

**FOR
AGENDA**

SM/08/350
Supplement 1
Correction 2

January 22, 2009

To: Members of the Executive Board
From: The Acting Secretary
Subject: **Charges and Maturities—Proposals for Reform**

The attached corrections to SM/08/350, Sup. 1 (1/16/09) have been provided by the staff:

Factual Errors Not Affecting the Presentation of Staff's Analysis or Views

Page 2, para. 1, line 5: text added: "The time-based surcharge(s) kicks in when credit outstanding remains above the quota threshold(s) of the corresponding surcharge system for the number of months stipulated in each system."

Page 3, Table 1, footnote added: "The time-based surcharge(s) kicks in when credit outstanding remains above the quota threshold(s) of the corresponding surcharge system for the number of months stipulated in each system."

Questions may be referred to Mr. Giorgianni, SPR (ext. 35326).

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities.

Att: (2)

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Department Heads

INTERNATIONAL MONETARY FUND

**Charges and Maturities—Proposals for Reform
Supplement**

Prepared by the Policy Development and Review, and Finance Departments

In consultation with Legal and other departments

Approved by Reza Moghadam and Andrew Tweedie

January 16, 2009

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A NEW SYSTEM OF SURCHARGES—SENSITIVITY ANALYSES OF STAFF'S PROPOSAL

In SM/08/350, staff proposed a new system of surcharges to replace the current system. At an informal seminar on December 16, 2008, Directors expressed interest in comparing the staff proposal with other possible surcharge systems. The question was also raised about the sensitivity of the pace of reserve accumulation to the level of credit outstanding. This supplement seeks to address these two issues.

I. ALTERNATIVE SURCHARGE SYSTEMS

1. **Table 1 summarizes the main features of the six alternative surcharge systems examined in this supplement.** All the systems combine level-based and time-based surcharges, but differ in (i) the access threshold (in percent of quota) after which surcharges start to apply; (ii) the time at which the time-based surcharge(s) kicks in; and (iii) the level of the surcharges. The time-based surcharge(s) kicks in when credit outstanding remains above the quota threshold(s) of the corresponding surcharge system for the number of months stipulated in each system.
 - Schedules 1 and 2 consist of a single level-based surcharge and a single time-based surcharge, as in the staff proposal of SM/08/350. In both schedules, the size of the level-based surcharge is 200 basis points: in Schedule 1, this is applicable to access above 500 percent of quota, while it is applicable to access above 300 percent of quota in Schedule 2. In both schedules, the time-based surcharge applies after 36 months: in Schedule 1, the size of this surcharge is 100 basis points, while it is 50 basis points in Schedule 2.
 - Schedules 3–4 combine a single level-based surcharge (respectively of 200 and 100 basis points) applying to access above 300 percent of quota, but two time-based surcharges of different sizes and kicking in at different times;
 - Schedule 5 contains two level-based surcharges each of 100 basis points (the first applicable to access between 200 percent and 500 percent of quota and the second to access above 500 percent of quota) and one time-based surcharge of 100 basis point kicking in after 36 months;
 - Schedule 6 contains three level-based surcharges each of 100 basis points (the first applicable to access between 200 percent and 300 percent of quota, the second to access between 300 percent and 500 percent of quota, and the third to access above 500 percent of quota) and one time-based surcharge of 100 basis point kicking in after 36 months.

Table 1. Alternative Surcharge Schedules

	Current schedule	Proposed schedule as in SM/08/350	Alternative schedules					
			1	2	3	4	5	6
Level-based surcharge	Y	Y	Y	Y	Y	Y	Y	Y
Number of tiers	2	1	1	1	1	1	2	3
Quota threshold								
First tier	200	300	500	300	300	300	200	200
Second tier	300						500	300
Third tier								500
Surcharge (cumulative, bps)								
First tier	100	200	200	200	200	100	100	100
Second tier	200						200	200
Third tier								300
Time-based surcharge 1/	N	Y	Y	Y	Y	Y	Y	Y
Number of steps		1	1	1	2	2	1	1
Duration trigger (in months)								
First step		36	36	36	27	24	36	36
Second step					39	36		
Surcharge (cumulative, bps)								
First step		100	100	50	50	100	100	100
Second step					100	150		

Source: Finance Department, IMF.

1/ The time-based surcharge(s) kicks in when credit outstanding remains above the quota threshold(s) of the corresponding surcharge system for the number of months stipulated in each system.

