



IMF POLICY PAPER

REVIEW OF THE FUND'S POLICY ON MULTIPLE CURRENCY PRACTICES—PROPOSALS FOR REFORM

July 2022

IMF staff regularly produces papers proposing new IMF policies, exploring options for reform, or reviewing existing IMF policies and operations. The following documents have been released and are included in this package:

- The **Staff Report**, prepared by IMF staff and completed on June 2, 2022 for the Executive Board's consideration on July 1, 2022.

The IMF's transparency policy allows for the deletion of market-sensitive information and premature disclosure of the authorities' policy intentions in published staff reports and other documents.

Electronic copies of IMF Policy Papers
are available to the public from
<http://www.imf.org/external/pp/ppindex.aspx>

International Monetary Fund
Washington, D.C.



July 1, 2022

REVIEW OF THE FUND'S POLICY ON MULTIPLE CURRENCY PRACTICES—PROPOSALS FOR REFORM

EXECUTIVE SUMMARY

In February 2019, the Executive Board considered staff's preliminary proposals for reforming the IMF's policy on multiple currency practices (MCPs) and supported the majority of the proposals. The Board expressed strong support for re-focusing the policy on official action that segments foreign exchange markets, eliminating the concept of potentiality, and replacing the current fixed two-percent rule for identifying MCPs for spot transactions with a country-specific market-based norm and tolerance margin that would apply uniformly across the membership for both spot and non-spot transactions. The Board also supported staff's proposals regarding the other elements of the new methodology to identify MCPs, the treatment of illegal parallel markets, excluding broken cross-rates from the scope of the policy, and the linkages with the Institutional View on the Liberalization and Management of Capital Flows.

Directors asked staff to prepare a follow-up paper, building on guidance received from the Executive Board, that would propose a decision to establish a new MCP policy. The Board agreed with the general direction of the review and most of the proposals, but requested further analysis in three main areas: the approval of MCPs maintained primarily for non-BOP reasons; addressing non-compliance; and ensuring a smooth transition. This paper responds to these requests and proposes a decision to reform the MCP policy. While the new policy does not introduce new or modify any existing obligations regarding data provision to the Fund, it aims to clarify data necessary for the implementation of the MCP policy.

Staff proposes to retain the possibility for the Board to approve MCPs maintained primarily for non-BOP reasons and to strengthen the existing approval criteria. In particular, it is proposed that temporary approval for non-BOP reasons would also require (i) a credible strategy for the removal of the measure and (ii) that the measure not constitute an exchange restriction. The additional conditions for approval should help guard against unwarranted use of MCPs for non-BOP reasons.

The paper outlines operational considerations to address noncompliance and to ensure a smooth transition. It is proposed to enhance the current cooperative approach to addressing noncompliance by increasing transparency and accountability. This would include more prominent and extensive coverage of MCPs in staff reports, with details to be outlined in the forthcoming guidance note, accompanied by annual reporting to the Board on all approved and unapproved MCPs. To ensure a smooth transition and avoid disruptions, it is proposed to delay the effective date of the new policy for nine months following approval, with some exceptions.

Approved By
**Tobias Adrian (MCM),
 Pierre-Olivier
 Gourinchas (RES),
 Ceyla Pazarbasioglu
 (SPR) and
 Rhoda Weeks-Brown
 (LEG)**

Prepared by a staff team from the Legal Department (LEG), Monetary and Capital Markets Department (MCM), and Strategy, Review and Policy Department (SPR), in collaboration with the Research Department (RES). The LEG team was led by Katharine Christopherson and Nadia Rendak, and comprised Chanda DeLong, and Jonathan Swanepoel. Under the overall guidance of Christopher Erceg and Ratna Sahay, the MCM team was led by Annamaria Kokenyne, and comprised Apoorv Bhargava, Pornpinun Chantapacdepong, Ingibjoerg Gudbjartsdottir, Salim Darbar, Waesh Khodabocus, Svetlana Popova, Asad Qureshi, and Romain Veyrune. The RES team was led by Giovanni Dell’Ariccia and Jonathan D. Ostry and comprised Suman Basu, Swarnali Hannan, Callum Jones, and Tamon Asonuma. Under the overall guidance of Petya Koeva Brooks and Jeromin Zettelmeyer, the SPR team was led by Vitaliy Kramarenko, Niamh Sheridan, and Murtaza Syed, and comprised Shakill Hassan, Marco Rodriguez Waldo, Masashi Saito, and Silvia Sgherri.

