on Good Governance*. The IMF also supports good governance through its emphasis on transparency, strong fiduciary diagnostics, and its promotion of market-based reforms.⁴ Recently, the IMF has been

⁴ IMF financing is provided to central banks to address balance of payments difficulties. The IMF does not lend to fund specific projects in member countries aimed at procurement and financial management controls.

particularly active in promoting good governance through its efforts to protect against abuse of the financial system and to fight corruption.

The Fund's involvement has focused on those governance aspects that are generally considered part of the IMF's core expertise, such as improving public administration, increasing government transparency, enhancing data dissemination, and implementing effective financial sector supervision. The IMF promotes best practice principles through its codes and standards, such as the *Code of Good Practices on Fiscal Transparency*, and is collaborating with the World Bank on strengthening the capacity of HIPC countries to track public sector spending. The Fund has worked with the World Bank and other donors to develop 28 Public Expenditure and Financial Accountability (PEFA) indicators, building on the 16 HIPC indicators, to measure and track countries' PMF performance over time. Supplementing this is the Fund's 2005 resource revenue guide, updated in 2007, a complement to the FISC ROSC for use in resource (oil-gas-mining) rich countries. The guide is being used increasingly in diagnostic work in extractive industry intense economies.

Examples of U.S. efforts to encourage good governance include the following:

- In its October 2006 statement on Burma's September 2006 Article IV, the USED observed that ongoing pervasive government control of the Burmese economy continues to generate serious macroeconomic imbalances, resulting in low investment, high and volatile inflation and entrenched poverty.
- In an August 2007 Board Statement on Angola's Article IV review, the USED urged authorities to increase oil and diamond sector transparency to ensure that the country's improved macroeconomic performance translates into lower poverty, a more diversified economy, and increased opportunities for all Angolans.
- During the July 2007 Third Review of Liberia's performance under the staff-monitored program, the USED urged timely passage of anti-corruption legislation to allow the government to continue its pursuit of good governance and greater transparency.
- In meetings with IMF staff, OUSED and Treasury staff encouraged the Fund to accelerate the use of the resource revenue guide in Fiscal ROSCs and to apply it more systematically in relevant Article IV reports.

(7) Channeling public funds away from unproductive purposes, including large "show case" projects and excessive military spending, and toward investment in human and physical capital to protect the neediest and promote social equity

The Fund published a *Code of Good Practices on Fiscal Transparency* in 1998 that aims to enhance fiscal policy transparency, promote quality audit and accounting standards, and reduce or eliminate off-budget transactions, which are often the source of unproductive government spending. The IMF also encourages countries to conduct "public expenditure reviews" with the World Bank.

- In its July, 2007 Article IV review of Bolivia, the USED encouraged Bolivian authorities to enact a new budget framework to strengthen the budget process and control subnational spending.
- In its Board statement at the most recent Brazil Article IV discussions, the USED questioned the value of Brazil's use of fiscal adjustors to the primary surplus, noting that such adjustments tend to cloud fiscal transparency.

(8) Economic prescriptions appropriate to the economic circumstances of each country

The United States has supported flexibility in Fund programs, while emphasizing the need to focus conditionality on issues critical to growth and macroeconomic stability using measurable results. Partly as a result of U.S. efforts, program conditions have focused increasingly on debt and financial vulnerability in middle-income countries and macroeconomic management in low-income countries. In low-income countries, the U.S. has supported the use of Poverty Reduction Strategy Papers ("PRSP"), which are developed by local authorities and civil society and help ensure that IMF programs meet specific needs of the country.

(9) Core labor standards (CLS)

Core labor standards provide a useful benchmark for assessing countries' treatment of workers against internationally agreed-upon standards. The State Department monitors labor standards in all IFI borrower countries and Treasury is mandated to submit a separate report to Congress assessing progress made with respect to internationally recognized worker rights.

(10) Discouraging practices that may promote ethnic or social strife

By helping to create the conditions for a sound economy, IMF assistance facilitates the reduction of ethnic and social strife, to the extent such strife is driven in part by economic deprivation. For example, with United States support, the IMF has increasingly encouraged the strengthening of social safety nets. The IMF also encourages consultation with various segments of society in the development of programs so that these segments have an opportunity to participate in the implementation of national priorities. IMF assistance has helped to free up resources for more productive public investment by contributing to a reduction in country military expenditures.

