IMF quotas and proposed increases

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IMF quotas are financial contributions provided by each of its 187 member states to support the organisation's lending activity. They largely determine member states' voting power and the amount they can borrow. Following a review, IMF quotas are set to double, to around $767bn in total. This is the first increase since 1998 and the largest in the organisation's history. The UK's quota will increase by less than this amount (88%) because of reforms which transfer a degree of power to emerging and low-income economies; these countries will see their quotas more than double.

Quotas are best understood as loans to the IMF: countries can draw down their quotas at short notice if required. In the UK, the portion of the quota that the IMF has drawn down counts as an asset of the National Loans Fund, and ***does not affect public borrowing or debt***.

In the UK, approval of a statutory instrument by the House of Commons is required to for the IMF quota to be increased. The most recent increase is covered by the *International Monetary Fund (Increase in Subscription) Order 2011*, which was made on 18 July 2011, having been debated in the Delegated Legislation Committee on 5 July 2011, and approved by the House on division (274 votes to 246) on 11 July 2011.

The changes to the quota will only come into effect once consent has been received from members representing at least 70% of the IMF's voting share. The IMF's objective is to complete this approval process by its 2012 Annual Meetings, which are likely to take place in October that year.

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1 What are IMF quotas?

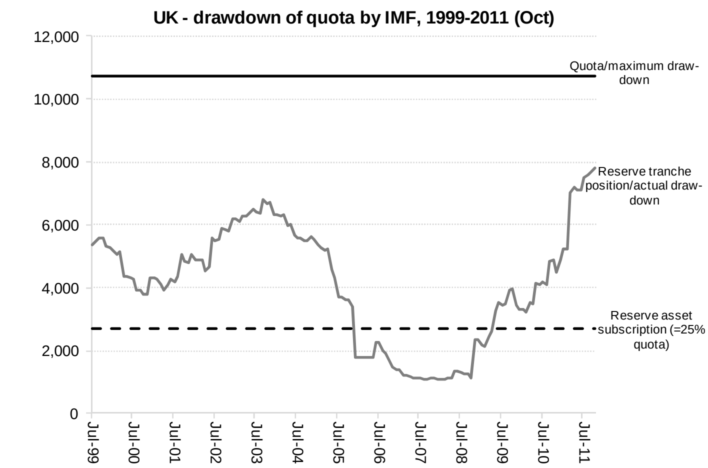
A country's IMF quota is the maximum amount of money it can be obliged to provide to the IMF. The quota size is determined by a weighted balance of the country's GDP, its openness to trade, its economic variability, and the size of its international currency reserves. Quotas also largely determine a country's voting power in the IMF, and the amount of money it can borrow.[1]

Quotas are one part of the IMF's financial resources, which it uses to provide lending to member countries. As the IMF cannot conduct open-market borrowing, the financial contributions of its members are essential to its effectiveness as a monetary institution.

In general, 25% of quotas are provided to the IMF in Special Drawing Rights (SDRs),[2] or a mix of widely-used foreign currencies (this is known as the **reserve asset subscription**), and 75% in domestic currency; in practice, the latter is usually provided in the form of non interest-bearing promissory notes.[3]

2 How does the IMF use quotas to lend money?

When a country needs to borrow money, it can always draw on its reserve asset subscription. If it needs to borrow more than this, it requires the approval of the IMF. Once granted, the IMF finances these additional amounts by using the reserve asset subscriptions of other members and/or by calling on financially strong countries[4] to provide funds over and above the reserve asset subscription, i.e. by eating into the domestic currency element of their quota. In order to do this the IMF cashes-in the domestic currency promissory notes of these strong countries for foreign reserves at prevailing exchange rates. It can only borrow up to 100% of any one member's quota.



In accounting terms, the reserve asset subscription constitutes an asset held by the UK, whilst the sterling promissory notes are a liability of the UK to the IMF. As the IMF exchanges UK sterling promissory notes for foreign reserves, the UK's IMF assets (i.e. its total lending to the IMF) increase. The difference between these assets and liabilities is the amount of the UK's total subscription the IMF has called, and is known as the UK's **reserve tranche position**; in effect, this is the difference between the UK's total quota, and the IMF's holdings of sterling. At one extreme, the reserve tranche position might be equal to the UK's quota, if the IMF has converted all the UK's sterling promissory notes. At the other, it might be zero, if the UK had decided to draw down its

[1] The amount that a country can borrow from the Fund, known as its access limit, varies depending on the type of loan, but is typically a multiple of the country's IMF quota.

