AUTHENTICATED
U.S. GOVERNMENT
INFORMATION
GPO

THE IMPACT OF THE INTERNATIONAL MONETARY FUND: ECONOMIC STABILITY OR MORAL HAZARD?

HEARING

BEFORE THE

SUBCOMMITTEE ON MONETARY POLICY AND TRADE

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED FOURTEENTH CONGRESS

FIRST SESSION

JUNE 17, 2015

Printed for the use of the Committee on Financial Services

Serial No. 114–35



U.S. GOVERNMENT PUBLISHING OFFICE

96–996 PDF WASHINGTON : 2016

For sale by the Superintendent of Documents, U.S. Government Publishing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2104 Mail: Stop IDCC, Washington, DC 20402–0001

HOUSE COMMITTEE ON FINANCIAL SERVICES

JEB HENSARLING, Texas, *Chairman*

PATRICK T. MCHENRY, North Carolina, *Vice Chairman*
PETER T. KING, New York
EDWARD R. ROYCE, California
FRANK D. LUCAS, Oklahoma
SCOTT GARRETT, New Jersey
RANDY NEUGEBAUER, Texas
STEVAN PEARCE, New Mexico
BILL POSEY, Florida
MICHAEL G. FITZPATRICK, Pennsylvania
LYNN A. WESTMORELAND, Georgia
BLAINE LUETKEMEYER, Missouri
BILL HUIZENGA, Michigan
SEAN P. DUFFY, Wisconsin
ROBERT HURT, Virginia
STEVE STIVERS, Ohio
STEPHEN LEE FINCHER, Tennessee
MARLIN A. STUTZMAN, Indiana
MICK MULVANEY, South Carolina
RANDY HULTGREN, Illinois
DENNIS A. ROSS, Florida
ROBERT PITTENGER, North Carolina
ANN WAGNER, Missouri
ANDY BARR, Kentucky
KEITH J. ROTHFUS, Pennsylvania
LUKE MESSER, Indiana
DAVID SCHWEIKERT, Arizona
FRANK GUINTA, New Hampshire
SCOTT TIPTON, Colorado
ROGER WILLIAMS, Texas
BRUCE POLIQUIN, Maine
MIA LOVE, Utah
FRENCH HILL, Arkansas
TOM EMMER, Minnesota

MAXINE WATERS, California, *Ranking Member*
CAROLYN B. MALONEY, New York
NYDIA M. VELÁZQUEZ, New York
BRAD SHERMAN, California
GREGORY W. MEEKS, New York
MICHAEL E. CAPUANO, Massachusetts
RUBÉN HINOJOSA, Texas
WM. LACY CLAY, Missouri
STEPHEN F. LYNCH, Massachusetts
DAVID SCOTT, Georgia
AL GREEN, Texas
EMANUEL CLEAVER, Missouri
GWEN MOORE, Wisconsin
KEITH ELLISON, Minnesota
ED PERLMUTTER, Colorado
JAMES A. HIMES, Connecticut
JOHN C. CARNEY, JR., Delaware
TERRI A. SEWELL, Alabama
BILL FOSTER, Illinois
DANIEL T. KILDEE, Michigan
PATRICK MURPHY, Florida
JOHN K. DELANEY, Maryland
KYRSTEN SINEMA, Arizona
JOYCE BEATTY, Ohio
DENNY HECK, Washington
JUAN VARGAS, California

SHANNON MCGAHN, *Staff Director*
JAMES H. CLINGER, *Chief Counsel*

SUBCOMMITTEE ON MONETARY POLICY AND TRADE

BILL HUIZENGA, Michigan, *Chairman*

MICK MULVANEY, South Carolina, *Vice Chairman*
FRANK D. LUCAS, Oklahoma
STEVAN PEARCE, New Mexico
BILL POSEY, Florida
LYNN A. WESTMORELAND, Georgia
MARLIN A. STUTZMAN, Indiana
ROBERT PITTENGER, North Carolina
LUKE MESSER, Indiana
DAVID SCHWEIKERT, Arizona
FRANK GUINTA, New Hampshire
MIA LOVE, Utah
TOM EMMER, Minnesota

GWEN MOORE, Wisconsin, *Ranking Member*
BILL FOSTER, Illinois
ED PERLMUTTER, Colorado
JAMES A. HIMES, Connecticut
JOHN C. CARNEY, JR., Delaware
TERRI A. SEWELL, Alabama
PATRICK MURPHY, Florida
DANIEL T. KILDEE, Michigan
DENNY HECK, Washington

CONTENTS

	Page
Hearing held on:	
June 17, 2015	1
Appendix:	
June 17, 2015	33

WITNESSES

WEDNESDAY, JUNE 17, 2015

Lowery, Clay, Vice President, Rock Creek Global Advisors LLC	3
Lundsager, Meg, Public Policy Fellow, Woodrow Wilson International Center for Scholars	5
Taylor, John B., Mary and Robert Raymond Professor of Economics, Stanford University	7

APPENDIX

Prepared statements:	
Lowery, Clay	34
Lundsager, Meg	40
Taylor, John B.	45

THE IMPACT OF THE INTERNATIONAL MONETARY FUND: ECONOMIC STABILITY OR MORAL HAZARD?

Wednesday, June 17, 2015

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON MONETARY POLICY AND TRADE,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 2:04 p.m., in room 2128, Rayburn House Office Building, Hon. Bill Huizenga [chairman of the subcommittee] presiding.

Members present: Representatives Huizenga, Mulvaney, Lucas, Pearce, Pittenger, Emmer; Moore, Kildee, and Heck.

Chairman HUIZENGA. This hearing of the Subcommittee on Monetary Policy and Trade will come to order.

Without objection, the Chair is authorized to declare a recess of the subcommittee at any time. And I will note that we have been told to expect votes sometime between 3:15 and 3:45.

Today's hearing is entitled, "The Impact of the International Monetary Fund: Economic Stability or Moral Hazard?"

And I now recognize myself for as much time as I may consume to give an opening statement.

Today, we will examine closely U.S. contributions to the International Monetary Fund (IMF), and the role that the IMF plays in terms of global financial surveillance, technical assistance, and, of course, lending.

Although the IMF membership is comprised of 188 countries, today the United States is the biggest contributor to the IMF, accounting for more than 17 percent of its quota resources. If a major default were to occur, it could put U.S. taxpayers on the hook for billions of dollars.

Since the global financial crisis of 2008, there has been an increased attention on the IMF's activities and the role in the global economy. In recent years, the IMF has bent the rules multiple times as it relates to exceptional access.

The most egregious was the loan to Greece, which was 3,212 percent of Greece's quota, I will note, well above any of those quota norms. We wouldn't let a bank in this country make a loan this exorbitant in nature. So why does the IMF believe American taxpayers should back a loan that, by our Nation's standards, should not have been made in the first place?

The 2009 Congress authorized a $100 billion commitment to the IMF in an account called, "New Arrangements to Borrow (NAB)." For the past 5 years, the Obama Administration has requested $63 billion of that authorization to be transferred to a permanent paid-in capital account. This would still leave billions in the NAB account, even though the NAB account is supposed to only be temporary.

Now, why should hardworking taxpayers' dollars be used to bail out other countries, especially after suffering from bailout fatigue in our own backyard? If you will recall, the American taxpayers were forced to bail out such entities as Fannie Mae, Freddie Mac, and the Federal Housing Authority.

Instead of furthering the bailout culture, wouldn't it make more sense for the United States to encourage advanced nations receiving loans from the IMF to better manage their spending and borrowing?

Currently, every dollar that Congress sends to the IMF implicitly condones the IMF sending money from countries struggling to find their economic footing to nations in danger of squandering their inheritance.

To be more direct, the use of the IMF as a backstop for advanced European countries calls into question, in my mind, whether this institution has become an enabling crutch instead of a helping hand.

As we know from our experiences in this country, guarantees in bailouts can create moral hazards. Even for the most advanced nations, the freedom to succeed requires the freedom to fall and get back up again.

I look forward to a meaningful discussion on the International Monetary Fund, and I look forward to hearing from our witnesses today.

With that, I yield back the balance of my time.

I will now recognize my ranking member, Ms. Moore from Wisconsin.

Ms. MOORE. Thank you so much, Mr. Chairman. And I want to thank you for calling this hearing. It is a very important hearing, and it is a subject that certainly deserves congressional attention.

We are increasingly in a global world, for all that means, good and bad. And so I think the importance of the mission of the IMF has only been elevated. From the onset, let me say that I think that the United States Congress needs to immediately move to ratify the new IMF quota system. There is broad agreement that it is the rational move, and it has been agreed to.

U.S. leadership and engagement in economic policy is vital in the long-term interest of our country. Global economic stability is, as we all know, smart geopolitics. Our borders are no longer a guarantee that what happens in far-off lands does not impact our shores economically or otherwise. Congress' lack of action has hurt U.S. standing internationally.

Further delay makes even less sense as China moves to fill the vacuum created by the lack of action by this Congress. I know that one of our witnesses wants to tie approval of the quota system to other IMF reforms, and I respectfully disagree on that point and welcome the engagement on that, while being entirely open to con-

sidering the case for IMF reforms, but not necessarily to making approval of the quota system contingent on acceptance of these yet-to-be-debated reforms.

First, time is of the essence, given the delay we have already seen. And, second, I think it would be an act of bad faith to hold this agreed-to quota realignment hostage to unspecified secondary demands.

Finally, I want to say that I think that the U.S. Federal Reserve, the Treasury, and the Financial Stability Oversight Council are great, but I think that the IMF remains an important second set of eyes in global stability. And I think that the advice and stability role that they fill provides a valuable service to the United States and to the world.

And, Mr. Chairman, I yield back.

Chairman HUIZENGA. The gentlelady yields back.

With that, we are going to start with our testimony. The order here will be Mr. Lowery, Ms. Lundsager, and then Mr. Taylor.

Clay Lowery, who is the vice president of Rock Creek Global Advisors, joins us today. He had served as the Assistant Secretary for International Affairs at the Treasury Department from 2005 to 2009.

And currently, with Rock Creek Global Advisors, he consults on sovereign debt, exchange rates, investment policy, and financial regulation. He is currently advising multi-national companies and financial institutions and trade associations on these matters.

So with that, Mr. Lowery, we appreciate you being here and recognize you for 5 minutes.

STATEMENT OF CLAY LOWERY, VICE PRESIDENT, ROCK CREEK GLOBAL ADVISORS LLC

Mr. LOWERY. Thank you very much, Chairman Huizenga and Ranking Member Moore, as well as the other members of the subcommittee. I want to thank you for this opportunity to testify on the IMF.

I am honored to be testifying alongside John Taylor, who is not only my former boss, but he is one of the most important macroeconomic thinkers in the United States, as well as with Meg Lundsager, who is a long-term colleague who is very deeply knowledgeable about the IMF.

The IMF promotes three objectives—macroeconomic stability, financial stability, and economic growth—using three basic tools: technical assistance; surveillance; or basically, evaluation of a country's financial policies and economic policies and lending.

When the IMF lends money, the country is usually in very deep financial trouble. To protect itself from this highly risky form of lending, the IMF relies on two things: one, a presumption that its credits are senior to other credits: and two, a requirement that the borrowing country undertake reforms to alleviate the concerns of throwing good money after bad. As you can imagine, these things can be controversial, as we are currently seeing in Greece.

The IMF finances itself through contributions by member countries, which are called quota. That takes into account a country's relative economic size. So, for instance, instead of being one country, one vote, as is the case in many international institutions, the

United States has roughly 17 percent of the voting share. No other country is even close. Japan is second, with around 6 percent.

The IMF has evolved over the last 70 years, but one area that has harmed it in its legitimacy and its relevance is a representation structure that no longer fit the international economy.

And so from 2005 through 2010, both in the Bush Administration and the Obama Administration, the United States led an effort to try to fix this problem. The 2010 agreement is the culmination of these efforts.

First, it alters the voting wage to make adjustments so that countries such as China and Mexico and Korea will see their votes increase noticeably while others will fall. The United States will basically stay the same.

Second, it alters how voting shares are translated into board seats. There are 188 members in the IMF, but only 24 board seats. Europe disproportionately holds too many seats. After the reform package is put together, we will see that dynamic emerging market countries will have more seats, Europe will have less seats, and the United States will still have its seat.

The quota reform also doubles IMF quota resources, as the chairman noted. It does this by reallocating money from an emergency pot of money called the "New Arrangements to Borrow" to the normal IMF pool of money based on quota allocation.

For the United States, we will not increase our total contribution to the IMF, but instead will transfer a portion of our NAB contribution to quota resources. This allocation requires authorization and appropriations from Congress. To date, every major country has ratified this reform package except for the United States.

So there are many economic and financial reasons for why we should support the United States, and it is probably not surprising to you that every Secretary of the Treasury, most U.S. Trade Representatives, and the Federal Reserve Chairmen since the Carter Administration have supported this IMF reform package.

But maybe, just as importantly, the IMF is a foreign policy tool that the United States has called upon many times to provide finance and advice, whether it was South Korea in the 1990s, Afghanistan and Iraq in the 2000 period, or Ukraine today. But I can provide you a more personal example of this.

In 2008, I worked for many hours with the Prime Minister of Georgia after his country was invaded by Russia. He was worried about a banking crisis, and he was looking for liquidity.

While the United States was very supportive of Georgia, we were in the midst of our own financial crisis in 2008 and were not in a position to provide emergency liquidity. Instead, we worked with the IMF, which stepped up very quickly to provide the financing Georgia needed to preserve confidence in its banking system and save its economy.