(11) Link between environmental and macroeconomic conditions and policies

With respect to its individual lending operations, the IMF does not itself evaluate positive or negative linkages between conditions and environmental sustainability. Rather, the IMF coordinates with the World Bank which, unlike the IMF, possesses the internal expertise to address such linkages. The United States has encouraged the inclusion of conditions on environmental issues in cases where such issues have significant macroeconomic consequences.

- In the August 2007 statement on Laos' July Article IV review, the USED noted that a transparent and predictable resource revenue management framework would help maximize the benefits of Lao's vast natural resources and strongly recommended that the authorities participate in the Extractive Industries Transparency Initiative and adhere to the Fund's guidelines on resource revenue management.

(12) *Greater transparency*

Over the last several years, the IMF has increased significantly the amount of information on its programs that it has made available to the public. The United States has stressed the need to build on this progress and expand the number of publications and IMF practices open to public scrutiny. As of July 2004, publication of all Article IV and Use of Fund Resources staff reports is presumed unless a country objects. In addition, all exceptional access reports will generally be published as a pre-condition for the Board's approval of such an arrangement.⁵ The USED consistently encourages countries to publish the full Article IV staff report on the IMF's public website. The percentage of staff reports published increased from 78 percent in 2004 to 84 percent in 2006.

(13) *Greater IMF accountability and enhanced self-evaluation*

In April 2000, with the strong urging of the USED, the Executive Board agreed to establish an Independent Evaluation Office ("IEO") to supplement existing internal and external evaluation activities. The IEO provides objective and independent evaluation on issues related to the IMF and operates independently of Fund management and at arm's length from the IMF Board. Since its inception, the IEO has published thirteen comprehensive reviews, including recent assessments of the IMF's structural conditionality, exchange rate policy advice, and aid to Sub-Saharan Africa. All reports are publicly available on the IEO's website at (<http://www.imf.org/external/np/ieo/index.htm>).

In response to recommendations of a 2002 IEO study on prolonged use of IMF resources, the IMF now requires "Ex Post Assessments" (EPAs) of IMF engagement in countries where the IMF has had a program in place for at least 7 out of the past 10 years. The EPAs are intended to provide a long-term, arms-length perspective and are led by someone other than the country mission chief, ideally someone outside of the area department. EPAs provide valuable insights to guide future engagement with "prolonged use" countries.

(14) *Structural reforms which facilitate the provision of credit to small businesses, including microenterprise lending*

The lack of financial services available to the poor is a significant obstacle to growth for many developing countries. The IMF does not have the lead role in microeconomic reforms to benefit small businesses; however, the Treasury Department engages with the IFIs to promote structural reforms that encourage the provision of credit to small and micro enterprises. The microfinance sector is frequently reviewed in the context of the Financial Sector Assessment Program (FSAP) in developing countries.

⁵ "Exceptional access" refers to financing arrangements in amounts that exceed the Fund's normal limits.

- In its July, 2007 Article IV response, the USED voiced concerns about the impact of a state-run development bank, BDP, on the Bolivian micro-credit industry, doubting its potential to complement the private sector without competition.

(15) *Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT)*

Comprehensive integration of the efforts of the IMF and the other IFI efforts as part of the global war on terrorism has been a consistent policy priority for the United States and its partners. We have encouraged collaboration between the IFIs and the Financial Action Task Force (FATF) to assess global compliance with the anti-money laundering (AML) and counter-terrorist financing (CFT) standards based on the FATF 40 Recommendations on Money Laundering and the 9 Special Recommendations on Terrorist Financing.

In April 2007, largely as a result of US and G7 leadership, the Executive Board of the IMF reiterated the importance of AML/CFT standards to strengthening the integrity of financial systems and deterring financial abuse, and affirmed the collaborative arrangements presently in place with the FATF and FATF-style regional bodies (FSRBs) for assessing AML/CFT regimes in the context of the IMF's financial sector work. The Board also encouraged greater transparency by calling for the publication of comprehensive country evaluations.