[2] Special Drawing Rights (SDRs) are the IMF's unit of account. Its value in relation to other currencies is determined by the value of the euro, dollar, yen and pound. It can be exchanged for freely usable currencies at this rate. **Currently (15 June 2011), the value of the SDR similar to sterling (£1=SDR1.02)**

[3] A promissory note is an unconditional promise in writing to pay a sum of money to the bearer at a fixed time, or on demand.

[4] The Executive Board selects these countries every three months. Most are industrial countries, but the list has also included currencies of lower income countries such as Botswana, China, and India.

reserve asset subscription. The UK's reserve tranche position since July 1999 is shown in the chart.

Members receive interest on their reserve tranche positions at the 'standard SDR rate': for the week 13-19 June 2011, this stood at 0.56%.[5]

3 Background to recent changes

Following the G20 summit in London in April 2009, leaders agreed to increase the resources available to the IMF. As part of this agreement, the deadline for the completion of the 14th General Review of Quotas was brought forward from 2013 to January 2011. The review proposed a 100% increase in overall quotas, the largest in the history of the IMF, alongside realignment of quota shares and (hence) voting power. The increase will bring total quotas to SDR750bn, and together with increases in other borrowing facilities agreed at the summit, will bring the IMF's total resources to around SDR1,150bn, and total lending capacity of around SDR650bn.

In justifying such a substantial increase, the review document stated that:-[6]

> The crisis emphasized anew the need for liquidity buffers to face capital market shocks, and showed that significant cross-border financial activity can create external financing gaps even among advanced economies. More modest growth outlooks than previously assumed, and major fiscal challenges in some countries, may raise demand for Fund resources and limit the scope for a sufficient response at the individual country level should such a need arise again.

It also pointed out that there had been no general quota increases since 1998, meaning the size of the Fund had shrunk relative to the size of the global economy and to members' potential financing needs. Even restoring quotas to their 1998 levels in terms of GDP would require a 93% increase.

4 Effect on the UK of quota increases

If the changes were approved, UK's quota share would decrease from 4.5% to 4.2%, whilst the value of its quota will increase by 88% from SDR10,739 to SDR20,155.

The increase in the quota will have no impact on public borrowing or debt. This is because quotas are loans, and can be refunded at short notice in the form of a convertible foreign currency if the need arises. More generally, IMF members can always draw down their full reserve tranche positions (i.e. their 25% reserve asset subscription plus any additional quota used by the IMF).

Reflecting this, the UK's financial transactions with the IMF take place through the National Loans Fund (NLF), central government's main borrowing and lending account. This in turn is administered by the Treasury. The reserve tranche position is an asset of the NLF, and is counted as part of the UK's official international reserves.[7]

[5] In the UK's case SDR700m is unremunerated, as this part of the quota was provided prior to the 1970s, at a time when there was no system of remuneration.

[6] IMF Fourteenth General Review of Quotas – the size of the Fund: initial considerations, March 2010

[7] The IMF has periodically created SDRs, and allocated them to members in proportion to their quotas. The UK's SDR allocation is a liability not of the NLF, but of the Exchange Equalisation Account (EEA), which is managed by the Bank of England. The UK's SDR allocation is a liability of the EEA and the resultant holding of SDRs by the UK are an asset of the EEA.

5 Next steps

The changes will only come into effect once consent has been received from members representing at least 70% of the IMF's voting share. The IMF's objective is to complete this approval process by the 2012 Annual Meetings, which are likely to take place in October that year.

In the UK, Section 1(2) of the *International Monetary Fund Act 1979* requires a statutory instrument to be made and approved by a resolution of the House of Commons for the quota to be increased. The current increase is covered by the *International Monetary Fund (Increase in Subscription) Order 2011*, which was made on 18 July 2011, having been debated in the Delegated Legislation Committee on 5 July 2011,[8] and approved by the House on division (274 votes to 246) on 11 July 2011.[9] Although the order was laid before the House on 14 June 2011, the order of magnitude of the increase has been known since March 2010,[10] and Resolution 66-2 of the IMF Executive Board, which finalised the proposals, was published in November 2010.

The delegated legislation committee debate on the last subscription increase (The International Monetary Fund (Increase in Subscription) Order 1998) is available online at the linked footnote.[11]

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[8] Text of the debate is available here.
[9] Full results of the division are available here [HC Deb 11 July 2011 c130]
[10] IMF Fourteenth General Review of Quotas – the size of the Fund: initial considerations, March 2010
[11] http://www.publications.parliament.uk/pa/cm199798/cmstand/deleg5/st980723/80723s01.htm