In other words, the IMF is an important tool to conduct strong foreign policy and to provide the conditions that assist in keeping our troops out of harm's way. Don't take my word for it.

Most of the Secretaries of Defense, National Security Advisors, and Secretaries of State from President Nixon through President Obama have supported the legislative request of this Administration. They recognize that U.S. leadership in the IMF is not only

vital to the institution, but also important to our own national security interests.

The IMF is far from perfect and will continue to need U.S. leadership to reform and evolve. However, U.S. leadership cannot occur from the sidelines and must come in the form of strong legislation with appropriate conditions.

Therefore, I ask that Congress work with the Administration and join what I believe is a strong bipartisan consensus and demonstrate this leadership.

Thank you. I am happy to answer any questions.

[The prepared statement of Mr. Lowery can be found on page 34 of the appendix.]

Chairman HUIZENGA. Thank you, Mr. Lowery.

With that, we will go to Ms. Meg Lundsager. She is a public policy fellow at the Woodrow Wilson International Center for Scholars, and she currently consults on international economic, financial, and regulatory issues.

And while the United States Executive Director on the IMF executive board from 2007 through 2014, she focused on achieving effective IMF input into lending programs in Europe, securing adequate IMF resources, supporting low-income countries, and strengthening IMM oversight of exchange rate policies.

And with that, Ms. Lundsager, we appreciate you being here and recognize you for 5 minutes.

STATEMENT OF MEG LUNDSAGER, PUBLIC POLICY FELLOW, WOODROW WILSON INTERNATIONAL CENTER FOR SCHOLARS

Ms. LUNDSAGER. Thank you, Chairman Huizenga, Ranking Member Moore, and members of the subcommittee for inviting me today.

During my 14 years with the IMF, I represented three Presidents. I was nominated first by President Clinton, then by President Bush, and I continued to serve under President Obama. I am currently a public policy fellow, and I should just note that my views today are my own and not those of the Wilson Center.

During the global financial crisis, the IMF was instrumental in helping many countries recover and return to private market financing. The IMF draws on many members to provide financing, keeping the U.S. share a little bit above 20 percent, as Mr. Lowery was just describing.

Nonetheless, U.S. leadership was crucial to bringing together all the elements needed for the IMF's international response, but that leadership is eroding as the United States delays approving the 2010 quota and governance reforms.

The United States has the largest single country vote in the IMF with a veto over key decisions, such as amending the articles and increasing IMF financing. This current voting structure, though, doesn't really represent the rapid growth and emerging markets in developing countries. So we have Belgium with a larger vote in South Korea, Mexico, or Turkey. That is quite anomalous.

The United States recognizes distribution of voting power threatens to undermine the legitimacy of the International Monetary Fund, and beginning in 2006 the Bush Administration proposed

steps to realign quotas. And in 2010, IMF members reached a broader agreement, which now awaits U.S. approval.

Today's hearing presents an opportunity to clarify the elements of the 2010 package, and I have provided many details in my written statement.

First, the U.S. share will remain comfortably above the 15 percent veto threshold. And, as you, Mr. Chairman, and Mr. Lowery explained, there is no change in the U.S. financial commitment with the shift coming from the New Arrangements to Borrow and being shifted to the quota.

But Europe's voting share will decline and dynamic emerging market share will increase. These changes should help keep global economic policymaking centered in the IMF, and key U.S. allies will gain, including Mexico, South Korea, Poland, and the Baltic nations.

Second, some claim the IMF should not have rescued Eurozone countries. But without the IMF as the crisis manager in Europe, I believe we risked a dissolution of the Eurozone, which would have reduced U.S. exports and increased the risk of European bank failures, ultimately affecting U.S. financial institutions and corporations as well as our stock and bond markets. The U.S. economic recovery would have been undercut.

Did the IMF's ability to lend large amounts incentivize Eurozone countries to mismanage their finances and slide into crisis? That hardly seems likely, as evidenced by the very demanding policy adjustment programs they have had to implement. Countries avoid turning to the IMF until no other option remains. And while some investors might seek high returns in higher-risk countries, thinking that IMF will finance their exit, those illusions should be dissipating as some countries resort to capital controls and others turn to debt restructurings.

Third, over the many decades of the IMF's existence, U.S. leadership and ideas has persuaded others to join in promoting reforms. The United States has been a leading voice for accountability, transparency, and change both at the institution itself and within member countries.

U.S. initiatives at the IMF have led to much more openness in government accounts, sounder financial institutions as countries improve regulatory oversight, reductions in the financing channels for money launderers and terrorists, and improved economic growth and stability in low-income countries.

Furthermore, important U.S. national security priorities were supported by IMF lending programs and technical assistance for Iraq, Afghanistan, Tunisia, and Jordan, among others.

More recently, the IMF responded to U.S. calls to increase support for the Ebola-affected countries in Western Africa and to underpin economic reforms in Ukraine with vital financing in the face of internal conflict and Russian economic pressure.

Sadly, U.S. leadership continues to erode as the United States delays approval of these reforms. In my last months at the IMF, it became increasingly clear that other countries had little enthusiasm for U.S. proposals such as extending the zero percent interest on low-income country loans.

Let me just turn to a key financing issue. The IMF has a backstop of numerous bilateral loan agreements with a subset of nations. I fear that, if the United States does not ratify the 2010 reform, strengthening the IMF core capital, the IMF will continue to seek bilateral loans negotiated with less transparency and without U.S. involvement. These decisions should be made around the board table with all of us there.

Thank you very much, Mr. Chairman. And I look forward to your questions.

[The prepared statement of Ms. Lundsager can be found on page 40 of the appendix.]

Chairman HUIZENGA. Thank you.

And, with that, we turn to Professor John Taylor. Professor Taylor has a very long and impressive career, including authoring many books and articles. He is currently the Mary and Robert Raymond Professor of Economics at Sanford University and the George P. Shultz Senior Fellow in Economics at the Hoover Institute.

He is known for his research on foundations on monetary theory and policy, which is applied by central banks and financial market analysts around the world.

And specifically related to this, for 4 years, between 2001 and 2005, Professor Taylor served as the Under Secretary of Treasury for International Affairs, where he was responsible for currency markets, trades and financial services, foreign investment, and also the IMF and the World Bank.

We welcome you, Dr. Taylor, again to this committee. You are recognized for 5 minutes for your opening statement.

STATEMENT OF JOHN B. TAYLOR, MARY AND ROBERT RAYMOND PROFESSOR OF ECONOMICS, STANFORD UNIVERSITY

Mr. TAYLOR. Thank you, Mr. Chairman, Ranking Member Moore, and members of the subcommittee.

For the IMF to achieve the goals that Clay Lowery mentioned, such as economic stability, it really has to have a clear and predictable framework or strategy for carrying out its goal. Otherwise, decisions become highly uncertain. They lead to excessive risk taking and international spillovers. I think a framework like that also provides for transparency and accountability.

A number of years ago, such a framework, called the "exceptional access framework," was adopted by the IMF. It set forth criteria that had to be met before the IMF could lend exceptionally large amounts to countries. The most important criterion said that the IMF could not make new loans to countries with unsustainable debts.

The expectation was that this way of limiting loans would reduce bailouts of the private sector, contain moral hazard, lower uncertainty, reduce the recipient country's debt burden, encourage more responsible fiscal and monetary policy, reduce spillovers, improve accountability, and, therefore, create more economic stability.

And, in fact, the introduction of this framework was accompanied by many such changes. Compared with the 1980s and 1990s, there were a few crises emanating from the emerging markets in the years that followed and emerging market countries weathered the

global financial crisis remarkably well and economic policy in those countries generally improved.

Unfortunately, this exceptional access framework is no longer in place. It was abandoned in 2010, when the Greek sovereign debt crisis emerged, and the IMF staff could not establish that the Greek debt was sustainable with high probability.

So the IMF simply changed the rule. It wrote in an exemption saying that new loans could be made in unsustainable situations so long as there was a "high risk of international systemic spillover." That exemption is still in place.

As is well known, events in Greece following the 2010 decision have not been pleasant. And it is time, in my view, to reform and strengthen that exceptional access framework. A starting place would simply be to repeal the exemption for systemic risk. That exemption is the problem, not the solution. I have found much support for this kind of reform in the international community, including at the IMF.

Importantly for the Congress, this reform is closely related to the quota and voting reallocation agreement that Meg and Clay just mentioned, which was negotiated way back in 2010.

This agreement would sensibly reallocate voting shares to give more votes to countries that have grown more rapidly. It would also increase the total quota commitment to the IMF. The main rationale for that increase is that the global economy and capital flows have expanded.

Of course, the increase in the quota must be scored by the CBO and may need offsets elsewhere in the budget. Legislation to approve the increased quotas and voting reallocation should, therefore, be tied to the exceptional access framework, which will also provide additional transparency and accountability.

It seems to me that with the global financial system in an uncertain state of flux right now, it is an important time, a good time for such reforms. Approving the international quota agreement in a way that helps ensure that these new resources are used strategically, effectively, and with accountability, as I show in more detail in my written testimony, would be an important pillar of any such reform movement.

Thank you, Mr. Chairman.

[The prepared statement of Dr. Taylor can be found on page 45 of the appendix.]

Chairman HUIZENGA. The gentleman yields back.

And, with that, we are going to go into our question period. I am going to recognize myself for 5 minutes.

Ms. Lundsager, when you were our Executive Director at the Fund—and I don't want to put words in your mouth—I assume you advised Treasury that a systemic exemption for Greece was a good idea. Is that accurate?

Ms. LUNDSAGER. Thank you, Mr. Chairman.

As you may be aware, the systemic exemption was inserted in the Greek program that we approved in May 2010. And there was no advance discussion of that.

So, at that point, I recall we were all very concerned about the situation in Greece. And, of course, any country has the right to ask for assistance from the IMF and the IMF responds. And, at

that point, Greece was committing to a number of adjustment measures that would start to address some of their problems.

And to be perfectly frank, at that time we were very worried about the rest of Europe. And my concern was that if contagion spread to a number of other countries, not just the smaller ones such as Portugal and Ireland who eventually needed IMF programs, but the larger ones, Italy or Spain—you remember the references to the GIIPS or the PIIGS years ago—that the IMF would not be able to handle, for instance, an Italy without great difficulty and that it would be very difficult for the Europeans to hold the Eurozone together, given that they had not built their own firewalls at that time.

So the systemic exemption in the end was inserted by the staff. The board approved it, although many of us just became aware of it at the meeting itself, since the change was buried in this long document.

I was dismayed that staff used that approach, but in the end, my concerns about Greece and about Europe overrode that dismay and I supported the program.

Chairman HUIZENGA. In retrospect, do you think it was a good idea? This is something I asked Secretary Lew earlier today.

And after a rather lengthy sidestep, he came out with yes, he felt it was still a good idea, at which point I was asking him, just as Professor Taylor was talking about, about the potential return of that language to that. And, as I have been having some conversations, I, too, am finding that support within the IMF and other countries that are involved with the IMF.

So do you still think it was a good idea? And what is your take on whether we should return that language and return to that policy?

Ms. LUNDSAGER. Whether or not we have that particular language, I still feel that the IMF needs an ability to exercise judgment. And by the IMF, I mean the executive board, the membership itself.

My concern with rigid rules is that, first of all, it is very difficult to know what the next crisis is going to be. And what we found when we had the exceptional access criteria, first set, each case ended up being different and didn't quite meet the criteria.

And so I am not comfortable with being able to predict what a future crisis might be and how a country might or might not meet particularly rigid rules.

I am also a little bit worried that these criteria are based on IMF calculations of debt sustainability, and these numbers are very difficult to pin down and very dependent on numerous assumptions, as I am sure you know, you are aware as you look at a number of these issues just in terms of the United States itself.

So I am a bit worried that it could end up being very arbitrary. And if it is a key U.S. ally and the fund says, "Well, we are not ready to do exceptional access. Okay, United States. You are going to have to do it all bilaterally," we are back to the very place that we did not want to be or else we are forcing that country into a debt restructuring immediately.

Chairman HUIZENGA. I have a little over a minute.

Dr. Taylor, you were there and helped developed the exceptional access framework at Treasury.

How do you respond to Ms. Lundsager, and what is sort of your take on the world right now?

Mr. TAYLOR. I think there is quite a bit of flexibility in the way the original access rules or framework was put in place. So I don't think you need any more. And I think, ideally, you could go back to something like that.

I think the experience has also shown that too much flexibility is a disadvantage. You think about the danger of lending to an unsustainable debt situation, you end up bailing out the private sector. That is basic. You think now, "Who owns most of the Greek debt?" It is the public sector. So it enabled the private sector to get out.

Chairman HUIZENGA. Between the IMF and the EU, are these—

Mr. TAYLOR. Yes. So that is the concern. I also think it creates an enormous amount of uncertainty. In talking to many in the private sector, they would prefer to go back to where we were because they recognize the current situation creates uncertainty. So for all the reasons you want to have a framework.

Also, I would say, for accountability and transparency, this is money that you are going to have to authorize and appropriate. I think it is part and parcel the institution describes as best it can its framework for allocating these large sums of money. It is not rocket science, to be sure, but I think it is quite workable.

Chairman HUIZENGA. All right. With that, my time has expired.

And I recognize my ranking member, Ms. Moore, for 5 minutes.

Ms. MOORE. Thank you so much, Mr. Chairman.

And I want to thank all of the witnesses for joining us today.

This is truly an opportunity, I think, for the committee to get a tremendous education with the aggregation of experience that you all have.

I want to continue to pursue the discussion, maybe starting with Professor Taylor. I can truly identify with your notion, perhaps, that there is some moral answer in abandoning a framework where riskier loans, countries like Greece, were enabled to access the lending facility.