Collaboration by the IMF, FATF and FSRBs, with the assessors, using the same common methodology, institutionalizes the global fight against terrorist financing and money laundering, and helps countries identify shortfalls in their AML and CFT regimes and implement reforms. As of September 2007, the IMF had conducted 50 assessments of country compliance with AML/CFT, four of which were conducted jointly with the World Bank.

The IMF is also a substantial source of funding for countries' efforts to strengthen their own AML/CFT regimes – an activity that Treasury has supported and has joined in to leverage Treasury's own bilateral AML/CFT assistance. The IMF has provided substantial technical assistance (TA) on a bilateral and regional basis, delivering 88 missions and events from May 2006 to April 2007.

In the latest Communiqué of the International Monetary and Financial Committee of the Board of Governors of the International Monetary Fund (IMFC) - the Secretary of the Treasury is the Governor for the United States - the IMFC reiterated the importance of these issues and called for closer cooperation between the IMF and FATF in promoting stronger implementation of AML/CFT standards and encouraged publication of comprehensive country evaluations.

The USED/IMF office played a crucial role in mobilizing the IMF Board support for this initiative, as well as making sure note is taken of AML/CFT issues in Article IV reviews and reports, IMF programs, and other regular reviews of country progress. Examples include:

- In its September 2007 statement on the United Arab Emirates' Article IV report, the USED concurred with IMF staff in calling upon the government of the United Arab Emirates to strengthen its legal framework for combating terrorist financing and money laundering.

- In the USED July 2007 Board Statement, the USED noted that MENA FATF (the regional FSRB for the Middle East and North Africa) had completed its AML/CFT assessment of Syria. The USED asked IMF staff to review the MENA FATF assessment and provide the Board with comment on its main findings.
- In its December 2006 statement on Hong Kong's Article IV review, the USED noted that Hong Kong authorities are taking steps to improve their AML/CFT legislative framework. The USED called for improved enforcement of AML/CFT measures, and highlighted the need for greater regulatory oversight.
- In its November 2006 statement on Pakistan's Article IV review, the USED congratulated Pakistani authorities on measures taken to date to build robust controls against illicit finance and emphasized that passage of the long-delayed legislation on money laundering would be an important step.

II. Section 801(c)(1)(B)

(I) Suspension of IMF financing if funds are being diverted for purposes other than the purposes for which the financing was intended

With strong United States support, the IMF has taken steps in the past several years to ensure that IMF resources are used solely for the purposes for which they are intended. These steps constitute a serious and far-reaching initiative to strengthen the system for safeguarding the use of Fund resources and for deterring the misreporting of data to the IMF.

The IMF's safeguards framework requires countries receiving funds to submit to external financial audits of their central bank's data. This process is designed to ensure that central banks have adequate control, accounting, reporting and auditing systems in place to protect central bank resources, including IMF disbursements. Any critical gaps identified during the assessment process must be remedied before additional IMF resources can be disbursed.

(II) IMF financing as a catalyst for private sector financing

The IMF recognizes that, if structured effectively, official financing can complement and attract private sector flows. The Fund promotes policy reforms that catalyze private financing and, in cases of financial crisis, allow countries to regain access to international private capital markets as quickly as possible. (See Section 5 above for a more in-depth discussion of private sector involvement.)

(III) Financing must be disbursed (i) on the basis of specific prior reforms; or (ii) incrementally upon implementation of specific reforms after initial disbursement

IMF disbursements are tranching based on a country's performance against specified policy actions, both prior to and during the program.

- In its Board statement at the February 2007 discussions on the Ex-post Assessment of the 2002-2006 PRGF program for Nicaragua, the USED noted that using an IMF disbursement of funds as a signal to other donors of compliance put pressure on the IMF to disburse funds despite countries not meeting program standards, limiting the IMF's ability to be an effective gatekeeper of funds.

(IV) Open markets and liberalization of trade in goods and services

The IMF has been a consistent advocate of open markets and trade liberalization. The Fund also recognizes that trade adjustments can cause temporary balance of payments problems and has developed the Trade Integration Mechanism to provide transitional financial assistance to countries if needed.

