

**IMMEDIATE
ATTENTION**

EBS/11/43

March 18, 2011

To: Members of the Executive Board

From: The Secretary

Subject: **Keeping Bilateral Agreements Open—Proposed Delegation of Authority to the Managing Director**

Attached for consideration by the Executive Directors is a paper on keeping bilateral agreements open—proposed delegation of authority to the Managing Director.

It is not proposed to bring this matter to the agenda of the Executive Board for discussion unless an Executive Director so requests by the **close of business on Wednesday, March 23, 2011**. In the absence of such a request, the draft decision that appears on pages 4 and 5 will be deemed approved by the Executive Board and it will be so recorded in the minutes of the next meeting thereafter.

It is intended that this paper will be published the Fund's external website after Wednesday, March 30, 2011.

Questions may be referred to Mr. Steinki, LEG (ext. 38222).

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

Att: (1)

Other Distribution:
Department Heads

INTERNATIONAL MONETARY FUND

**Keeping Bilateral Borrowing Agreements Open—Proposed Delegation of Authority
to the Managing Director**

Prepared by the Legal Department

(In consultation with the Finance Department)

Approved by Sean Hagan

March 17, 2011

This paper proposes to delegate to the Managing Director the authority to enter into the necessary agreements to implement the understandings with bilateral creditors pursuant to which their bilateral lines are to be kept open on a temporary basis to fund commitments approved by the Fund prior to the first activation of the expanded and amended New Arrangements to Borrow (NAB).

1. **In the context of the transition to the expanded and amended NAB, creditors with bilateral borrowing agreements have been asked to keep their lines open for the financing of commitments approved under Fund arrangements prior to the first activation of the expanded NAB.**¹ All but two creditors (reflecting domestic legal constraints) have indicated a willingness in principle to keep their lines open, subject to certain legally binding safeguards, in particular to prevent “double-dipping” and to minimize the period for which it is necessary to keep the bilateral lines in place. A number of creditors also stressed the importance of exploring all options to promote fair burden sharing between NAB participants that have bilateral lines and NAB participants that do not have such lines.
2. **A January 3, 2011 staff note to bilateral creditors addressed implementation of the agreement to keep bilateral borrowing agreements open, including safeguards (Attachment).** The note elaborated on the safeguards requested by creditors and clarified that there would be binding protections in these areas. The note also provided language for the implementation of the agreement of creditors to keep their bilateral lines open. The note further outlined two modalities for implementing these understandings: either (a) an amendment of the original borrowing agreement or (b) a supplementary Memorandum of Understanding (MoU).
3. **With respect to safeguards for creditors, the clauses envisaged for inclusion in the amendments/MoUs would specify as follows:**

- (i) *No double-dipping*—No drawings would be made under a bilateral borrowing agreement that would cause the combined outstanding drawings under that

¹ Letter from the Managing Director dated November 24, 2010.

agreement and the creditor's (or its related member's or institution's) NAB credit arrangement to exceed the amount of the NAB credit arrangement;

(ii) *Circumscribed use*—Following the effectiveness of the expanded NAB, drawings under bilateral borrowing agreements would only be made to finance commitments under arrangements approved prior to the first activation of the expanded NAB. The Fund would also continue to have the right to draw under bilateral borrowing agreements to meet requests for early repayments of claims under other bilateral borrowing agreements. However, in practice, since it is expected that bilateral claims would be folded into the NAB, such early repayments would be expected to be met from NAB resources; and

(iii) *Termination*—The borrowing agreements would be terminated when there are no longer any commitments outstanding under arrangements approved prior to the first activation of the expanded NAB or, prior to that date, when the Fund has determined that the bilateral lines are no longer needed. The amendment/MoU would also specify that the Fund would review regularly whether the bilateral agreements need to be kept open, taking into account its overall liquidity situation and outlook, including after the payment of quota increases under the Fourteen General Review.