But I hearken back—I was here when Secretary Paulson came and said, "Give us $700 billion or else the United States' economy is going to collapse." And my first reaction was not a very ladylike response. It was like, "blank, no."

But as I listened to experts such as yourself, I concluded that it just had to be done. And there was moral hazard. I think we are still experiencing it. I think we sort of bailed out the private sector more so than we did homeowners.

And so I guess my question to you, sir, and to Ms. Lundsager, and perhaps to Mr. Lowery would be, what do you make of the "high risk of international spillover"—the exception being the high risk of international spillover?

Do you honestly believe that if the IMF is not in a space like Greece or the Eurozone or other things, that there will be no impact on our economy here?

Mr. TAYLOR. What will happen in a situation like that is the IMF will say, "Your debt is unsustainable, with high probability. There

is no exemption for a systemic spillover. So, therefore, unless your debt is restructured, unless the private sector comes in and says, 'We are writing down or reprofiling that debt,' you don't get a loan."

But the result most likely will be that the private sector will get involved in that. And so that is really what—to have a clear rule in advance, a clear process in advance, that is basically what you hope will happen.

I would add a few things based on my own experience. It is nearly impossible to determine about the systemic spillover risk. Therefore, it is very susceptible to political maneuvering and for people to claim there is this risk, systemically, of spillover, when nobody really knows.

We discussed the difficulty of doing a sustainability analysis, what the likelihood is of the debt being sustainable. That does require numbers. But that is far easier than trying to determine the systemic risk.

Ms. MOORE. Ms. Lundsager, do you have a comment?

Ms. LUNDSAGER. Thank you.

It is very difficult, first of all, to determine insolvency versus illiquidity for a particular country.

But contagion can be a very real risk as deposits leave a country, leave the banking system, which causes problems as our banking systems are based on deposits not all being withdrawn at one time. This can then spread to other countries that have similar characteristics.

We saw this in 2010. We saw more of this in 2011 in Europe. And you have all seen the market jitters right now as all this uncertainty about Greece remains in the market as Europe's leaders debate the next step.

So, yes, I was bothered about contagion then, and I still think that is the main reason that we have the International Monetary Fund. Thank you.

Ms. MOORE. Mr. Lowery, just very briefly, I think at least you and Ms. Lundsager have talked about the lack of leadership from the United States, given its veto power and so forth in the IMF. If we don't sort of adopt the framework, pay our dues, be the leader, what could ultimately be the impact?

I am thinking of the formation of BRICS, for example. Could any of you sort of share with us what you think the consequences are of a diminishing influence of the IMF and the rise of something like the BRICS?

Mr. LOWERY. That is a good question.

I think that—look, my own view is that the United States should be taking a leading role. We help formed the IMF. We are the leading country in the IMF.

If that means that we need to pursue some of the reforms that John Taylor is talking about, I think we should probably be looking at doing that. If it means to do some other reforms, we should be looking at doing that.

But that does not mean we should be holding up going forward on an agreement that everybody in the world has agreed to years ago that—I think that most people in the United States, people

who have sat in the Executive Branch, actually think that this is a helpful institution for us to support.

As to whether or not it means that the Asian Infrastructure Investment Bank or the BRICS bank is going to be created and those are the reasons it got created, I can't answer that because I don't know the mindset of the Chinese.

I do know this, that there is concern that the United States is not stepping up as an international leader in a number of areas that are not just about the IMF, and this is an area where I think that we can come to an agreement if we worked hard together.

Ms. MOORE. Thank you. My time has expired.

Chairman HUIZENGA. The gentlelady's time has expired.

With that, we go to our Vice Chair, Mr. Mulvaney, for 5 minutes.

Mr. MULVANEY. Before we come back to Greece, I want to follow up very briefly on what Mr. Lowery just said to speak to the issue raised by the gentlelady from Wisconsin, which is, on the 2010 reforms, we have had some hearings on that before, back when John Campbell was the subcommittee Chair here. And, if I remember correctly, one of the fundamental principles of the reform was that we were going to move money out the New Agreements to Borrow into the quota.

And I remember an issue coming up at the hearing, Mr. Chairman, which was, essentially, those two pots of money, for lack of a better word, are subject to different rules, different governance.

And my understanding—correct me if I am wrong—is that, while the quota system is subject to rules essentially by consensus, the NAB, the New Agreements to Borrow, is subject heavily to our veto.

That is my understanding. Am I wrong about that?

Mr. LOWERY. I think the rule for the NAB is that it is activated every 6 months. So, on that, the United States has a veto right. However, if there is a loan provided by the NAB, it is done on a majority decision.

Mr. MULVANEY. Yes. That is my recollection. We can shut it off every 6 months.

And I guess, Mr. Lowery, to your point, and Ms. Moore, to your point, that was one of the hang-ups we had, was that we were effectively moving money out of an area where we had considerable control and into an area where we had less control. That concern remains.

And then I look at that concern against the backdrop of what we are talking about today in Greece and the difficulties that some of us have with the changes that were made regarding contagion, regarding systemic risk.

Now, Ms. Lundsager, you said something—I am not interested in debating what happened with Greece several years back. But you did say something that I thought was relevant to the discussion about whether or not we should go back to the old rules as we go forward.

You said that the Europeans did not have firewalls in place at the time and that, in part, justified changing the rules in the IMF in order to allow the IMF to participate.

Those firewalls exist today, don't they?

Ms. LUNDSAGER. Yes, Congressman. They have built firewalls, and the European Central Bank is taking a number of actions. With that said, each country is still entitled to seek help from the IMF, to seek advice and to seek a program.

Mr. MULVANEY. I am fine with all that. I am not trying to change the underlying rules. I am just trying to talk about whether or not that special exception—we are not going to look at whether or not they can pay the debt back, for example, if we fear contagion.

And my point to you, I think, is that the firewalls that you said did not exist, accurately so, several years back do exist. So the need, perhaps, for the special exceptions for contagion have gone down.

I also think that we need to recognize the fact that, while the Europeans were not ready at the beginning of the Greek crisis, they have loaned them, like, 8 times more money than the IMF has in the last couple of years.

So, while the IMF's $25 billion to $30 billion was critical at the time, it pales in comparison to the couple hundred billion dollars that the Europeans have loaned them. This seems to be their problem. The contagion was the countries that you mentioned, all European countries. So it seems like it might be more appropriate to let them take the lead.

Mr. Taylor, you have had some thoughts—and I want to get some more input from you in my last 2 minutes—on why you think we should make the changes and how you think we should go about the changes.

So the rest of my time, sir, I will open up to you to help the committee understand why you think it is critical that we go back to the old rules and get rid of these special considerations for contagion.

Mr. TAYLOR. I think the old rules worked. We thought about them a lot in advance. Other people thought about them. They were put in place to address exactly these problems, which was spillover, emerging market crises, which were very common in the 1990s and continued into the early 2000s.

So it was part of a reform to really provide some guidelines or limits to what the IMF would do in these circumstances. It was essential, in my view, because, otherwise it was very ad hoc, very uncertain, and, in fact, causing the problems.

So it worked well as far as we thought in advance, and in practice it worked well. Moreover, when we violated it, it has been a disaster. So a lot of evidence, it seems—

Mr. MULVANEY. Examples of where we violated it in the past?

Mr. TAYLOR. Greece.

Mr. MULVANEY. Okay. So that is where we are today.

And I guess, to the extent we are still talking about it, it doesn't seem to have solved the problem. I think Ms. Lundsager admits that the contagion risk is still there as of today.

And I would suggest that the $30 billion that the IMF put in probably didn't make the difference one way or the other, but they were always charged with the problem of proving a negative. I hope we get a chance to get a second round.

With that, I yield back the balance of my time.

Chairman HUIZENGA. The gentleman yields back.

And, with that, the Chair recognizes Mr. Heck of Washington for 5 minutes.

Mr. HECK. Thank you, Mr. Chairman. And thanks very much for holding this hearing.

My gratitude as well to the panel. You possess an amazing depth and breadth of expertise in this area, and I am genuinely grateful that you would share your time here.

I just have two questions, if I can get to the second one even, however. I would like each of you to answer the following, beginning with you, Mr. Lowery: Given that the United States' attempt to dissuade other major economies from joining the Asian Infrastructure Investment Bank led by China failed somewhat miserably, what strategy would you recommend that we pursue as a result of that?

And I would like each of you to answer that question, if you would, please.

Mr. LOWERY. In terms of the IMF, I think that I actually—I agree with most of what John Taylor said in terms of some of the reforms.

I think that my own view is that the legislation should be written with conditionality into it, but I don't think that I would hold back the authorization appropriations while we try to solve the problem that John is trying to get at.

I think that should be part of the conditionality of the legislation and that the Treasury Department should work on behalf of Congress within the IMF to actually make the types of changes that John is talking about.

So I think that is the way that I would try to approach it as opposed to taking two unilateral stands, which, obviously, in the Asian Infrastructure Investment Bank we did and failed.

Mr. HECK. So if I heard you correctly, you would have Congress pursue that particular avenue of action. I guess the question, given that we haven't been able to do that very well, is: Absent that, what should we do?

Mr. LOWERY. I am here to say that I think that we, the United States, through the Congress, should be pursuing an action of supporting the IMF. I believe that strongly. I believe that can be done in a way that is conditioned.

I remember sitting in the Executive Branch going through many conditions on the IMF, the World Bank, and many other different institutions in which we were able to meet the obligations that Congress set upon us. They were not easy, but that doesn't mean we couldn't do it. I think it can be done here.

Mr. HECK. Professor Taylor?

Mr. TAYLOR. I think the reform of the exceptional access framework—the United States would not be unilateral here. There is a lot of interest in doing this.

As I mentioned in my testimony, the staff and the management of the IMF seem comfortable with it. So, in a way, it is—the expression is it is almost a slam dunk for the Administration to say, "This is fine."

I don't know what the members will do. I am not part of any negotiation. But this is something that several members seem interested in. It seems to me the Administration knows that they have

allies. The United States is influential, anyway, in these discussions. I think it could move very quickly.

Mr. HECK. Ms. Lundsager?

Ms. LUNDSAGER. Thank you.

I would agree with what Mr. Lowery said, but I would hope Congress could move forward and approve these 2010 reforms and, at the same time, continue to work with the Administration as they work with the IMF to pursue reforms. I think it will be a challenge among the membership to come up with an agreement on how to deal with this going forward.

And I think one of the difficulties will be, under this new framework the IMF is talking about, that the IMF, by standing back a bit and limiting its participation, will either be forcing the country into an immediate debt action when it may not be clear if it is insolvency or illiquidity and, at the same time, then looking to bilateral creditors to step up to the plate to fill up the remaining gap.

And then I fear that the next crisis country that comes along would be a key U.S. ally and then the IMF will be turning to the United States. The United States Administration would have to come to Congress and seek the authorization and appropriation for bilateral support, which, as I recall, has been very difficult even for the very low-income countries such as Liberia or Haiti that we seek to support. Coming up with concessional resources for middle-income countries would be a real challenge.

So I fear that the United States, as an official bilateral creditor, might be turned to in a bigger way and more frequently at a time when we have our own budget considerations and we are focusing on our other priorities. So I am not so sure this new framework is going to work out quite so smoothly. Thank you.

Mr. HECK. To you, again, ma'am. I hope it is an easy yes or no—it is not, but I am going to do it anyway.

Is there a point at which failure to enact reforms renders it all irrelevant because the fact of the matter is, other institutions will have developed over that period of time? How long before we are really in the pinch here because we haven't acted?

Ms. LUNDSAGER. I can't really put a timeframe on it, but it is clear the BRICS, China, are moving ahead in a number of areas, whether it is balance of payments backstops for each other or the infrastructure and BRICS bank. The Chinese are asserting their global leadership.

And I really think it would be terrible if the United States conceded that, when over the years, I found over my many years in government—that countries valued United States' leadership and valued our participation in the international system and our engagement and our listening and our working out what the solution should be to different problems. And I think we should reassert that leadership by getting these reforms done. Thank you.

Mr. HECK. Thank you for your forbearance, Mr. Chairman.

Chairman HUIZENGA. The Chair has been rather generous, yes, with those, but I am happy to do so.

With that, I would like to recognize Mr. Pittenger of North Carolina for 5 minutes.

Mr. PITTENGER. Thank you, Mr. Chairman.

And thank you to the witnesses for being here with us today.

I was troubled and really amazed last week, I guess it was, when I picked up the Journal and there was an article by the President of Greece rebuffing the European Bank for the reform demands that were being required of him. And I thought, how pompous: "I owe you money," and yet, he had the ability to go back to them and say, "How dare you make those requirements." I just imagine myself going to my banker to whom I owe money, and challenging my banker, "How dare you make these demands."

But it brought me to more a clear focus of a different person, Margaret Thatcher. She was in Charlotte some 20 years ago for a dinner to speak of the challenges that she met in Great Britain when she was Prime Minister and all the enormous amount of rebuff that she received and, really, difficulty in trying to bring restructure and reform to her government. Well, go 20 years further, nearly.

A couple of years ago I was with a member of Labor, and we were riding in a bus out to Fenway Park. Joe Kennedy had invited us to come out there for dinner one night. And I just reluctantly brought up the name of Margaret Thatcher and wondering what she would say, knowing the darts would fly. And her comment was, "God bless her. She saved our country. Without Margaret Thatcher, we wouldn't be where we are today."

So I think my question is, the flexibility of exceptional access, has it created the lack of commitment to austerity reform? Has that flexibility created the lack of commitment or interest to pursue that, that they feel like, "Well, they gave me one time. They will be lenient again" and not make that full commitment internally to do what is necessary? Was that part of the case with Greece?