- In its Board statement at the December 2006 Article IV discussion for India, the USED agreed with IMF staff that India can play a proactive role in restarting multilateral trade talks and noted that in the Doha Round, key developing countries such as India also need to reduce tariffs and other trade barriers in order to promote new trade flows in agriculture, manufactured goods and services.
- In its Board statement at the February 2007 Article IV discussions, the USED encouraged Panama that implementation of the US-Panama FTA would provide additional impetus for reforms and help sustain growth.

(V) IMF financing to concentrate chiefly on short-term balance of payments financing

In September 2000, with strong United States support, the IMF agreed to reorient IMF lending to discourage continued or prolonged use of IMF funds, and provide incentives for quick repayment. In particular, the IMF shortened the expected repayment periods for both Stand-By and Extended Arrangements and established surcharges for higher levels of access.

In early 2006 the IMF activated an Exogenous Shocks Facility (ESF) for low-income countries, which the U.S. supported to bolster the IMF's focus on addressing short-term balance of payments needs. The U.S. also successfully pressed for the adoption of the non-borrowing Policy Support Instrument (PSI), to provide a framework for IMF policy advice and donor signaling without the need for IMF lending. The U.S. has discouraged low-income countries from pursuing serial PRGF programs. The U.S. urges those countries without a clear balance of payments financing need to opt for a PSI, in which case they would retain the option of seeking ESF financing in the event of sudden adverse developments in their balance of payments.

(VI) Graduation from receiving financing on concessionary terms

The United States supports comprehensive growth strategies to move countries from concessional to market-based lending. The United States works closely with the IMF and World Bank to promote a growth-oriented agenda in developing countries based on strong monetary and fiscal policies, trade liberalization, and reduction of impediments to private sector job creation. The IMF extends concessional credit through the PRGF. Eligibility is based

principally on a country's per capita income and eligibility under the International Development Association (“IDA”), the World Bank's concessional window (the current operational cutoff point for IDA eligibility is a 2004 per capita GNI level of \$965). Factors that would contribute to reduced reliance on concessional resources include a country’s growth performance and prospects, capacity to borrow on non-concessional terms, vulnerability to adverse external developments such as swings in commodity prices, and balance of payments dynamics.

ANNEX 1
Report to Congress on International Monetary Fund Lending
October 1, 2006 – September 30, 2007

Board Approval Date	Country	Amount	Type	U.S. Position	Reason, if Opposed
11/20/2006	Haiti	SDR 73.7 million (US \$110 million)	PRGF	Support	
12/15/2006	Moldova	SDR 30.8 million (US \$46 million)	PRGF Augmentation	Support	
12/18/2006	Mauritania	SDR 16.1 million (US \$24 million)	PRGF	Support	
12/22/2006	Central African Republic	SDR 36.2 million (US \$54 million)	PRGF	Support	
01/26/2007	Peru	SDR 172.4 million (\$258 million)	SBA	Support	
02/21/2007	The Gambia	SDR 14 million (\$21 million)	PRGF	Support	
04/23/2007	Burkina Faso	SDR 6 million (\$9 million)	PRGF	Support	
05/07/2007	Gabon	SDR 77.2 million (\$116 million)	SBA	Support	
08/03/2007	Côte d'Ivoire	SDR 40.6 million (US\$62 million)	EPCA	Support	

Legislative Provisions
Section 1503 of the International Financial Institutions Act, as amended
(originally passed as Section 610 of the
Foreign Operations, Export Financing, and
Related Programs Appropriations Act, 1999, and amended in 2004)

The Secretary of the Treasury shall instruct the United States Executive Director of the International Monetary Fund to use aggressively the voice and vote of the Executive Director to do the following:

- (1) Vigorously promote policies to increase the effectiveness of the International Monetary Fund in structuring programs and assistance so as to promote policies and actions that will contribute to exchange rate stability and avoid competitive devaluations that will further destabilize the international financial and trade systems.*
- (2) Vigorously promote policies to increase the effectiveness of the International Monetary Fund in promoting market-oriented reform, trade liberalization, economic growth, democratic governance, and social stability through –*
 - (A) Establishing an independent monetary authority, with full power to conduct monetary policy, that provides for a non-inflationary domestic currency that is fully convertible in foreign exchange markets;*
 - (B) Opening domestic markets to fair and open internal competition among domestic enterprises by eliminating inappropriate favoritism for small or large businesses, eliminating elite monopolies, creating and effectively implementing anti-trust and anti-monopoly laws to protect free competition, and establishing fair and accessible legal procedures for dispute settlement among domestic enterprises;*
 - (C) Privatizing industry in a fair and equitable manner that provides economic opportunities to a broad spectrum of the population, eliminating government and elite monopolies, closing loss-making enterprises, and reducing government control over the factors of production;*
 - (D) Economic deregulation by eliminating inefficient and overly burdensome regulations and strengthening the legal framework supporting private contract and intellectual property rights;*
 - (E) Establishing or strengthening key elements of a social safety net to cushion the effects on workers of unemployment and dislocation; and*
 - (F) Encouraging the opening of markets for agricultural commodities and products by requiring recipient countries to make efforts to reduce trade barriers.*
- (3) Vigorously promote policies to increase the effectiveness of the International Monetary Fund, in concert with appropriate international authorities and other international financial institutions (as defined in Section 1701(c)(2)), in strengthening financial systems in developing countries, and encouraging the adoption of sound banking principles and practices, including the development of laws and regulations that will help to ensure that domestic financial institutions meet strong standards regarding capital reserves, regulatory oversight, and transparency.*

- (4) *Vigorously promote policies to increase the effectiveness of the International Monetary Fund, in concert with appropriate international authorities and other international financial institutions (as defined in Section 1701(c)(2)), in facilitating the development and implementation of internationally acceptable domestic bankruptcy laws and regulations in developing countries, including the provision of technical assistance as appropriate.*
- (5) *Vigorously promote policies that aim at appropriate burden-sharing by the private sector so that investors and creditors bear more fully the consequences of their decisions, and accordingly advocate policies which include –*
- (A) *Strengthening crisis prevention and early warning signals through improved and more effective surveillance of the national economic policies and financial market development of countries (including monitoring of the structure and volume of capital flows to identify problematic imbalances in the inflow of short and medium term investment capital, potentially destabilizing inflows of offshore lending and foreign investment, or problems with the maturity profiles of capital to provide warnings of imminent economic instability), and fuller disclosure of such information to market participants;*
 - (B) *Accelerating work on strengthening financial systems in emerging market economies so as to reduce the risk of financial crises;*
 - (C) *Consideration of provisions in debt contracts that would foster dialogue and consultation between a sovereign debtor and its private creditors, and among those creditors;*
 - (D) *Consideration of extending the scope of the International Monetary Fund’s policy on lending to members in arrears and of other policies so as to foster the dialogue and consultation referred to in subparagraph (C);*
 - (E) *Intensified consideration of mechanisms to facilitate orderly workout mechanisms for countries experiencing debt or liquidity crises;*
 - (F) *Consideration of establishing ad hoc or formal linkages between the provision of official financing to countries experiencing a financial crisis and the willingness of market participants to meaningfully participate in any stabilization effort led by the International Monetary Fund;*
 - (G) *Using the International Monetary Fund to facilitate discussions between debtors and private creditors to help ensure that financial difficulties are resolved without inappropriate resort to public resources; and*
 - (H) *The International Monetary Fund accompanying the provision of funding to countries experiencing a financial crisis resulting from imprudent borrowing with efforts to achieve a significant contribution by the private creditors, investors, and banks which had extended such credits.*
- (6) *Vigorously promote policies that would make the International Monetary Fund a more effective mechanism, in concert with appropriate international authorities and other international financial institutions (as defined in Section 1701(c)(2)), for promoting good governance principles within recipient countries by fostering structural reforms, including procurement reform, that reduce opportunities for corruption and bribery, and drug-related money laundering.*
- (7) *Vigorously promote the design of International Monetary Fund programs and assistance so that governments that draw on the International Monetary Fund channel public funds away*

from unproductive purposes, including large “show case” projects and excessive military spending, and toward investment in human and physical capital as well as social programs to protect the neediest and promote social equity.