4. **Keeping the bilateral lines open requires that creditors agree not to exercise the right to terminate their agreements upon effectiveness of the expanded NAB, and maintain these agreements as long as they are needed by the Fund to finance commitments approved prior to the first activation of the expanded NAB.** Most borrowing agreements include the right of the creditor to terminate the agreement following the effectiveness of the expanded NAB if the creditor (or its related member/institution) is a participant in the NAB. Most bilateral borrowing agreements also include a time limit that, beyond a certain initial period (usually two years), extensions of the term of the agreement for additional periods (in most cases, one or two years) require the agreement of the creditor. The January 3 note contained specific language on the non-termination issue, and also proposed two options to deal with extensions of the term. Under the first option, if a creditor does not wish to extend the term of its borrowing agreement at this stage but instead closer to the expiration date of the current term, then such extension could be deferred for now, on the understanding that the creditor would later agree to extend the term if requested by the Fund, in line with the political commitment to keep the bilateral agreement open to fund pre-NAB commitments. Under the second option, the amendment or MoU would at this stage provide for a new maximum term for drawings, which would not need to extend beyond January 31, 2013, in view of the expiration of the arrangements under the FCL for Mexico, Poland and Columbia by that date (after which staff assesses that quota resources should be adequate to cover the remaining relatively small commitments approved prior to the first activation of the NAB).²

² By January 31, 2013, remaining outstanding commitments under arrangements approved prior to NAB activation would be about SDR 2 billion, based on the assumption that Greece's current stand-by arrangement is cancelled and a new EFF arrangement approved. If the Greek arrangement were not to be cancelled, total outstanding pre-NAB commitments at end-January 2013 would be about SDR 3.9 billion.

5. **A satisfactory solution has also now been reached on burden sharing, responding to the separate concerns that some bilateral creditors have raised.** Specifically, there is substantial support among Executive Directors for a temporary modification to the rules concerning the operation of the Financial Transactions Plan (FTP), so as to allow the use of more quota resources from FTP members that are NAB participants (or whose institutions are NAB participants) and that do not have bilateral borrowing agreements. Such use will—over time—offset the initially larger NAB creditor positions of participants that have bilateral agreements (for details see Option 2 of FO/DIS/11/35, 3/1/11 and the companion paper entitled *Financial Transactions Plan—Temporary Modification of Guidelines for Allocation of Currencies Used for Transfers*). Fund management has also emphasized that other approaches to promoting burden sharing remain possible and could be pursued in parallel with the FTP adjustments described above. In particular, pre-NAB arrangements could be cancelled by members and successor arrangements approved by the Fund as opportunities arise, and the Fund stands ready to facilitate any voluntary transfer of NAB claims that participants may wish to make.

6. **In light of the above, and consistent with the January 3 note, it is proposed that the Executive Board now authorize the Managing Director to conclude the envisaged changes to the bilateral arrangements.** Under the current arrangements governing bilateral agreements, the Executive Board would need to approve each amendment or MoU on behalf of the Fund.³ However, the January 3 staff note indicated that staff would propose that the Executive Board authorize the Managing Director to agree to the necessary technical amendments to the bilateral agreements or to the conclusion of MoUs to implement the agreement in principle to keep the bilateral agreements open. Providing the Managing Director with this authority would facilitate expeditious implementation of the agreement to keep bilateral lines open. Staff has initiated discussions with all bilateral lenders on the formalization of the necessary amendments/MoUs, and expects to reach agreements with individual creditors shortly.

7. **The proposed decision below would give effect to the proposal summarized above.** It would delegate to the Managing Director the authority to enter into the necessary amendments and MoUs with creditors on behalf of the Fund. As contemplated in the January 3 staff note, the decision would also require that copies of any amendment agreement or MoU be circulated promptly to the Executive Board for information.

³ While the Managing Director is currently authorized under the bilateral agreements to agree on extensions of the term of these agreements, he lacks authority to agree to other amendments, such as the safeguards that have been requested by creditors regarding double-dipping and circumscribed use.

Proposed Decision

Accordingly, the following decision, which may be adopted by a majority of the votes cast, is proposed for adoption by the Executive Board:

1. The Managing Director is hereby authorized to agree to amendments of the bilateral loan and note purchase agreements (“borrowing agreements”) that were entered into by the Fund prior to the effectiveness of the expanded and amended New Arrangements to Borrow (NAB), and to enter into supplementary Memoranda of Understandings with respect such agreements, as the case may be, in order to implement understandings with bilateral creditors regarding:

- (i) The non-exercise by creditors of the right to terminate their borrowing agreements upon effectiveness of the expanded NAB;
- (ii) The extension of the term of the borrowing agreements, including agreement on a new maximum term, provided that the maximum term under borrowing agreements shall normally not extend beyond January 31, 2013;
- (iii) The commitment of the Fund to review regularly whether the bilateral agreements need to be kept open, taking into account the Fund’s overall liquidity situation and outlook, including after the payment of quota increases under the Fourteen General Review;

- (iv) The inclusion of clauses that would limit the use of resources drawn under the borrowing agreements to the funding of commitments under General Resources Account arrangements approved by the Fund prior to the first activation of the expanded NAB, and the funding of requests for early repayments of claims under other bilateral borrowing agreements; and
- (v) The inclusion of clauses that would limit drawings under the borrowing agreements by specifying that the combined outstanding claims under a member's or its official institution's borrowing agreement and NAB credit arrangement will in no case exceed the amount of their NAB credit arrangement.