You can each respond.

Mr. TAYLOR. I think, briefly, the concern—it is sometimes called moral hazard—is that, if countries and their people recognize that there is going to be an increased chance to bail out, they will be more reluctant to make the reforms or the things that they need to do.

I have always wondered how you prove that kind of thing, but I emphasize more the uncertainty that is caused by the lack of framework.

I would say, in addition, it is not simply the exceptional access framework or not that is the situation in Greece now. There are a lot of other things happening. If you look at sort of the structural things the IMF wanted them to do, they make so much sense. They are really just moving towards more markets and less intervention by the government.

And, of course, this government in Greece is not interested in that. And so I think that is really the problem. The structural reforms they have to do are clear, but they just don't want to do it.

Mr. LOWERY. If you don't mind, I will weigh in for just 1 second.

I think it depends on the case. Portugal and Ireland were in, not a similar situation, but a pretty bad situation just a few years ago.

They have actually taken on very tough economic reforms in their countries and, frankly, if it wasn't for Greece dragging down sort of the rest of Europe, people would be celebrating how far and how much progress Ireland and Portugal have made during that time.

So it is a tough argument. I think it is a good point that you are making about whether or not—if you put so much money on the table, do governments have a tough time taking those tough steps. I think it depends on the government.

Mr. PITTENGER. Sure. Thank you.

Ms. LUNDSAGER. Thank you.

I would agree with what Mr. Lowery just said. And, frankly, I would also look to the countries that didn't seek IMF programs, but undertook very strong reforms, such as Estonia & Lithuania, Poland & Slovakia, and some of the others in Europe who have really—look at Poland over the years without seeking IMF support, and they have done it because they think it is in their own interest and that it is important for their unity with the European Union.

Mr. PITTENGER. Thank you. I yield back.

Chairman HUIZENGA. The gentleman yields back.

Mr. Kildee of Michigan has decided to pass. But I will recognize the ranking member again for 5 minutes. And we are going to start a second round as well. We still have a few more on our side.

But, with that, Ms. Moore.

Ms. MOORE. Thank you, Mr. Chairman.

And, again, I thank the witnesses for sitting through a second round of questioning.

Professor Taylor, I want to go back to you. You spoke in the first round about—we were finishing our discussion; I didn't go any further—how Greece should restructure its debt, that is what they should have been required to do.

And in the Wall Street Journal, you had an article talking about sovereign debt collective action clauses. And I guess I wanted you to expand a bit on these clauses.

Let me tell you what the thrust of my question is. I am concerned that taking the board's discretion away, not having any flexibility, will impede the operations, just is not workable.

So under what circumstances should the IMF require restructuring versus kind of reprofiling a country's debt? You say it should be part of a preset requirement. But what would be wrong with sort of a case-by-case basis within some framework?

Mr. TAYLOR. A framework, in its own sense, has less case-by-case to it. There is a treatment of, "This is how we are going to treat people or countries in different circumstances." It sort of lays out your strategy to do it.

There are different cases. And whether that is sustainable or not sustainable, for example, that creates different cases. But you ask, "How you are going to treat those different cases?"

So there is flexibility in the sense you have laid out your strategy, but that is laid out in advance as much as you can so people can understand it and so we can assess whether it is working or not and see when there is exceptions to it. I think that is the way to think about it.

There is always a sense in which, especially if you are in public policy, you would like to have—you would like to get around that framework, you would like to, for some reason, do it differently. I have been there myself. I know what happens. Somebody gets a call from somebody who says, "Look, something is wrong here. Our bank is in trouble. Could you help us out?"

And you want to be able to resist that because, no, you have your principles, you have your rules, you have your strategy in place. If it becomes all tactics, it becomes hopeless. So I think that is the—

Ms. MOORE. But the whole point of this hearing is to talk about moral hazard versus contagion. And I guess I am concerned that completely abandoning the new regime that is being proposed would, of course, help us avoid more moral hazard, just to say, "We are not going to lend to you."

But I guess, Ms. Lundsager, Mr. Lowery, do you think that would increase the contagion?

Ms. LUNDSAGER. Thank you.

I would be a little bit worried because I fear that, if they set this in place, there is going to have to be some sense to the market and everyone what is the number, what is the debt-to-GDP number that is going to be the cutoff.

We have the Maastricht numbers in Europe of 60 percent, and we have seen how well that has worked. But we don't know, really, what is sustainable in countries.

And so, in Ukraine, they have set a goal of 70 percent of GDP. In Greece, the goal was set at 120 percent of GDP. How do we know what exactly is sustainable and what is unsustainable?

And my fear is that U.S. authorities would be faced with the situation of a country saying, "No. I am going to take the measures. I am going to adjust. I want to honor my debt."

Brazil did this in the early 2000s. They were not going to restructure, even though market commentators all over the place were saying Brazil would have to restructure. They did not restructure. They had a fund program. They drew on it. They adjusted and turned things around.

And so it is very hard, if you have someone like that calling the White House and saying, "No. I am not going to restructure my debt. The fund is pushing me into something that is not needed," for the United States bilaterally to resist that—right?—if it is a key U.S. ally. So I think we need to keep the flexibility. Thank you.

Mr. LOWERY. On my part, I—you are talking about a very, very tricky issue, which is the nuances of moral hazard and the nuances of contagion.

I am not a humongous believer that there is moral hazard to countries. I am a believer that there is moral hazard to lenders and to investors. But could there be contagion? I think the answer is yes.

But that does not mean that we should have the exceptional access—or systemic exemption for the exceptional access does strike me as a loophole that is extremely large.

And so I would want to tighten it up, whether it is going back to the proposal that John Taylor is talking about, going to the proposal IMF staff is pushing. I would want to close it up a bit because of that worry.

Chairman HUIZENGA. All right. The gentlelady's time has expired.

And, with that, I need to correct a slight misstep on my part. We are supposed to go through an entire round first before we recognize Members a second time.

Ms. MOORE. You are so kind, Mr. Chairman.

Chairman HUIZENGA. I am here for you, Ms. Moore.

So, with that, I would like to recognize the new member of the committee and the subcommittee from Minnesota, Mr. Emmer, for 5 minutes.

Mr. EMMER. Thank you Mr. Chairman. And thank you to the ranking member and the panel. Thank you for being here.

I think I will be brief. It is interesting getting up to speed. And I appreciate the information and all the background materials.

The IMF, along with the World Bank and the World Trade Organization, have all been around for 70-some years. The IMF had a different initial purpose that changed in 1973, primarily, when we adopted a new system of floating exchange rates. And I think today this institution plays a major role in monitoring the economic and financial policies of member countries.

I think, Mr. Lowery, you started off by saying there are three specific tools: technical assistance; surveillance; and lending when necessary. It caused me to wonder about the surveillance piece. Where are we at today? And this is for all of you.

But if surveillance has been a tool of the IMF since the 1970s, maybe even before, since the beginning, why wasn't the alarm bell sounded well in advance of the Asian crisis? Why weren't we given warnings through the IMF about the crisis in 2008?

We have talked plenty about Greece. But could you just, amongst the three of you, whomever wants to address where is the surveillance at, why didn't it work back then, or maybe it did work and we just didn't hear about it, and what needs to happen in the future?

Mr. LOWERY. My own view is the surveillance piece of what the IMF does is probably the most important piece. It is the least talked about in some respects because there is not really money involved.

But in terms of getting it right and understanding exactly whether or not a country is on the verge of catastrophe financially, it is a hard thing to do. Markets don't get it right. And there is, obviously, people making a lot of money out there thinking about this. And official sector actors don't get it right.

But I think that the IMF does a pretty good job of looking at a number of countries as to why they didn't get this right or that right. I think that, one, sometimes their advice is not listened to, so that can't be on the IMF; and two, sometimes they just get it wrong.

There are good economists there, but at the same time, it is hard to see, sometimes, where the crisis is going to come from. We look at our own country. We have how many people surveil, analyze, think about the U.S. economy? Only a handful got it right back in 2006 and 2007.

Mr. EMMER. Which I appreciate.

Professor Taylor and Ms. Lundsager, please take the next step. But you had two major ones in the late 1990s and then 2008. We weren't just talking about one country. We were talking about a whole bunch.

The question is, why? And what has been done to, hopefully, improve that so it doesn't happen in the future?

Mr. TAYLOR. I think the surveillance with respect to other countries is important to think about, not just the major countries. And, also, that verges into this third role of technical assistance, which I think is very important.

There are a lot of countries that just don't know about even budgeting or about monetary policy. And so there is actually good advice that can be conveyed.

I actually think that, in a way, maybe there should be a fourth category. It is possible to have programs without loans. It is something called a program support instrument, I believe.

But it is effectively like an IMF program where you lay out, "Here is our"—it may be like a debt reduction strategy. It may be a way to get inflation down, whatever it happens to be. But the IMF works with a country. But it doesn't have to be a loan.

Frequently the loan is the way they engage, but there are other ways to do it, which I would prefer. You engage with them and you help them. And there are people who haven't really haven't done much before. And the IMF does have expertise on that.

Ms. LUNDSAGER. Thank you, John, for mentioning the policy support instrument. I agree that has been very important and countries have liked that.

In terms of the IMF engaging in surveillance, what has been really important is that the IMF has conversations with officials, the annual article IV review, and will raise its frank concerns.

So, in 2008 and 2007, it was raising concerns in the United States about the subprime loans, even though the broad view across the Federal Reserve System, across many commentators, was that, "Oh, we can handle this. These loans are a small part of our mortgage side."

Well, it turns out it wasn't such a small part, and it was a problem. But at that point, there wasn't agreement that it was going to blow up the way it did.

So the strength of the IMF is to bring issues to the fore and to raise them with the country authorities and to say, "You really ought to be worried. We see imbalances emerging here that—perhaps you are seeing your debt having to be more and more short term. You are not able to issue longer term debt in an emergency."

So I think the IMF has done a very good job on that. But sometimes that is more private than public because the IMF, of course, doesn't want to be the cause of a crisis by saying, "Oh, it is headed your way."

Mr. EMMER. Thank you. My time has expired.

Chairman HUIZENGA. The gentleman's time has expired.

With that, we recognize the gentleman from Arizona, Mr. Schweikert, for 5 minutes.

Mr. SCHWEIKERT. Thank you, Mr. Chairman.

In a small attempt to sort of go on the theme of the hearing, the moral hazard, I would like to do this slightly more conversationally, because I want to sort of do the "Wayback Machine," for the last 25 or 30 years.

From the 1980s to the 1990s, being someone who was very interested in the Tequila Crisis, when the Asian tigers—having been in Thailand, visited it on my way to India, when all hell was breaking loose.

What countries through IMF and other bilateral agreements kept their promises, demonstrated a level of discipline? And where did we create almost a cycle where, once again, we see Argentina unavailable for comment or constantly—so walk me through this.

And then, as we are doing this, I have always had a concern about some of the debt swap mechanisms, particularly when it is private capital being swapped out, and making sure that it does not become sort of a bailout mechanism for either bad credit decisions or large industries or large banking institutions that are ultimately swapping their debt position for what eventually is taxpayer money from around the world.

Mr. Lowery, could you start with this, what has worked and what hasn't and debt swaps?

Mr. LOWERY. I think that what works usually is when the countries themselves make the reforms. It is not about the IMF imposing those reforms. The IMF will try to impose those reforms as part of its conditionality.

But when the countries start adapting those reforms—you pointed to Mexico back in the Tequila Crisis. The Mexican authorities took very, very difficult steps over the next few years after the crisis, in 1994 and 1995, to the point where the ruling party lost its power in 2000 for the first time in 70 years.

Mr. SCHWEIKERT. But that also had an additional—was it $50 billion through U.S. taxpayers?

Mr. LOWERY. Yes.

Mr. SCHWEIKERT. Managed by the IMF, but—

Mr. LOWERY. No. No. The IMF did not manage. The taxpayer money—

Mr. SCHWEIKERT. I thought that the $50 billion came from a special—

Mr. LOWERY. The exchange stabilization fund within the Treasury Department.

Mr. SCHWEIKERT. But those dollars were managed through the IMF, I thought.

Mr. LOWERY. No. That was actually managed through the Treasury Department.

Mr. SCHWEIKERT. Okay.

Mr. LOWERY. It is one of the few times that the Treasury Department actually kind of worked almost like the IMF during a crisis.

Another example would be Korea back in 1997. An example I know that John worked on very closely, which would have been Uruguay. So during the Argentina crisis, which you mentioned, Uruguay also went through a crisis.

Mr. SCHWEIKERT. Because of the limits of time, your model basically is, when the countries produce the list of reforms themselves, we have better outcomes?

Mr. LOWERY. Yes. When they are very serious about—

Mr. SCHWEIKERT. Professor Taylor, tell me, what has worked out there, what hasn't, and your vision of what—

Mr. TAYLOR. I agree with that part for sure.

I think there are other things. That is the nature of the engagement. I like to compare Russia in 1998, where there was contagion.

That decision was a shock, not to continue funding. It had to do with politics, a concern about the nuclear arsenal, et cetera. It

wasn't really an economic decision. And there seemed to be a lot of contagion.

Then you move 3 years later. And while Argentina was a problem, there wasn't contagion when it defaulted. It was really zero. And that is, I think, because the nature of our engagement was very clear, what we were going to do, when we were going to do it.

And, also, there was the sense of trying to help Uruguay and Brazil nearby. So you had another way rather than just to do the bailout. So I think the nature of the program matters, too.

Mr. SCHWEIKERT. Ms. Lundsager?