2. **The effects of these alternative surcharge systems on the potential cost for borrowers and, relatedly, the Fund's income depend on a number of parameters.** As discussed in SM/08/350, the amount and distribution over time of surcharge income from high access arrangements and, accordingly, the pace of accumulation of precautionary balances, depend on the type of Fund arrangement (e.g., under the SRF versus in the credit tranches), the total amount of access, the phasing of total access, and the repurchase schedule. For ease of comparison, this supplement presents calculations of surcharge income using a hypothetical arrangement with the same parameters used in the calculations reported in Sections IV and V of SM/08/350, namely, a 24-month Stand-by Arrangement (SBA) for a member country with quota of SDR 1300 million. One third of the total access under the arrangement is assumed to be disbursed upon approval, while the remaining two thirds is assumed to be evenly distributed in eight quarterly purchases. For the purposes of this exercise, repurchases are assumed to follow the obligations schedule, in order to highlight the impact of different assumptions for the time-based surcharge. As discussed in SM/08/350, however, the purpose of the time-based surcharge is to provide a price incentive for early repayment to substitute for the TBRE policy. Accordingly, the effective cost for borrowers and surcharge income for the Fund would be lower than indicated here to the extent members respond to the incentives in the new system and repay the Fund in advance of the obligations schedule. As in Table 6 of SM/08/350, surcharge income is calculated for three different access levels: 400, 800, and 1200 percent of quota.

II. IMPLICATIONS FOR SURCHARGE INCOME AND PRECAUTIONARY BALANCES

3. **The alternative surcharge systems considered here would in some cases have a significant impact on potential surcharge income for the Fund.** Compared to the system proposed in SM/08/350, the impact would be largest with Schedules 1 and 6 (Table 2, Figure 1). The former would yield consistently lower surcharge income, reflecting the higher threshold for the introduction of surcharges (500 percent of quota rather than 300 percent as proposed in SM/08/350), while the latter would yield consistently higher surcharge income. The differences are less marked, but still significant, with Schedules 2-5. Schedule 3, which has two time-based steps, would potentially yield moderately more than the proposal in SM/08/350 at higher access levels, while Schedules 2, 4, and 5 would yield moderately less.

Table 2. Comparison of Surcharges Income under Alternative Schedules
(in SDR millions) 1/

	Current schedule	Proposed schedule as in SM/08/350	Alternative schedules 2/					
			1	2	3	4	5	6
Access of 400 percent of quota								
Surcharge income	97.4	51.5	0.0	51.5	52.2	29.2	83.3	107.5
Change relative to current schedule			-97.4	-45.9	-45.2	-68.1	-14.1	10.2
Change relative to proposed schedule as in SM/08/350			-51.5	0.0	0.7	-22.2	31.8	56.1
Access of 800 percent of quota								
Surcharge income	473.4	473.4	191.8	439.3	516.8	438.2	447.4	643.5
Change relative to current schedule			-281.7	-34.1	43.3	-35.2	-26.0	170.1
Change relative to proposed schedule as in SM/08/350			-281.7	-34.1	43.3	-35.2	-26.0	170.1
Access of 1200 percent of quota								
Surcharge income	886.0	984.8	615.9	898.6	1085.5	953.9	915.7	1321.9
Change relative to current schedule			-270.2	12.6	199.5	67.8	29.7	435.9
Change relative to proposed schedule as in SM/08/350			-368.9	-86.1	100.8	-30.9	-69.1	337.2

Source: Finance Department, IMF.

1/ Calculations assume a 24-month SBA where one-third of the committed resources is disbursed upon approval, and the remaining two-thirds are evenly disbursed in eight quarterly installments. Repurchases are assumed to follow obligation schedule. The quota of the country is assumed to be SDR 1300 million.

2/ Key parameters of surcharge schedules as described in Table 1.

4. **The potential effects of these alternative schedules on the pace of accumulation of precautionary balances are summarized in Figure 2.** In all cases, the scenarios use the stylized example in Figure 8 of SM/08/350, where total credit outstanding stays constant at SDR 40 billion, of which SDR 30 billion is assumed to be subject to surcharges.¹ Examples are provided assuming access of 500 percent of quota (top panel) and 1000 percent of quota (bottom panel). These scenarios should be viewed as purely illustrative as, in practice, total Fund credit outstanding is not constant, but rather varies significantly over time and tends to

¹ See *Review of the Role and Adequacy of the Fund's Precautionary Balances*, EBS/08/110 (9/24/08), page 19.