CONTENTS

INTRODUCTION	4
ISSUES FOR FURTHER CONSIDERATION	7
A. Eliminating Approval of MCPs Maintained for non-BOP Reasons	7
B. Addressing Noncompliance	8
SUMMARY OF THE PROPOSED NEW MCP POLICY	10
A. Concept of Official Action	10
B. New Methodology: Identifying and Eliminating MCPs	16
C. Links with Capital Transactions and the Institutional View	20
D. Resource and Data Issues	21
TRANSITIONAL ARRANGEMENTS	23
A. Application of the New MCP Policy	23
B. Status of Existing and New MCP Findings	24
BOXES	
1. Summary of Proposals Discussed at February 2019 Board Meeting	5
2. Non-Deliverable Forwards and Agreements between Central Banks	15

FIGURE

1. Proposed Methodology: Illustrative Example _____17

TABLE

1. Comparison of Official Actions Considered Under the Current and Proposed Policies _____20

INTRODUCTION

1. In February 2019, the Executive Board considered staff’s preliminary proposals (“Initial Considerations”) for reforming the IMF’s policy on multiple currency practices (MCPs) and supported the majority of the proposals (Box 1).¹ The Fund’s MCP policy is a cornerstone of the Fund’s legal and policy framework for exchange rates. The obligation of member countries to refrain from engaging in MCPs is an original provision of the Articles of Agreement. However, the current policy is outdated, having not been reviewed since 1981. Since the last review, there have been significant changes in foreign exchange (FX) markets calling for a sweeping review of the policy. Additionally, the review aims to address operational issues that have arisen in the implementation of the policy. The overarching aim of the review is to make the policy and its application more relevant, that is, to adjust the policy so that it does not discourage good practices in FX markets and is aligned with the Fund’s other policies, while ensuring that it continues to address policy actions that are objectionable.

2. The Board expressed strong support for three key reform proposals (summarized in Box 1). Directors agreed that the core principle of the current MCP policy, i.e., that official actions should not cause unreasonable deviations in exchange rate spreads compared to normal costs and risks, remained appropriate. There was strong support to refocus the policy on official action that segments FX markets and to eliminate the practice of finding an MCP due to *potential* exchange rate spreads, that is, an MCP should only arise if an official action results in an actual exchange rate spread exceeding the permissible margin. Directors also agreed with the *Initial Considerations’* proposal to update the methodology to replace the current fixed two-percent rule for identifying an MCP for spot transactions with a country-specific market-based norm and tolerance margin that would apply uniformly across the membership for both spot (including bank notes) and non-spot transactions. The Board also supported staff’s proposals regarding the other elements of the new methodology, the treatment of illegal parallel markets and broken cross-rates, and linkages with the Institutional View on the Liberalization and Management of Capital Flows (the “IV”).

3. The Board requested further analysis in three main areas. The Board was roughly equally divided on the proposal to eliminate the ability to approve MCPs maintained for reasons unrelated to the member’s balance of payments (“BOP”), with a number of Directors expressing concern that abolishing approval of MCPs maintained primarily for non-BOP reasons could create unnecessary constraints for member countries. In addition, while most Directors favored the current cooperative approach to addressing unapproved MCPs within the membership, some saw scope for enhancement, including through greater transparency. Finally, the Board requested staff to consider how best to ensure a smooth transition to the new policy, in a way that would provide adequate time for member countries to adjust their policies.

¹ See [Review of the Fund’s Policy on Multiple Currency Practices – Initial Considerations](#) (SM/18/208, 8/15/2019) (“Initial Considerations”) and its three supplements.