2. Copies of the amendments to borrowing agreements and supplementary Memoranda of Understandings concluded pursuant to paragraph 1 above shall be circulated promptly to the Executive Board for information.

ATTACHMENT. KEEPING BILATERAL BORROWING AGREEMENTS OPEN— IMPLEMENTATION AND SAFEGUARDS

In response to the letter from the Managing Director of November 24, 2010, almost all bilateral creditors that are also participants in the expanded NAB have agreed in principle to keep their bilateral loan and note purchase agreements (“borrowing agreements”) open after the expanded New Arrangements to Borrow (NAB) become effective, with the aim of ensuring sufficient resources to finance commitments under Fund arrangements approved prior to the effectiveness of the NAB. This agreement by creditors is conditioned upon the implementation of safeguards to promote burden sharing among bilateral creditors and other NAB participants and to minimize the period for which it is necessary to keep the bilateral lines open.

This note aims to facilitate the timely implementation of this agreement in principle, including the necessary safeguards. Section A provides an overview. Section B sets out proposed language and alternative legal modalities which aim to provide flexibility to creditors to accommodate their domestic frameworks.

A. Safeguards for Extending Bilateral Lines

Key Safeguards for Bilateral Creditors

As set out in the Managing Director’s letter, binding safeguards will be established to provide those creditors that keep their bilateral agreement open with full assurance that:

- (i) ***No Double-Dipping***: no drawings would be made under a bilateral borrowing agreement that would cause the combined outstanding drawings under that agreement and the creditor’s NAB credit arrangement to exceed the amount of the NAB credit arrangement.^{1 2}
- (ii) ***Circumscribed Use***: drawings on bilateral agreements will only be made to finance commitments under arrangements approved prior to the first activation of the expanded NAB. The Fund would continue to have the right to draw under bilateral agreements to meet requests for early repayments of claims under other bilateral borrowing agreements. However, in practice, since it is expected that bilateral claims would be folded into the NAB, early repayments would be expected to be met from NAB resources.

¹ Where a central bank is the counterparty to a bilateral agreement while the member is the NAB participant (or vice versa), the clause would include specific language to limit drawings on the member and its central bank.

² A mechanism providing certain protection against double-dipping is already in place under the NAB where the folding-in of bilateral claims in accordance with paragraph 23 reduces the room for NAB drawings. However, this mechanism does not enable drawings under a NAB credit arrangement to reduce the creditor’s commitment under its bilateral agreement.

(iii) **Termination:** The borrowing agreements would be terminated when there are no longer any commitments outstanding under arrangements approved prior to the first activation of the expanded NAB or when the Fund has determined that the bilateral lines are no longer needed. The Fund will, however, review regularly whether the bilateral agreements need to be kept open, taking into account its overall liquidity situation and outlook, including after the payment of quota increases under the Fourteenth General Review.

Extending Bilateral Lines

The expanded NAB is currently expected to become effective during the first quarter of 2011. Most bilateral agreements include an option for the creditor (typically paragraph 2(c)) to terminate further drawings when the expanded NAB becomes effective if the creditor/relevant member/relevant institution is a NAB participant. Staff proposes that, to implement their agreement in principle to keep their bilateral lines in place, creditors would agree—either through an amendment to the bilateral borrowing agreement or through a binding Memorandum of Understanding (MOU) supplementing the borrowing agreement—not to exercise the termination option.

Most bilateral agreements also include a provision that beyond a certain initial period (normally two years), extensions of the term of the agreement for additional periods (normally one or two years) require the agreement of the creditor (typically paragraph 2(b)). Staff proposes two alternative options to deal with future extensions of the term:

Under the **first option**, if a creditor does not wish to extend the term of its borrowing agreement at this stage but instead closer to the expiration date of the current term, such extension would not be required now on the understanding that the creditor would later agree to extend the term if so requested by the Fund, in line with the political commitment to keep the bilateral agreement open.

Under the **second option**, the amendment/MOU would provide for a new maximum term for drawings.

B. Execution of Agreement and Safeguards—Alternative Modalities

As indicated in the October 14, 2010 memorandum to NAB participants on *NAB Transition Options—Legal Protection Against “Double-Dipping”* (attachment), alternative options can be considered to provide legal protection to creditors under borrowing agreements against double-dipping in case creditors agree to keep their borrowing agreements open following the effectiveness of the expanded NAB to fund drawings under arrangements approved prior to the first activation of the expanded NAB.