Ms. LUNDSAGER. Thank you.

I think the ultimate goal or the immediate goal to fund programs is for countries to adjust enough, restore confidence, and resume borrowing from private markets.

And I think we have had a number of successes in that case. And we have seen it in Europe, successes in terms of Ireland and Portugal turning things around.

Mr. SCHWEIKERT. If I were to look at our last 25 years of history of participation, what would you consider our greatest failure and our greatest success? And what was the difference?

Ms. LUNDSAGER. I would say our greatest success is managing to convince the world that we still believe that being multilateral is important, that the United States is deeply engaged.

Mr. SCHWEIKERT. I was trying to get it down to a country level. I know that is more uncomfortable. I am trying to understand—

Ms. LUNDSAGER. I would say Mexico.

Mr. SCHWEIKERT. So Mexico post-1994?

Ms. LUNDSAGER. Yes.

Mr. SCHWEIKERT. And what do you believe is our greatest failure?

Ms. LUNDSAGER. What is going on in Greece right now is a failure on the part of Greece and a failure on the part of everyone else as well to be able to put this together.

Mr. SCHWEIKERT. Any quick comment in my last couple of seconds on my debt swap concern?

Ms. LUNDSAGER. I'm sorry. I didn't quite understand what you meant by debt swaps.

Mr. SCHWEIKERT. The IMF comes in, provides a bilateral loan, and it is often used to pay off or move money around to pay off other obligations that are privately held.

Ms. LUNDSAGER. Yes. At times, the Fund does help countries honor their current obligations, and that can include paying off some of the private debts.

But, as I said, the goal is to restore enough confidence that in a very short amount of time those private creditors do come back to the country.

Mr. SCHWEIKERT. I yield back, Mr. Chairman.

Within that, should be a conversation of what haircuts should be required by all participants.

Thank you, Mr. Chairman.

Chairman HUIZENGA. The gentleman yields back.

I will note that you have definitely gotten the attention of every intern on Capitol Hill, talking about haircuts and tequila crises. There is great worry happening here on Capitol Hill.

With that, the Chair recognizes the gentleman from New Mexico, Mr. Pearce, for 5 minutes.

Mr. PEARCE. Thank you, Mr. Chairman.

I appreciate each of you being here.

The Wall Street Journal said earlier this year, I think it was, that the IMF departed from its own regulatory rules and limits in order to make loans to Greece.

Is that a fair characterization, Ms. Lundsager?

Ms. LUNDSAGER. Thank you.

That was what we have been talking about in terms of the IMF changing the exceptional access rules when the staff and management asked the board to approve the program in May 2010.

Mr. PEARCE. I found that amazing. Earlier this year, I asked Secretary Lew that same question, and he said that he didn't believe they had changed anything, that they were acting with the same rules as before. I found that to be an amazing statement.

What impact is the failure of Greece to pay earlier this week or whenever it was they didn't make their payment—what impact is that going to have? Mr. Taylor, I would look at you on that. What is the impact going to have worldwide on the confidence in the system?

Mr. TAYLOR. It is very unusual to do this, although, technically, they can bundle, as I understand it. If they really completely go into arrears, then that is really damaging to the IMF. And I hope that doesn't happen, but it is on its way.

It is actually, I think, for me, in our discussion an illustration of some of the problems I think you get into when loans are made to countries whose debt is just not sustainable. I wouldn't say I want to blame all this on that. There are obviously many other things.

But I look back at what if, in 2010, there was then a serious restructuring of Greece as part of that loan. It would have made it much easier for Greece to start making the adjustments.

But it was delayed, and then they had a restructuring. And it was sort of part of—people hoped that would be enough, and they said it wasn't enough.

So I think addressing the problem at the time would have made a difference. And it is a counterfactual. You don't really know.

But I think, to me, it is an example of why you need those frameworks and why changing them, especially at the same time you make the deal—that is probably the most disturbing.

Mr. PEARCE. Thank you, sir.

Ms. Lundsager, I have read reports. I don't know if it is accurate myself. But in the surveillance of country policies, one of the reports is that Greece is having trouble because up to 40 percent of their population just refuses to pay the taxes that they owe. In other words, it is well-characterized.

Is that report somewhat accurate?

Ms. LUNDSAGER. IMF staff reports have highlighted the problems with revenue collection, and that has been an element of the program from the beginning.

So the Greek authorities are working on making the revenue administration more independent and doing a better job to have their own citizens—

Mr. PEARCE. And my quandary is that the average pay in my district is probably $31,000 to $35,000, and I have to go back to that district and explain to them why I should use their money to pay for people who refuse to pay their own taxes to bail them out.

And I understand what you are saying, that the entire world system is kind of on thin ice and, if we don't do anything in the Eurozone, then we have spreading problems. But, to tell you the truth, people just barely making ends meet in New Mexico, they could hardly care, and I am not sure I am willing to make the case to them.

So I just—

Ms. LUNDSAGER. I insisted on improving tax collection in every statement I have made on the Greek programs. Absolutely.

Mr. PEARCE. I appreciate it.

Mr. Lowery, one of the things that I see a lot in the press about is that the IMF has recast itself, that they were facing the irrelevancy, or whatever words that one of you used in your testimony, and that one of the things they are doing in this reinventing is placing themselves where they can become the world's reserve currency with the SDRs and getting some gold to back that up.

Is that a real possibility, in your opinion, that becoming the world's reserve currency—

Mr. LOWERY. No.

Mr. PEARCE. Ms. Lundsager?

Ms. LUNDSAGER. No.

Mr. PEARCE. Mr. Taylor, how about you?

Mr. TAYLOR. No.

Mr. PEARCE. You don't think it is a possibility?

Mr. TAYLOR. The SDR is a different—

Mr. LOWERY. The SDR is a reserve asset for how the IMF moves money among its members. It has nothing do with how you and I go buy a candy bar. We are not using an SDR.

Mr. PEARCE. Have you seen those reports that are saying that they are positioning themselves to take the place of the United States when people lose confidence in our currency?

Mr. LOWERY. I haven't seen those reports, and I wouldn't put much stock in them.

Mr. PEARCE. Okay. All right. I see my time has elapsed, Mr. Chairman. I yield back.

Chairman HUIZENGA. The gentleman yields back.

And still seeing no additional new Members on the Democrat side, we will continue with our side for our first round.

Mr. Guinta from New Hampshire is recognized for 5 minutes.

Mr. GUINTA. Thank you very much, Mr. Chairman.

Professor Taylor, you touched on something a little bit earlier that I am interested in. When I go back and look at the categories of focus of the IMF—lending, technical assistance, and surveillance—you touched on what I think you referred to as possibly a fourth area, what you called program support.

That is something I am very interested in because I subscribe to the notion that—as Mr. Pearce was saying, this concern that con-

stituents have about utilizing taxpayer money to bail out people in foreign countries.

So it lends to the argument or the discussion of, how do we change the mission or modify the mission of the IMF? So you touched on it a little bit.

But could you talk about, in the context of trying to keep balance within the financial world, what program support without a loan program could look like and how that would differ from what we are doing relative to, say, Greece: when we bail out, they fail to make a payment and you see front page news as a result of it?

Mr. TAYLOR. Actually, it has been done, a policy support instrument. I guess the word is policy, not program, support instrument.

And the goal is to have the same kind of program you would have as if you gave a loan to a country, with payments and tranches and all that, except you wouldn't have that. You would engage—you could think of it in our context.

I just testified at the Budget Committee this morning. As you know, the resolution has a 10-year program to reduce the deficit to zero in 10 years. So that is like a policy.

And so now you consider another country wants to implement such a policy and the IMF helps them with it. And they don't have to give them a loan to do it. They just help them with it. They maybe have meetings at certain dates. They have benchmarks to make. And it can work very well.

Traditionally, that has been done in the context of a loan. But you really don't need a loan in many cases. And the loan kind of screws things up. So often debt becomes a major problem in our engagement.

So I think it is a great idea. I hope they do more of it.

Mr. GUINTA. Should we be considering what the debt-to-GDP ratio is in how we—and I want to ask this of Mr. Lowery—how we consider the countries to which the IMF loans?

Mr. LOWERY. Yes. I think that is a helpful statistic in terms of trying to figure out the debt sustainability of a country.

And this goes towards kind of the aspect of, if a country gets into a balance-of-payments problem—so not the policy support instrument you guys were just talking about, but an actual balance-of-payments problem—one of the measurement tools that the IMF will be looking at is: What is their debt-to-GDP? What does their debt profile look like going forward? What is their stock-to-debt going forward? They are trying to make a judgment: Is this a liquidity problem or do they have a solvency problem?

And that, I think, should help you make an argument as to what could the IMF do to help in that situation and do you need to go to a situation where the IMF can do something, but they can't do all of it. And so there needs to be some debt reprofiling or debt restructuring or what have you.

Mr. GUINTA. So in the circumstance of Greece, would you identify Greece as more of a solvency problem than a liquidity problem?

Mr. LOWERY. Yes. And I think the IMF would say that, too. And, remember, Greece has gone through two sections of—in 2010, it was IMF money plus European money on the table. In 2012, it was more IMF and European money, but also they restructured and

took a big haircut, to use the words that were used earlier, on private sector creditors.

And now we are in a situation where the only creditors left, pretty much—I think it is about 80 percent—are official sector creditors. And you do see reports out of the IMF that they think European members are going to have to potentially take a haircut themselves going forward.

Mr. GUINTA. What is the debt-to-GDP ratio for Greece? Do you know? Rough guess.

Mr. LOWERY. I am guessing it is about 175 percent.

Mr. GUINTA. Okay. So I think I heard Ms. Lundsager say earlier—I don't want to put words in your mouth, but I thought you said something like it is sort of difficult to specifically pinpoint what that ratio should be.

But I think it is probably fair to say, logically, people would argue that kind of ratio is excessive and it is not liquidity, it is solvency. So it would stand to reason that a program support approach, in my view, would make more sense in the context of Greece, at least at that level.

Is that fair to say, Ms. Lundsager?

Ms. LUNDSAGER. I think that is a possibility, where the IMF could be there providing advice and helping put the overall economic policy program together.

And then the Europeans and the private sector, through a debt operation, would provide the financing. That certainly is a possibility.

Mr. GUINTA. Thank you.

Chairman HUIZENGA. The gentleman's time has expired.

We are going to go into round two. And as I have been consulting with my good ranking member, she has slid into that round two before we were supposed to. Mr. Heck is choosing to pass at this point.

So going into round two, I am going to take my 5 minutes. I may not use it all. But I wanted to touch on a couple of quick things.

Just as I have been listening through all this, I am curious, Dr. Taylor, in your view, returning to Greece and sort of the systematic exemption here, what would have happened had the IMF not stepped in? Would the EU and the ECB have really picked up that slack, in your opinion?

Mr. TAYLOR. I think it is quite possible. Early on, the Europeans said they didn't want the IMF in. The president of the European Central Bank, Jean-Claude Trichet, originally had that position.

So at the time of 2010, I wasn't in the room, but my sense is the Europeans could very well have started providing loan support. It may have been that they would have asked the IMF to monitor.

It wouldn't have been called a policy support instrument, but the IMF could certainly have monitored the framework and the conditions. But I think that is one possibility.

The Europeans talk most about the spillovers. I think a lot of their banks were holding the Greek debt at the time. So they would be talking their banks' books, so to speak. I wasn't in the room. I don't know for sure how that worked.

But another possibility would be very straightforward, saying, "Look, the debt is not sustainable. There are a lot of people in the

private sector who are holding this debt. If we are going to put some new money in, the private sector has to think about reprofiling or more, restructuring."

And that is kind of the ideal, really. That is really what the exceptional access framework—if it is working well, that is what you would want to have happen, because you don't want the public sector just to bail out.

In the banking area, we call this bail-in. Right? The Europeans call it bail-in now. We want some bail-in in these cases as well. So I think that is the ideal.

Chairman HUIZENGA. Do you believe that it was maybe more of an intent that the Europeans had a belief that, with the IMF getting involved, that they would come in and sort of play bad cop to their good cop with Greece?

Mr. TAYLOR. I don't know. I'm sorry.

Chairman HUIZENGA. All right. I want to touch a little bit on Ukraine and support of the IMF that they have.

Last week IMF stepped in and said it may go ahead with a $1.7 billion payment to backstop the country, even though the Fund has been wary about lending to countries that are in arrears with private creditors.

And, obviously, Ukraine has a certain strategic importance to us and to Europe and the Europeans. And I am curious, any of the three of you, how you view the IMF's involvement in Ukraine so far? Any of the three of you feel free to jump in.

Mr. TAYLOR. Let me say this is part of a broader context, and Ms. Lundsager also referred to this. There is always a strategic aspect of our engagements with countries. And sometimes there will be a strategic aspect of another country's engagement, maybe an African case for Europe.

And I think it is really important to try to distinguish those as much as you can. Sometimes it is going to have to be there. But, ultimately, some of those things are going to have to be bilateral rather than use the international institution.

I think the Uruguayan thing is very complicated because it has both strategic and serious economic issues. You just have to be wary of those circumstances. The exceptional access framework is a way in which you can bring the economic considerations in more rather than the political ones. I think that is generally healthy. You can't do it all the time.

Ms. LUNDSAGER. Thank you.

I was just going to add that, on Ukraine—and I am not part of this decision-making, but I suspect the point is to indicate that the IMF and the community—the executive board representing all the countries wants to continue to support Ukraine so it can take the measures it is starting to take, reforms that are very much needed, and to keep the pressure on the private sector to come to the table and reach terms on finding a way to work and reduce the debt burden that Ukraine is facing.