- (8) Work with the International Monetary Fund to foster economic prescriptions that are appropriate to the individual economic circumstances of each recipient country, recognizing that inappropriate stabilization programs may only serve to further destabilize the economy and create unnecessary economic, social, and political dislocation.*
- (9) Structure International Monetary Fund programs and assistance so that the maintenance and improvement of core labor standards are routinely incorporated as an integral goal in the policy dialogue with recipient countries, so that –*
 - (A) Recipient governments commit to affording workers the right to exercise internationally recognized core worker rights, including the right of free association and collective bargaining through unions of their own choosing;*
 - (B) Measures designed to facilitate labor market flexibility are consistent with such core worker rights; and*
 - (C) The staff of the International Monetary Fund surveys the labor market policies and practices of recipient countries and recommends policy initiatives that will help to ensure the maintenance or improvement of core labor standards.*
- (10) Vigorously promote International Monetary Fund programs and assistance that are structured to the maximum extent feasible to discourage practices which may promote ethnic or social strife in a recipient country.*
- (11) Vigorously promote recognition by the International Monetary Fund that macroeconomic developments and policies can affect and be affected by environmental conditions and policies, and urge the International Monetary Fund to encourage member countries to pursue macroeconomic stability while promoting environmental protection.*
- (12) Facilitate greater International Monetary Fund transparency, including by enhancing accessibility of the International Monetary Fund and its staff, foster a more open release policy toward working papers, past evaluations, and other International Monetary Fund documents, seeking to publish all Letters of Intent to the International Monetary Fund and Policy Framework Papers, and establishing a more open release policy regarding Article IV consultations.*
- (13) Facilitate greater International Monetary Fund accountability and enhance International Monetary Fund self-evaluation by vigorously promoting review of the effectiveness of the Office of Internal Audit and Inspection and the Executive Board’s external evaluation pilot program and, if necessary, the establishment of an operations evaluation department modeled on the experience of the International Bank for Reconstruction and Development, guided by such key principles as usefulness, credibility, transparency, and independence.*

- (14) *Vigorously promote coordination with the International Bank for Reconstruction and Development and other international financial institutions (as defined in Section 1701 (c)(2)) in promoting structural reforms which facilitate the provision of credit to small businesses, including microenterprise lending, especially in the world's poorest, heavily indebted countries.*
- (15) *Work with the International Monetary Fund to*
- (A) *foster strong global anti-money laundering (AML) and combat the financing of terrorism (CFT) regimes;*
 - (B) *ensure that country performance under the Financial Action Task Force anti-money laundering and counterterrorist financing standards is effectively and comprehensively monitored;*
 - (C) *ensure note is taken of AML and CFT issues in Article IV reports, International Monetary Fund programs, and other regular reviews of country progress;*
 - (D) *ensure that effective AML and CFT regimes are considered to be indispensable elements of sound financial systems; and*
 - (E) *emphasize the importance of sound AML and CFT regimes to global growth and development.*

Legislative Provisions
Section 801 (c) (1) (B)
Foreign Operations, Export Financing, and
Related Programs Appropriations Act, 2001

Treasury should report on the extent to which the IMF is implementing –

- I. Policies providing for the suspension of financing if funds are being diverted for purposes other than the purpose for which the financing was intended;*
- II. Policies seeking to ensure that financing by the Fund normally serves as a catalyst for private sector financing and does not displace such financing;*
- III. Policies requiring that financing must be disbursed (i) on the basis of specific prior reforms; or (ii) incrementally upon implementation of specific reforms after initial disbursement;*
- IV. Policies vigorously promoting open markets and liberalization of trade in goods and services;*
- V. Policies providing that financing by the Fund concentrates chiefly on short-term balance of payments financing;*
- VI. Policies providing for the use, in conjunction with the Bank, of appropriate qualitative and quantitative indicators to measure progress toward graduation from receiving financing on concessionary terms, including an estimated timetable by which countries may graduate over the next 15 years.*

Legislative Provisions
Section 605(d) of the Foreign Operations, Export Financing, and
Related Programs Appropriations Act, 1999

On a quarterly basis, the Secretary of the Treasury shall report to the appropriate committees on the standby or other arrangements of the Fund made during the preceding quarter, identifying separately the arrangements to which the policies described in section 601(4) of this title apply and the arrangements to which such policies do not apply.