These options are, in particular, an amendment of the bilateral borrowing agreement or a MOU that would supplement the borrowing agreement. While from the Fund’s perspective both approaches are legally equivalent (i.e. both entail a change to the

understandings set out in the bilateral agreement), from the perspective of a creditor there could be a preference for one or the other option depending on their domestic frameworks. This note provides model language for both approaches. The model language would need to be adjusted for each particular agreement to reflect the specific features of each borrowing agreement.

With respect to Executive Board approval, staff will propose that the Executive Board authorize the Managing Director to agree to the necessary technical amendments to the bilateral borrowing agreements or to the conclusion of an MOU with the respective bilateral creditors, with copies of any such agreements or MOUs circulated to the Executive Board for information.

1. Amendment Option 1—Non-termination, protection against double-dipping and circumscribed use (no extension of term)

Paragraphs 2(c) and 3(a) of each bilateral agreement (or equivalent provisions in other paragraphs as necessary) would be amended as follows:

“2. Term of the Agreement.

(c) Notwithstanding subparagraphs (a) and (b), the term of this Agreement shall be terminated when (i) there are no longer any outstanding commitments made under Fund arrangements that have been approved prior to the first activation of the expanded and amended New Arrangements to Borrow (NAB) or (ii) the Fund has determined and notified [lender] that it would no longer need to make drawings under this Agreement. The Fund will regularly review whether its liquidity situation, including after the payment of quota increases under the Fourteenth General Review, would allow termination of drawings under bilateral borrowing agreements with a view to minimizing the period for which it is necessary to keep the bilateral agreements open.

3. Uses, Estimates and Limits on Drawings.

(a) After consultation with [lender], and taking into account both the Fund's liquidity position and the need to achieve, in the medium-term, broadly balanced drawings under the Fund's bilateral borrowing agreements, the Fund may make drawings under this Agreement in connection with (i) any use of Fund resources in the General Resources Account, or (ii) the payment of the Fund's outstanding indebtedness under other official sector borrowing effected pursuant to Article VII, Section 1(i) of the Fund's Articles of Agreement in circumstances where the terms of such other borrowing permit the Fund to make drawings under such other borrowing in connection with the payment of the Fund's outstanding indebtedness under this Agreement; provided however that following the first activation of the enlarged and amended NAB, drawings under this Agreement may only be made to fund commitments under arrangements approved by the Fund prior to such activation or to fund the repayment of the Fund's outstanding indebtedness

referred to under (ii) above. No drawings shall be made following the first activation of the enlarged and amended NAB that would cause outstanding drawings under this Agreement and under [lender's/member's] NAB credit arrangement to exceed the amount of the [lender's/member's] NAB credit arrangement.

2. Amendment Option 2—Non-termination, protection against double-dipping, circumscribed use and extension of term.

Paragraphs 2 and 3(a) of each bilateral borrowing agreement (or equivalent provisions in other paragraphs as necessary) would be amended to read as follows:

“2. Term of the Agreement.

(a) The Fund may make drawings in accordance with the terms of this Agreement until mm/dd/yyyy. Unless otherwise agreed between [lender] and the Fund, the Fund shall give [lender] at least five business days' ([lender's principal place of business]) notice of its intention to draw, and shall provide payment instructions at least two business days ([lender's principal place of business]) prior to the value date of the transaction by SWIFT.

(b) Notwithstanding subparagraph (a), the term of this Agreement shall be terminated when (i) there are no longer any outstanding commitments made under Fund arrangements that have been approved prior to the first activation of the amended New Arrangements to Borrow (NAB) or (ii) the Fund has determined and notified [lender] that it would no longer need to make drawings under this Agreement. The Fund will regularly review whether its liquidity situation, including after the payment of quota increases under the Fourteenth General Review, would allow termination of drawings under bilateral borrowing agreements with a view to minimizing the period for which it is necessary to keep the bilateral agreements open.