So I think that is why the IMF is going ahead, because Ukraine is still working with the creditors, consulting and negotiating, but the intent is to keep the country going, too.

Mr. LOWERY. The only thing I was just going to add is I think Ukraine is a very difficult circumstance. IMF is putting money in.

They are actually taking a lot of the type of actions that John Taylor has talked about, which is they are actually saying, "We need you to do a debt restructuring with your private creditors," which they are trying to do. And they are taking significant reforms, the Ukrainian Government.

The biggest problem Ukraine has is Russia. That is creating huge, huge financial and economic pressure. So they can be taking lots of reforms, but they have this significant problem right next to them.

Chairman HUIZENGA. Okay. My time has expired.

With that, I will recognize our Vice Chair for a second round, Mr. Mulvaney.

Mr. MULVANEY. Just a few things.

Professor Taylor, to follow up on a question that the chairman asked you, you mentioned that when the Greek crisis originally started, the Europeans had expressed some concern about the IMF getting involved.

Do you have any insights as to why they were apprehensive about that?

Mr. TAYLOR. I really don't. I think the issue was—remember, the IMF lending to these developed countries is quite unusual in recent years. Emerging markets have been the focus.

In fact, the exceptional access framework had—so, in a sense, the Europeans I think originally were saying, "This is our problem. We don't want the IMF here. The IMF is for those guys who are problem guys," Latin America or something.

I think that was the concept that they had. I don't think I know for sure, but that is my sense, that, "We will handle this," but then it just got too big. I'm not sure.

Mr. MULVANEY. Ms. Lundsager, you were involved at that point. Correct?

Ms. LUNDSAGER. Yes. In Greece, yes.

Mr. MULVANEY. Any insight as to why the Europeans—same question to you. I am just trying to get a feel for the lay of the land in 2010, I guess.

Ms. LUNDSAGER. Again, I wasn't directly in the conversations with the European leaders. But I understood that, initially, they felt that, if it is the Eurozone, they should solve the problem themselves, which, of course, many of us fully supported.

But I think, in the end, what happened was the Europeans realized they are going to need a real adjustment program in Greece and that it was very difficult for the Europeans to do that bilaterally, to impose that kind of conditionality.

And, furthermore, for them to come up with the financing all on their own meant—and it did initially as well with the EFSF—they had to go back to each one of their individual Parliaments for approval. So it took a while to—

Mr. MULVANEY. It took some time.

Ms. LUNDSAGER. Yes. It took some time.

So I think, in the end, they realized they needed the IMF because the IMF can move quickly and pull together the resources.

Mr. MULVANEY. Coming forward to an issue that I think Ms. Moore raised regarding bailouts, you mentioned bail-in, Professor Taylor. The money ultimately ended up where?

At the beginning of the crisis, most, a majority—I don't remember the percentage—of the Greek debt was held by private financial institutions, Ms. Moore. At the end, it had been socialized, held by governments and by the IMF.

It strikes me that what the IMF did is bail out the private banks in Europe. Am I wrong about that? The money certainly didn't go to the Greek people. And to the extent it went to the Greek government, it was immediately paid to the private money center banks. Correct?

Mr. TAYLOR. I think that is a good way to describe it. It is not perfect. Bailout is an ambiguous term. But I think that is right.

Originally, you had a lot of private sector holding debt, and now you have a lot of public sector holding debt. So it does look like—I think the word "swap" was used earlier.

Mr. MULVANEY. And I know she has to leave. But I do hope that our Democrat colleagues understand that some of us have a problem with that and that, if we are looking to reform the IMF, it may be to prevent circumstances like that.

That is a very different thing for the IMF to do. If they were lending money to a Third World country, to an undeveloped nation, that really wouldn't be as much as an issue as they are when they are lending to either emerging economies or even more so to developed economies.

So, anyway, I am starting to get a little sidetracked on various issues. Thank you very much for your time.

I yield back.

Mr. LOWERY. Can I just make—there is one slight amendment in that—

Mr. MULVANEY. Sure.

Mr. LOWERY. —in 2012, Greece did work with the IMF and there was a fairly significant haircut to a number of private creditors. So I don't disagree with the premise of your question in the 2010. But, in 2012, there was actually—a lot of private creditors took a major haircut on their claims.

Mr. MULVANEY. Thank you, Mr. Lowery.

And thank you, Mr. Chairman.

Chairman HUIZENGA. The gentleman yields back.

And we have had votes called. We are going to try and quickly get in one or two more, if that is okay with the panel.

And, with that, I would like to recognize Mr. Pearce from New Mexico for 5 minutes.

Mr. PEARCE. Thank you, Mr. Chairman.

Kind of following along the same line—you may have already answered. I apologize. I have been in and out—there is generally a truism in business that when the bank loan gets big enough, they no longer have a loan. They have a partner.

Was there a conversation like that in the IMF as we are going up to lending to Greece, that we are lending at 3,200 percent of their quota share? Was there any conversation in the room?

Ms. Lundsager, I think you would be the one who might have been there.

Ms. LUNDSAGER. Thank you.

We were all very aware that it was a large number in terms of percent of quota. In terms of Greece's GDP, it was maybe around 12 percent of Greece's GDP.

And, of course, earlier we had done some fairly large programs. The Uruguay program was about 18 percent of GDP. And I always preferred that metric because quotas could be very much out of line in terms of a country's real economic situation.

So, yes, all board members were very well aware of how big the program was. But it was the sense that—and I went back and looked at the discussion and what I said. But at every board meeting I insisted that the Europeans reconfirm their support for their Eurozone partner, which they did.

Mr. PEARCE. They did give that support?

Ms. LUNDSAGER. They did give that support. Of course, it is conditioned on the Greek authorities adhering to their program.

But my bottom line is I still feel that it is very much the European responsibility to ensure that Greece honors its obligations to the IMF.

The IMF has been a supremely valuable institution for Europe not just in the Eurozone, but in European engagement with countries around the world. So I do look to my former European colleagues, their governments, to make sure that this problem is resolved. Thank you.

Mr. PEARCE. You had also mentioned that you had insisted that adjustments be made in the way that the Greek authorities collect their taxes.

Ms. LUNDSAGER. Yes.

Mr. PEARCE. You went ahead and voted for the transfer even though I don't think they have made much progress in collecting those taxes.

But you voted for the loan.

Ms. LUNDSAGER. Yes. I voted for the loan, and I did support the reviews that came along the way, again, because the Greek authorities were committing to taking measures. They would have taken some parliamentary actions and were committing to take additional measures.

We did start to see some improvements in some of the numbers, even though I think many of us were hoping that there would have been quite a bit better performance.

Mr. PEARCE. Okay. If the performance stays roughly the same as it is and the question came up again and they maybe weren't making their payments and asked for more money, would you still vote for it?

Ms. LUNDSAGER. Well, no. If a country is not making its payments to the IMF, basically, it can't draw on the IMF. And, frankly, Greece hasn't been able to draw this past year while this program review has been under negotiation. But any country in arrears to the IMF cannot draw.

Mr. PEARCE. Let's say that they make the payment that was due. Let's say they make that, but they have not made the internal adjustments.

Because I asked the German Bundestag or Bundesrat, whichever was here, "How long will your people tax themselves more in order to pay for the people who refuse to pay their own taxes?"

They understand that is a ticking bomb that they are going to have to deal with at some point because the Germans appear, when I visited there last, that was getting to be softer ground, that total commitment to the idea that we are going to hold the Eurozone, no matter the pain, was being felt at the ballot box. And that was the ultimate test.

So if they made their payments and they had not made significant changes in their internal collections, would you still vote then if they were asking for more?

Ms. LUNDSAGER. It would depend on the constellation of what they were proposing they would do.

Mr. PEARCE. Fair enough.

I yield back, Mr. Chairman.

I appreciate the input from all of the panelists. Thank you very much.

Chairman HUIZENGA. The gentleman yields back.

And, with that, we have about 8 minutes left to go in our vote, so I am going to call an end to this hearing.

I just would like to say thank you to each of our witnesses for their testimony today.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

And with that, this hearing is adjourned.

[Whereupon, at 3:37 p.m., the hearing was adjourned.]

A P P E N D I X

June 17, 2015

Statement of the Honorable Clay Lowery
Vice President
Rock Creek Global Advisors LLC

Before the U.S. House Subcommittee on
International Monetary Policy and Trade
June 17, 2015

Chairman Huizenga, Ranking Member Moore, and Members of the Subcommittee, I thank you for the opportunity to testify on the International Monetary Fund.

My name is Clay Lowery and I am currently Vice President of Rock Creek Global Advisors, a consulting firm that advises its clients on international economic and financial policy matters. I also serve as a visiting fellow at the Center for Global Development and as a senior advisor to the Center for Strategic and International Studies. From 2005 to 2009, I was the Assistant Secretary of International Affairs for the Treasury Department which exercises oversight of the executive branch of U.S. involvement in the IMF.

I am honored to be testifying alongside John Taylor, who is not only a former boss of mine at Treasury but also one of the most important macroeconomic thinkers in the United States, as well as Meg Lundsager who is a former colleague of mine for many years and deeply knowledgeable about the IMF.

In my testimony, I will describe (i) the core functions of the IMF, (ii) the quota reform package negotiated by IMF members in 2010, and (iii) why I think Congress should approve legislation to implement that reform package.

The IMF

The United States and its allies established the IMF, along with the World Bank and the predecessor of the World Trade Organization, during the Bretton Woods conference of 1944. The idea at the time – an idea that is still true today – was that international cooperation on key economic, financial and trade issues and the maintenance of an open, rules-based economic order are important for global stability and prosperity.

For its 188 member countries, the purpose of the IMF is to promote three objectives: macroeconomic stability, financial stability, and economic growth. The IMF has three primary tools to achieve these objectives:

1) It provides technical assistance, particularly to fiscal authorities, in areas such as data collection and analysis, expenditure management and tax administration. For instance, the IMF is currently providing assistance to the Government of Afghanistan in statistical data systems and customs issues.

2) It conducts surveillance on a country, regional, and global level. IMF staff monitor countries based on their monetary, fiscal, foreign exchange, and financial policies and analyze factors such as capital flows, a country's balance of payments, and structural issues that can impact a country's macroeconomic or financial position. The IMF identifies strengths and vulnerabilities and provides recommendations – privately and publicly.

3) It lends to countries that are suffering from a balance of payments crisis and provides a line of credit to countries implementing sound policies that want additional insurance in case of external or even internal shocks. Some people confuse this lending activity with the work of the World Bank. For comparison sake, the World Bank is designed to provide long-term finance – whether project finance or direct budgetary support – to assist less developed countries. The IMF, by contrast, provides temporary support to any of its member countries – not just the least developed – to stabilize that country's financial situation or insure against shocks. Currently, the IMF has roughly 20 lending programs[1], including notable ones with Greece, Ukraine, and Jordan, and currently has undrawn lines of credit extended to countries such as Mexico and Poland.

The IMF and the World Bank also differ in their mechanisms for financing loans. Member countries provide the World Bank with capital that enables the institution to issue bonds in global capital markets. The World Bank uses the proceeds to provide financing to its borrowing countries. In contrast, the IMF is less like a bank and more like a credit union in which members contribute shares to a general resource fund from which the IMF can provide loans. The size of the contribution, which is called a country's quota, is based on a formula that takes into account a country's economic size relative to other members.

IMF members decide collectively how to allocate IMF resources. Unlike some international institutions where each country is allowed one vote, the IMF largely bases its voting share on the size of the country's contribution. The United States is the largest economy in the world and its voting share is almost 17 percent, whereas the next largest voting share, held by Japan, is slightly more than 6 percent.

[1] The IMF also extends highly concessional finance to lower income countries. These programs are typically much smaller. There are roughly 20 of these lending programs at this time.

Before explaining the quota reform package of 2010, it is important to understand how the IMF lends money. When the IMF provides loans, the country receiving funds is usually in deep financial trouble, such as a liquidity crisis or a potential solvency crisis. As the IMF does not receive collateral for this highly risky form of lending, it instead relies on two key factors: (i) a presumption that IMF loans are senior to other creditors, and (ii) conditionality on macroeconomic and financial reforms to alleviate the concern that the IMF is simply "throwing good money after bad." We are currently witnessing how difficult these reforms can be in the drama taking place among Greece and its official-sector creditors, including the IMF.

Quota Reform Agreement

The IMF has evolved since its founding seventy years ago, and it must continue to evolve in order to remain relevant and legitimate. A key weakness of the institution has been that IMF voting shares – again, based on a country's relative economic size – have not kept up with economic reality.

Starting roughly ten years ago, the United States led an effort to change the voting structure within the IMF so that emerging market countries would receive a greater share of the governance responsibilities in the IMF. This made sense to the Bush Administration then, as well as to the Obama Administration now. The proposal was to increase the voting shares for some countries while decreasing it for others because the relative size of economies in 2015 no longer reflects what it was in the 1950s, 60s, and 70s. A series of negotiations with interim steps took place culminating in the 2010 quota reform package, which is the subject of pending legislation. The package has two major governance reform elements and one significant financial element.

1) First, it alters the voting weights to reflect more accurately today's global economy. Countries such as China, India, Mexico, Brazil, Korea, and Singapore will see their votes increase noticeably, whereas a number of European countries, oil-producing states and a few others will see their voting shares decline. The United States' voting share will barely change at all, moving from 16.7 percent of the total votes to 16.5 percent.