4. This paper responds to these requests, summarizes key elements of the revised MCP policy and proposes a decision to reform the MCP policy. The paper is organized as follows: Section I refines staff’s proposal regarding approval of MCPs maintained for non-BOP reasons and proposes an enhanced cooperative framework for addressing unapproved MCPs. Section II summarizes and further clarifies key elements of the revised policy, including the treatment of different forms of official action, the new methodology for identifying MCPs and data sources, the relationship with the IV, as well as resource implications. Section III proposes transitional arrangements. The paper concludes by presenting for the Board’s consideration the proposed decision for reforming the MCP policy.

5. Following the Board’s approval of a revised MCP policy, staff will prepare a detailed guidance note to assist implementation. The guidance note will be shared with the Executive Board for information and published. Staff will also conduct outreach on the new policy with member countries. Staff proposes a review of the new MCP policy within a period of five years, once sufficient experience with its application has been accumulated, with subsequent reviews to be conducted every five years or more, as needed.

Box 1. Summary of Proposals Discussed at February 2019 Board Meeting^{1/}

Directors expressed strong support for three key reform proposals: (i) adopting a clearer definition of official action; (ii) eliminating potentiality; and (iii) setting the permissible spread^{2/} according to a market-based norm that reflects country circumstances, with a fixed tolerance margin to avoid capturing minor deviations. Directors were divided on removing approval of MCPs maintained primarily for non-BOP reasons; and expressed no broad support for extending the MCP policy to capital transactions, or for introducing a formal remedial framework for unapproved MCPs.

Directors agreed that the focus of official action should be on actions by the authorities that segment the FX market, leading to differentiated exchange rates available only for select participants or transactions. Accordingly, certain practices currently captured by the MCP policy—illegal parallel markets, foreign exchange auctions that conform to best practice, and the use of official exchange rates based on market exchange rates of the previous day—should be excluded from the remit of the policy. A number of Directors stressed that removing illegal parallel markets from the MCP analysis should be complemented with reasonable efforts by country authorities to eliminate such markets, and a stronger emphasis on exchange restrictions in Fund surveillance. Directors also supported excluding from the scope of the policy broken cross rates, which have virtually disappeared.

Directors agreed to eliminate potentiality. MCPs can currently arise from official action that *could* lead to impermissible spreads. Directors endorsed the proposal to cease this practice: an MCP would only arise if official action results in an actual spread that exceeds the permissible margin.

Directors agreed to setting the permissible spread according to a country-specific market-based norm. A spread of more than 2 percent between buying and selling rates for spot transactions currently gives rise to an MCP. Directors agreed to replace this rule by a market-based norm (the range between the highest and the lowest exchange rates of the day in the wholesale market), with a tolerance margin of 2 percent to avoid capturing minor deviations. Directors supported the proposal to treat non-spot transactions in an analogous manner, noting the need for further refinement and guidance as experience is gained with application of the methodology to non-spot transactions.

Box 1. Summary of Proposals Discussed at February 2019 Board Meeting (Concluded)

The Board was divided on whether approval of MCPs maintained primarily for non-BOP reasons should be permitted.

About half of the Directors endorsed staff's proposal to remove the Fund's ability to temporarily approve MCPs maintained primarily for non-BOP reasons, to reflect that the Fund generally discourages using the FX system for purposes unrelated to the BOP and to more closely align the policies for approval of MCPs and exchange restrictions (the latter can only be approved if maintained for BOP reasons). Others, however, noted that removing the possibility to approve MCPs maintained for non-BOP reasons could introduce unnecessary constraints for the membership and preferred to maintain the flexibility under the current policy.

There was no broad support for extending the MCP policy to capital transactions. Most Directors maintained the view that they were not prepared to endorse the position that MCPs applying solely to capital transactions are subject to the Fund's jurisdiction under Article VIII, Section 3 and therefore subject to Fund approval.^{3/} They also saw merit in clarifying links of the MCP policy to the Institutional View on the Liberalization and Management of Capital Flows (IV), agreeing that where MCPs also constitute capital flow management measures, they should be assessed under the IV and if approved, would be considered appropriate under the IV for the approval period.^{4/} Some Directors were however open to considering the inclusion of MCPs applying solely to capital transactions within the scope of the Fund's jurisdiction under Article VIII, Section 3, noting the potential distortionary effects of such MCPs.