3. Uses, Estimates and Limits on Drawings.

(a) After consultation with [lender], and taking into account both the Fund's liquidity position and the need to achieve, in the medium-term, broadly balanced drawings under the Fund's bilateral borrowing agreements, the Fund may make drawings under this Agreement in connection with (i) any use of Fund resources in the General Resources Account, or (ii) the payment of the Fund's outstanding indebtedness under other official sector borrowing effected pursuant to Article VII, Section 1(i) of the Fund's Articles of Agreement in circumstances where the terms of such other borrowing permit the Fund to make drawings under such other borrowing in connection with the payment of the Fund's outstanding indebtedness under this Agreement; provided however that, following the first

activation of the enlarged and amended NAB, drawings under this Agreement may only be made to fund commitments under arrangements approved by the Fund prior to such activation or to fund the repayment of the Fund's outstanding indebtedness referred to under (ii) above. No drawings shall be made following the first activation of the enlarged and amended NAB that would cause outstanding drawings under this Agreement and under [lender's/member's] NAB credit arrangement to exceed the amount of the [lender's/member's] NAB credit arrangement.

3. Memorandum of Understanding Option 1—Non-termination, protection against double-dipping and circumscribed use

For lenders that have a preference for an MOU, language along the lines below could address the cancellation and double-dipping assurance issues:

“This memorandum of understanding is entered into between the International Monetary Fund (the “Fund”) and [lender] and contains understandings regarding the implementation of the bilateral borrowing agreement between the Fund and [lender] effective [date] (the “Agreement”) that are intended to ensure that the Fund has adequate resources to fund commitments made under Fund arrangements approved prior to the first activation of the enlarged and amended New Arrangements to Borrow (the “NAB”). Specifically, [lender] and the Fund agree on the following:

1. [Lender] will not exercise its right under paragraph 2(c) of the Agreement to terminate the term of the Agreement. The term of the Agreement shall be terminated when (i) there are no longer any outstanding commitments that have been made under Fund arrangements approved prior to the first activation of the expanded and amended NAB, or (ii) the Fund has determined and notified [lender] that it would no longer need to make drawings under the Agreement.
2. Following the first activation of the enlarged and amended NAB, the Fund may only make drawings under the Agreement to fund commitments under Fund arrangements approved before that date or to fund the repayment of the Fund's outstanding indebtedness under other official sector borrowing effected pursuant to Article VII, Section (i) of the Fund's Articles in circumstances where the terms of such other borrowing permit the Fund to make drawings under such other borrowing in connection with the payment of the Fund's outstanding indebtedness under the Agreement with [lender], provided that no drawings shall be made that would cause outstanding drawings under the Agreement and under [lender's/member's] NAB credit arrangement to exceed the amount of the [lender's/member's] NAB credit arrangement.
3. The Fund will regularly review whether its liquidity situation, including after the payment of quota increases under the Fourteenth General Review, would

allow termination of drawings under bilateral borrowing agreements with a view to minimizing the period for which it is necessary to keep the bilateral borrowing agreements open.

4. Memorandum of Understanding Option 2—Non-termination, protection against double-dipping, circumscribed use and new term

“This memorandum of understanding is entered into between the International Monetary Fund (the “Fund”) and [lender] and contains understandings regarding the implementation of the bilateral borrowing agreement between the Fund and [lender] effective [date] (the “Agreement”) that are intended to ensure that the Fund has adequate resources to fund commitments made under Fund arrangements approved prior to the first activation of the enlarged and amended New Arrangements to Borrow (the “NAB”). Specifically, [lender] and the Fund agree on the following:

1. [Lender] will not exercise its right under paragraph 2(c) of the Agreement to terminate the term of the Agreement, and, in light of the liquidity and borrowing needs referred to in Paragraph 2(b) of the Agreement, the term of the Agreement shall be extended through [date], without the need for further successive notices by the Fund. The term of the Agreement shall be terminated when (i) there are no longer any outstanding commitments that have been made under Fund arrangements approved prior to the first activation of the expanded and amended NAB or (ii) the Fund has determined and notified [lender] that it would no longer need to make drawings under the Agreement.
2. Following the first activation of the enlarged and amended NAB, the Fund may only make drawings under the Agreement to fund commitments under Fund arrangements approved before that date or to fund the repayment of the Fund’s outstanding indebtedness under other official sector borrowing effected pursuant to Article VII, Section (i) of the Fund’s Articles in circumstances where the terms of such other borrowing permit the Fund to make drawings under such other borrowing in connection with the payment of the Fund’s outstanding indebtedness under the Agreement with [lender], provided that no drawings shall be made that would cause outstanding drawings under the Agreement and under [lender’s/member’s] NAB credit arrangement to exceed the amount of the [lender’s/member’s] NAB credit arrangement.
3. The Fund will regularly review whether its liquidity situation, including after the payment of quota increases under the Fourteenth General Review, would allow termination of drawings under bilateral borrowing agreements with a view to minimizing the period for which it is necessary to keep the bilateral borrowing agreements open.