2) Second, it alters how voting shares are translated into "voting chairs" which oversee the IMF's management day-to-day. While there are 188 member countries in the IMF, there are only 24 board seats.[2] By mandate, five of these seats are held by the U.S., Japan, Germany, France, and the UK, while the remaining seats are held by different constituencies of countries – typically based on geographic regions. In many respects, the mandatory appointment of board

[2] IMF governance consists of staff and management reporting to a "resident" board of directors that represent member countries and vote on day-to-day decisions at the IMF. This structure is overseen by a board of governors consisting of finance ministers and central bank governors. The United States is represented at the board of governors level by the Secretary of the Treasury and at the board of directors by a senate confirmed official.

seats is part of the larger problem of imbalanced representation within the IMF. While European member states occupy 8 or 9 of the 24 chairs, including three mandatory appointments, Africa has 2 chairs representing 46 countries and Latin America has 2 or 3 chairs. Under the quota reform package, the mandatory appointed seats would be eliminated and Europe would consolidate its board chairs, thereby enabling dynamic emerging markets to enjoy greater representation. This proposed change is significant, as the number of board seats occupied can be just as significant as voting shares when an issue is brought forward to the board for debate.

Some observers have raised the concern that the reform package would include the U.S. also giving up its appointed seat. In the end, however, this turns out to be irrelevant. Let me explain:

> Today, each board seat represents a constituency of countries that together account for -- on average – four percent of the voting shares (100 percent of the voting share divided by 24 board seats). The United States has nearly 17 percent of the voting shares, nearly four times the amount of those represented by the average board chair, and therefore will be assured of maintaining its board seat despite no longer having an appointed seat.

In addition to improving the IMF voting structure, the 2010 reform package aims to normalize the emergency increase of IMF resources that occurred in 2009. As noted earlier, the IMF is designed to work as a cooperative in which every member country contributes its designated shares – or their quota. The 2009 increase in IMF resources was agreed to under exigent circumstances, when there was little time for a protracted debate about quotas and voting shares, which is highly technical and politically sensitive particularly to those countries losing their voting shares. Instead, many IMF member countries, including the U.S., in 2009 boosted the resources of the institution by contributing to a special financial account called the New Arrangements to Borrow (NAB) that historically had been relatively small and created for emergency liquidity purposes. This infusion made the NAB larger than quota resources.

The 2010 quota reform package would transfer a large portion of those NAB resources into quota resources. The effect is to shrink the NAB resources but double the IMF's quota, which allows for the reallocation of voting shares mentioned above and to return the IMF – in essence – back to regular order.

For the United States, the 2010 package does not require the U.S. to increase its total contribution to the IMF. Rather, it requires us to increase our quota resources but reduce our NAB contribution by an equal amount. This reallocation from NAB to quota requires authorization from Congress as well as appropriations because NAB resources were provided under emergency legislation but quota resources are not, which leads to a different budget scoring.

As this committee is well aware, every major country has ratified the quota reform package except the U.S. Due to our voting shares being greater than 15 percent, the U.S. has a veto for some of the changes that have been negotiated in this package.

U.S. Interests

There are many economic and financial reasons for the United States to support the IMF. Global financial stability, a core objective of the IMF, is important to U.S. economic growth, exports, and job creation. Secondly, the IMF is a bargain for U.S. taxpayers. The U.S. leverages its resources many-fold with the contributions of the other 187 member countries. Without the IMF, were a financial crisis to occur, the U.S. and other wealthy nations would most likely end up shouldering the burden directly at a much higher cost, with more concentrated repayment risks. Thirdly, the IMF's mission of open markets and sound economic policies to strengthen economic and financial stability is in line with our international ideals and vision.

Maybe just as importantly, the IMF is a key foreign policy tool that the U.S. has called upon many times.

- In the 1980s, the IMF played a key role in advising Latin American countries' to reform their economies as well as providing financing to complement the efforts of President Reagan and President Bush to develop the Baker and Brady plans that finally ended the Latin America debt crisis.

- In the 1990s, the IMF provided significant financing to South Korea – a country where many of our troops are stationed -- during the Asian economic crisis at a time when Korea's economy was on the verge of collapse.

- In the 2000s, the IMF played a leading role in providing finance to Pakistan after 9/11, when that country came under incredible financial pressure. In addition, the IMF worked in Iraq and Afghanistan to provide technical advice and financial support throughout the decade. In fact, in the past two weeks, the IMF is working on a financing program to help Iraq stabilize its finances in the face of the growing threat of ISIS and falling oil prices.

- In just the last year, we have seen the IMF provide large sums of money to support Ukraine soon after the country was invaded by Russia. However, the IMF's support is not free. Despite the urgency of the situation, the IMF worked with Ukraine to design reforms that could place the country in a more secure financial position.

On a more personal note, in 2008, I recall speaking for a few hours on the phone with the prime minister of Georgia when Russia invaded that country. He was worried that the loss of confidence would create a bank run and was urgently looking for liquidity support from the U.S. to boost central bank reserves. The U.S. was very supportive of Georgia during that time, but we were in the midst of our own financial crisis and providing emergency liquidity support to another country is difficult for the U.S. to do even during stable times. Instead, we worked with the IMF which stepped up very quickly to provide the financing Georgia needed to preserve confidence in the banking system.

It should be of no surprise to this committee that every Secretary of Treasury going back to the Carter Administration and former Federal Reserve Chairs have supported the IMF quota reform package. And it is probably no surprise that almost every U.S. Trade Representative going back to the Reagan Administration has supported this package given the role that the IMF plays in fostering open trade and investment.

However, what may surprise you is that most Secretaries of Defense, Secretaries of State, and National Security Advisors to Presidents Nixon, Carter, Reagan, Bush, Clinton, Bush, and Obama have also supported this legislative request of the Administration. They recognize that the IMF is an important tool to conduct strong foreign policy and to provide the conditions that assist in keeping our troops out of harm's way. They recognize that U.S. leadership in the IMF is not only vital to the institution, but also important for our own national security interests.

The IMF is far from perfect and will continue to need U.S. leadership to reform and evolve. I know that John Taylor and Meg Lundsager have ideas about this, and I look forward to discussing them. However, U.S. leadership cannot occur from the sidelines; it must come in the form of strong legislation that can certainly have conditions.

Therefore, I ask that Congress work with the Administration and join what I believe is a strong bipartisan consensus and demonstrate this leadership.

Thank you and I'm happy to field any questions.

The Impact of the IMF: Economic Stability or Moral Hazard?

Testimony before the

Subcommittee on Monetary Policy and Trade

Committee on Financial Services

House of Representatives

June 17, 2015

Meg Lundsager

Public Policy Fellow

Woodrow Wilson International Center for Scholars

Thank you Chairman Huizenga and Ranking Member Moore for inviting me to testify today on the International Monetary Fund (IMF). During my 14 years at the IMF I represented three Administrations, nominated first by President Clinton and subsequently by President Bush. I continued serving as United States Executive Director representing President Obama until last year. I am currently a Public Policy Fellow at the Woodrow Wilson Center. My testimony today reflects my personal views, not those of the Wilson Center.

During my years at the IMF the global economy generated strong growth up until the global financial crisis erupted several years ago. The United States led the recovery from that crisis by taking forceful monetary and fiscal policy actions to stop the downward spiral in the United States and by advocating actions in the IMF supporting multilateral financing and adjustment programs in a number of crisis countries.

The International Monetary Fund was instrumental in helping many countries to return to economic stability and financial viability, thereby restoring access to private sector financing. The IMF's mission is to help countries with financing needs, and the IMF did this by designing policy adjustment programs and pooling financing from across its member countries. Thus the United States did not carry the full burden of providing financial support; instead almost 80% of financing came from other countries around the world. While the IMF was leading crisis resolution efforts in Europe and the Middle East, it also continued its important support for low income countries.

US leadership was crucial in bringing together all the elements needed for the IMF's international response. But that leadership is eroding as the United States loses status and influence due to US delays in approving the IMF quota and governance reforms agreed to in 2010.

IMF Quota and Governance Reform is in the US National Interest

The United States remains the largest economy in the world and has the largest single country vote in the International Monetary Fund, which gives the United States veto power over key decisions such as amending the IMF Articles of Agreement and increasing overall IMF financial resources.

Voting power at the IMF generally rests on a country's economic weight, yet current shares do not reflect the more rapid growth of many emerging market and developing countries. As a result, Belgium still has a larger quota share and vote than South Korea, Mexico, or Turkey.

The United States recognized this distribution of voting power was outdated and threatened to undermine the global legitimacy of the IMF. Beginning in 2006 the US Treasury Department proposed initial steps to realign quotas. IMF members reached a broader agreement in 2010 that would further change the distribution of voting shares to reflect the growth of dynamic emerging markets and developing countries. Since then progress has stalled as the world awaits US ratification.

In the meantime, the rest of the world is moving ahead with new regional and specialized financial institutions. Brazil, Russia, India, China and South Africa (BRICS) are forming a development bank, and now China is leading the formation of the Asian Infrastructure Investment Bank (AIIB), with many US allies already participating. The BRICS have also formed a Contingent Reserve Arrangement as a mutual balance of payments backstop.

US Role at the IMF

Today's hearing presents an opportunity to clarify many of the elements of the 2010 IMF quota and governance reform package.

First, the US share will remain comfortably above the 15% veto threshold. In fact, this 2010 agreement includes no change in the US financial commitment to the IMF. The increase in the US quota, or share, will be financed by an equal reduction in the US participation in the New Arrangements to Borrow (NAB), a line of credit the US and many others have provided the IMF. Importantly, this reform will reduce the overall share and voting power of Europe, while increasing that of dynamic emerging markets and sustaining the voting power of the poorest countries.

The US priority should be to recognize the rapid growth and development of the emerging markets. This would keep global economic policy-making centered in the International Monetary Fund, where the United States plays a leading role in setting standards of behavior and guidelines for international lending. With emerging markets generating larger shares of global growth, their contribution to and their stake in the multilateral system should be acknowledged. Approving the IMF reforms would demonstrate that and would help sustain emerging markets' commitment to this system.

Furthermore, countries that will benefit from higher quota shares include key allies of the United States such as Mexico, South Korea, Poland, and the Baltic nations – all countries supporting and demonstrating the benefits of economic reform and sharing US views on political and economic freedoms.

Second, some view the IMF view as an instrument of Europe and claim the IMF should not have rescued Eurozone countries. But without the IMF as the crisis manager in Europe, we risked the dissolution of the Eurozone as a growing crisis erupted in several Eurozone countries in 2010. If the Eurozone had fallen apart, the US dollar would have risen sharply on global markets as investors fled a disintegrating European currency union and sought the US safe haven, with negative effects on our economy. Our exports such as capital goods and our import competing industries such as autos would have felt the most direct effects. A collapsing Eurozone would have increased the risk of European bank failures, which would have affected US financial institutions and corporations as well as stock and bond markets. The US economic recovery would have been undercut.

Did the IMF ability to lend large amounts incentivize Eurozone countries to mismanage their finances and slide into crisis? That hardly seems likely, as evidenced by the very demanding policy adjustment programs that were put in place. Clearly, countries avoid turning to the IMF until no other option remains. And while some investors might seek high returns in higher risk countries thinking that IMF lending will finance their exit, those illusions should be dissipating as some countries resort to capital controls and others turn to debt restructurings.

What is clear is that IMF participation in these adjustment programs helped prevent a downward spiral. The European Union had not yet built its own defenses for Eurozone countries and thus could not quickly mobilize the financing needed to restore confidence and stabilize financial markets. Since then, Europe has made progress building its own firewalls and actions of the ECB have helped reduce these risks. But as current EU uncertainties show, significant challenges remain and longer-term solutions are needed. And as all countries remain entitled to turn to the IMF for assistance, IMF engagement in Europe, in one form or another, will likely continue. This spares the United States from making bilateral financial commitments to support key allies in Europe.

Third, over the many decades of the IMF's existence, US leadership has persuaded others to join in promoting reforms. The United States has been a leading voice for accountability, transparency, and change at both the institution itself and within member countries. US initiatives at the IMF have led to much more openness in government accounts, sounder financial institutions as countries improved regulatory oversight, reductions in the financing channels for money launderers and terrorists, and improved economic growth and stability in low income countries.

Important US national security priorities were supported by IMF lending programs and technical assistance for Iraq, Afghanistan, Tunisia, and Jordan. More recently the IMF responded to US calls to increase support for the Ebola-affected countries in Western Africa and to underpin the economic reforms in Ukraine with vital financing in the face of internal conflict and Russian economic pressure.

Sadly, US leadership continues to erode as the United States delays approval of the 2010 reforms. In my last months at the IMF it became increasingly clear that other countries had little enthusiasm for US proposals, such as extending the zero percent interest on low income country loans. And privately many of my IMF counterparts lamented a weakened United States, recognizing that over the years our many ideas had helped promote global growth and economic development.

How IMF Reforms are Adopted

It would be useful to explain how the IMF adopts new policies for its operations, whether to engage in more intensive examination of financial regulatory policies or to change how it imposes conditionality on its lending. Most IMF decisions, such as its conditions for lending or the focus of country macroeconomic analysis (surveillance), are taken by simple majority voting. The United States' voting power of between 16-17% of course helps in starting to build a supportive coalition. But the US needs much broader support to achieve success. That meant I would visit the 23 other Executive Directors to make the case for US proposals and to persuade my counterparts of the benefits to their countries of expanded IMF work on anti-money laundering and countering the financing of terrorism, or the merits of more rapid public release of IMF documents. Important IMF initiatives to support low income countries required the approval of many other countries, as they had to agree to the financing mechanisms. In the last year or so of my tenure, this became increasingly difficult, as my IMF counterparts would each cite their frustration with US delays in ratifying the 2010 reforms and remain noncommittal on my request.

Remaining Misconceptions

Some commentators claim the United States will lose its chair on the Executive Board if all Executive Directors are elected (currently the countries with the five largest quotas appoint their Executive Director (ED)). That is incorrect; the United States will *not* lose its seat on the Executive Board when all EDs are elected. The rules for ED elections are set by an 85% vote of the IMF membership; I am sure the US Governor for the IMF, the Treasury Secretary, would veto any rules that would prevent a US seat at the table.

Others express dismay at China's growing voting power. China does receive the largest share increase of any country with its voting share increasing from about 4% to 6%, yet its voting power will remain below its share of the global economy, as will India's. China will retain its single country chair, as will Russia and Saudi Arabia, but

Russia's voting share, once these reforms are enacted, will remain lower than it was before 2006. In comparison, the US voting share under these reforms will be about 16.5%, comfortably above the veto threshold.

IMF lending terms have been described as too generous, too long term, but that perception is outdated. As a result of reforms put in place in 2000, the IMF levies surcharges on its larger loans. Thus, the interest rates on these loans are much higher than market rates for countries in normal situations. This generates the incentive for countries to repay as quickly as possible, once their market borrowing rates have returned to more normal levels. Many countries have repaid early, including Ireland, Latvia, Iceland, Bulgaria, Philippines, Uruguay, Indonesia and Argentina. Historically countries have repaid the IMF before any other creditor. This policy has strengthened the revolving nature of IMF lending, enabling the IMF to meet future country needs.

Worries about the strength of the IMF balance sheet are also unwarranted. The IMF has a very strong balance sheet due to its own reserves and its gold holdings. To reassure all its members that the IMF is a sound institution it has built up its own reserves, now above $16 billion. In addition, the IMF holds over 90 million ounces of gold, with an unrealized market value of over $100 billion. This far exceeds the current outstanding lending of the IMF, about $75 billion, indicating that the IMF's overall financial health and therefore the US position in the IMF are well protected.

Financing Issues

The IMF currently has a backstop of numerous bilateral loan agreements with a subset of members. This does not include the United States; US commitments continue to be through the quota subscription and the NAB. The United States has veto power over NAB activation every six months (individual country programs have always been approved by a simple majority vote of the Executive Board). Other groupings of countries also have veto power over NAB activation, leaving the lingering concern that if the United States does not ratify the reforms strengthening the IMF's core capital, the IMF will continue to seek bilateral loans, negotiated with less transparency and without US involvement. Decisions on IMF financing should be made around the table with all IMF members represented.

In conclusion, I am honored to have represented the United States during three Administrations at a critically important global institution that has provided many benefits to our country and the global economy. The United States' commitment to this vital institution over the years has underpinned the US leadership role, going far beyond holding veto power over a few key decisions. Approval of the 2010 reforms would restore and sustain that leadership role.

Thank you.

IMF Reforms and Global Economic Stability

John B. Taylor[1]

Testimony before the Subcommittee on Monetary Policy and Trade
Committee on Financial Services
U.S. House of Representatives

June 17, 2015

Chair Huizenga, Ranking Member Moore, and members of the Subcommittee on Monetary Policy and Trade thank you for inviting me to testify at this hearing on "The Impact of the IMF: Economic Stability or Moral Hazard?"

For the International Monetary Fund—or any other international financial institution—to achieve the goal of promoting economic stability, it is essential that it have a clear and predictable framework or strategy for carrying out the goal. Without such a framework decisions become highly uncertain—influenced more by politics than economics—and create perverse incentives, including moral hazard, leading to excessive risk-taking and harmful international spillovers. For institutions like the IMF that can lend exceptionally large amounts supported by taxpayer funds, such a framework is essential for transparency, accountability, and preventing public bailouts of the private sector.

The IMF's Exceptional Access Framework

A dozen years ago such a framework—called the Exceptional Access Framework—was adopted at the IMF as part of a general reform that included the greater use of collective action clauses in sovereign debt. The aim was to improve global economic stability by ending, or at least reducing the likelihood of, the financial crises that had been raging in emerging markets. International monetary and financial policy needed more predictability, more accountability, and more systematic behavior on the part of the official sector. More focus needed to be placed on what public sector actions were likely to be in a given circumstance, on what accountability there would be for those actions, and on what the strategy and the principles behind the actions were.

The exceptional access framework moved in this direction by setting forth criteria that had to be met before the IMF could lend exceptionally large amounts to countries. The criteria included evidence of exceptional pressure on the country's capital account, good prospects that the IMF loans would be temporary, and a strong implementable economic program. Most

[1] Mary and Robert Raymond Professor of Economics at Stanford University, George P. Shultz Senior Fellow in Economics at Stanford's Hoover Institution, and former Under Secretary of Treasury for International Affairs, 2001-2005.

important was the criterion saying that the IMF could not make new loans to countries with unsustainable debts.[2]

The expectation was that limiting loans in this way would reduce bailouts of private sector creditors, contain moral hazard, lower uncertainty, reduce the recipient country's debt burden, encourage more responsible fiscal and monetary policy, reduce spillovers, improve accountability, and thereby create more economic stability. And, in fact, the 2003 framework was accompanied by many such changes. Compared with the 1980s and 1990s there were few crises emanating from emerging markets in the years that followed, and the emerging market countries as a whole weathered the global financial crisis remarkably well. Economic policy in emerging market countries generally improved: Monetary policy focused more on price stability, and fiscal policy relied less on foreign borrowing or debt linked to foreign currencies. So the framework worked well, as long as it was in place.

The Need to Reform the Exceptional Access Framework

Unfortunately, this exceptional access framework has not remained in place. It was abandoned in 2010 when the Greek sovereign-debt crisis emerged and the IMF staff could not establish that the Greek debt was sustainable with high probability. Rather than follow the "no loans to a country with unsustainable debt" rule, the IMF simply changed the rule. It wrote in an exemption saying that new loans could be made in unsustainable or uncertain situations after all so long as there was a "high risk of international systemic spillover." The IMF then claimed, with very little evidence, that spillover risk was high and approved an exceptionally large loan to Greece.[3] The loan was made without any debt restructuring.

As is well known, events in Greece following this 2010 decision have not been pleasant. The Greek economy continued to deteriorate under the burden of the large debt. By February 2012 it was clear to all that a restructuring was essential and Greek debt was written down by 60%. Acrimonious debate over the debt continues today with Greece falling behind in debt service payments to the IMF. By now most of the private sector creditors have gotten out with the IMF and European governments left holding much of the Greek public debt.

The fact that the original framework was broken at the same meeting that the Greek loan was approved provides strong evidence that the framework was broken to allow for the loan.

---

[2] Specifically, the original criteria were: Criterion 1: The member is experiencing exceptional balance of payments pressures on the capital account resulting in a need for Fund financing that cannot be met within the normal limits. Criterion 2: A rigorous and systematic analysis indicates that there is a high probability that debt will remain sustainable. Criterion 3: The member has good prospects of regaining access to private capital markets within the time Fund resources would be outstanding, so that the Fund's financing would provide a bridge. Criterion 4: The policy program of the member country provides a reasonably strong prospect of success, based in part on an assessment of the government's institutional and political capacity to implement that program." (See, International Monetary Fund (2002, 2003).)

[3] International Monetary Fund (2010)

Nevertheless, the exemption for systemic risk remains.[4] And because systemic risk is often "in the eye of the beholder," loan decisions are again largely discretionary.

Reforming the Exceptional Access Framework

For these reasons, it is time to reform (actually re-reform) and strengthen the exceptional access framework. A starting place would be simply to repeal the exemption for systemic risk which has causes much of the problem and may have had the unintended consequence of increasing systemic risk.

I have found much support for such a reform in the international community including among IMF management and staff. Some worry about the loss of discretion that eliminating the exemption risk of systemic spillovers would imply. But that very discretion causes uncertainty and the resulting spillovers. Moreover, the expectation that a workout would be more orderly with the collective action clauses—especially now that they have usefully been expanded to aggregate across different debt issues—reduces the chance of systemic spillovers. The exemption is the problem not the solution.

The International Agreement on Voting Reallocation and Quota Increases

Congressional approval of the international agreement (negotiated at a 2010 G-20 meeting) on IMF voting reallocation and quota increases is closely related to exceptional access reform.

This previously-negotiated international agreement would sensibly reallocate voting shares to give more votes to countries that have grown more rapidly (mainly emerging market and developing countries) and fewer votes to countries that have grown more slowly in the past few decades. The United States would lose a bit, but would remain above 17% and thus sufficiently high to be able to block major policy actions that require 85% of the membership.

The agreement would also increase the total value of the quota commitment to the IMF, the central source of funds for IMF lending. The main rationale for the increase is that the global

[4] More specifically, the original Criterion 2 (listed in footnote 2) has been changed to read as follows: "Criterion 2: A rigorous and systematic analysis indicates that there is a high probability that the member's public debt is sustainable in the medium term. However, in instances where there are significant uncertainties that make it difficult to state categorically that there is a high probability that the debt is sustainable over this period, exceptional access would be justified if there is a high risk of international systemic spillovers. Debt sustainability for these purposes will be evaluated on a forward-looking basis and may take into account, inter alia, the intended restructuring of debt to restore sustainability. This criterion applies only to public (domestic and external) debt. However, the analysis of such public debt sustainability will incorporate any potential contingent liabilities of the government, including those potentially arising from private external indebtedness." (See International Monetary Fund (2014)).

economy, international financial markets, and capital flows have expanded. It is important to note that the total amount of credit outstanding by the fund during the global financial crisis, including the exceptionally large loans to Eurozone countries, is far below what available resources would be with the international agreement.

For the United States the quota increase would be by about $63 billion (depending on exchange rate changes). It would be matched dollar for dollar by a reduction in the U.S. contribution to the New Arrangements to Borrow (NAB), another source of funds which was increased by $100 billion in 2009. Thus, after this partial offset about $37 billion of U.S. funding would remain in the NAB. At the time of the Congressional approval of $100 billion NAB increase in 2009, many in Congress viewed the increase as temporary, lasting only 5 years, and thus they question the concept of a partial offset. In reality the NAB can evidently be renewed without action by Congress.

Moreover, the increase in the quota must be scored by the Congressional Budget Office. Thus, approval of the agreement has direct implications for the federal budget which depend on how the Federal Credit Reform Act is applied and may need offsets elsewhere in the budget.

Legislation That Ties the Reforms Together

Given these budget implications, it is appropriate for legislation to tie approval of the international quota and voting shares agreement to exceptional access reform, and thereby provide a degree of accountability and transparency. It is both politically responsible and economically attractive to provide safeguards on how the appropriated funds are used.

Some may complain that it is not the role of the United States to insist on such reforms, but in my experience as an international finance official it is not unusual for the United States to lead on these issues.[5] In fact, many expect the United States to be a leader. The United States, working with key emerging market and developed countries, was a major force behind the enabling collective action clauses and the exceptional access framework in the first place.

Others may worry that any reinstated framework would be broken again. Indeed, some may view the whole issue cynically, perhaps saying that if exceptional access reform is all we need to get the quota increased, then let's do it and reverse the decision later if need be. This fragility is a concern, but the fact that the Congress would tie the exceptional access framework to the quota increase would make the framework more visible and therefore harder to break. In addition, in order to give greater public awareness and accountability regarding the criteria, the Secretary of the Treasury could be required to submit an exceptional access report to the relevant Congressional Committees in cases of exceptional access lending. There could also be additional requirements on the ability of the Congress to vote on renewals of the NAB.

[5] Taylor (2007)

Conclusion

In this testimony I have argued that in order to achieve the goal of economic stability, the IMF should have a clear strategy for achieving the goal; this is also true for the other international financial institutions and for the international financial system as a whole. I have showed how an effective exceptional access framework provides such a strategy for IMF lending decisions, and that a reform of the current framework is needed. Legislation to approve the international agreement to reallocate votes and increase quotas should be tied to the reform.

With the global financial system in an uncertain state of flux, now is a good time for such a reform. As Paul Volker (2014) has emphasized, recalling "memories of a more orderly rules-based world," the international financial system is in need of reforms that "can better reconcile reasonably free and open markets with independent national policies, maintaining in the process the stability in markets and economies that is in the common interest." Approving the international quota agreement in a way that helps ensure that new resources are used strategically, effectively and with accountability—as I showed in this testimony—would be an important pillar of any such a reform movement.

References

International Monetary Fund (2002), "Summing Up by the Acting Chair: Access Policy in Capital Account Crises," Executive Board Meeting 02/94. BUFF/02/159, Sept 20, 2002.

International Monetary Fund (2003), "The Acting Chair's Summing Up: Review of Access Policy Under the Credit Tranches and the Extended Fund Facility, and Access Policy in Capital Account Crises—Modifications to the Supplemental Reserve Facility and Follow-Up Issues Related to Exceptional Access Policy," Executive Board Meeting 03/16, BUFF/03/28, February 26, 2003.

International Monetary Fund (2010), "Greece: Staff Report on Request for Stand-By Arrangement," IMF Country Report No. 10/110, May 5, 2010.

International Monetary Fund (2014), "The Fund's Lending Framework and Sovereign Debt—Preliminary Considerations," Staff Report, June 2014

Schadler, Susan (2013), "Unsustainable Debt and the Political Economy of Lending: Constraining the IMF's Role in Sovereign Debt Crises," Center for International Governance Innovation, CIGI Papers No. 19, October

Volcker, Paul (2014), "A New Breton Woods???" Remarks at the Bretton Woods Committee Annual Meeting, June 17

Taylor, John B. (2007), *Global Financial Warriors: The Untold Story of International Finance in the Post 9/11 World*, W.W. Norton, New York.

○