Most Directors cautioned against adopting a formal remedial framework for unapproved MCPs, favoring preserving the current cooperative approach. However, a few expressed concerns with the effectiveness of the existing cooperative approach in eliminating MCPs and were willing to consider a remedial framework for prolonged cases of MCPs.

Other issues. Directors supported (i) putting in place transitional arrangements to allow adequate time for member countries to adjust their policies, and (ii) periodic review of the policy henceforth. A number of Directors saw merit in reviewing the policy on exchange restrictions, in light of the proposed changes to the MCP policy; and some asked about the resource implications of the implementation of the reformed policy.

^{1/} See [The Acting Chair's Summing Up – Review of the Fund's Policy on Multiple Currency Practices – Initial Considerations](#) (SU/19/13, February 8, 2019).

^{2/} The terms "permissible spread" and "permissible margin" are used in this paper interchangeably.

^{3/} Transactions that are registered in the capital and financial accounts of the balance of payments, except for those considered "current" under the Fund's Articles of Agreement. As the Executive Board declined to assert jurisdiction over MCPs that apply solely to capital transactions, while staff identifies MCPs applicable to capital transactions in Article IV consultation reports, no finding of a breach of obligation is made and they are not subject to Fund approval. See the Chairman's Summing Up at the Conclusion of the Discussion on Multiple Currency Practices Applicable Solely to Capital Transactions, BUFF/85/34, February 25, 1985; and EBM/85/23, February 13, 1985.

^{4/} Staff's revised proposal on the links between the MCP policy and the Institutional View is set forth in paragraphs 31-32.

ISSUES FOR FURTHER CONSIDERATION

A. Eliminating Approval of MCPs Maintained for non-BOP Reasons

6. Under the current policy, MCPs can be temporarily approved for both BOP² and non-BOP reasons. The Fund may grant approval if MCPs are introduced or maintained for BOP reasons, are temporary and are being applied while the member is endeavoring to eliminate its balance of payments problem, and provided they do not give the member an unfair competitive advantage over other members or discriminate among members. Temporary approval may also be granted for MCPs that are maintained primarily for non-BOP reasons, if these MCPs do not materially impede the member's BOP adjustment, do not harm the interests of other members, and do not discriminate among members.³ Approval for MCPs is generally granted for one year, to allow regular review by the Executive Board normally in the context of Article IV consultations.

7. In *Initial Considerations*, staff proposed eliminating the possibility of temporary approval of MCPs for non-BOP reasons. This would be consistent with the Fund's long-standing view that using the FX system for purposes unrelated to the balance of payments should generally be discouraged. Moreover, allowing approval of MCPs maintained only for BOP reasons would bring the policy on approval of MCPs closer with that of exchange restrictions, which can only be approved if maintained for BOP reasons. However, Directors' support was roughly equally divided at the February 2019 Board meeting.

8. To address concerns expressed by Directors, staff considered further whether approval for non-BOP reasons should be retained. Historically, countries have maintained non-BOP based MCPs for two main purposes: raising revenue by taxing exchange transactions and achieving special resource allocation objectives. Like MCPs in general, such policies have had some short-term benefits, but have tended to hurt long-term growth, distort trade and resource allocation, and impose burden on businesses and consumers. Moreover, countries have faced difficulties in removing such MCPs, reflecting a lack of progress on domestic revenue mobilization and other fiscal reforms.⁴ In light of these concerns, the Board has exercised restraint in approving MCPs maintained for non-BOP reasons.⁵ In addition, more recently, MCPs have also occurred due to low levels of FX market development.⁶ While the reformed policy would exclude many measures that currently give rise to MCPs maintained for non-BOP reasons, it would not completely eliminate them. For example,

² MCPs maintained for BOP reasons relate to measures enacted in response to pressures on the BOP's current or capital and financial accounts that are leading to or could lead to disorderly market conditions and/or harmful domestic effects.

³ Paragraph 4 of Decision No. 6790-(81/43), as amended.

⁴ See *Initial Considerations*, [Supplement 2](#).

⁵ Among 120 MCP findings made between 2000 and end-2017, 30 MCPs were approved, of which 12 MCPs were approved for non-BOP reasons.

⁶ Among 45 cases of MCPs reported in the latest Article IV staff reports issued before end-2017, about half of the cases were maintained for non-BOP reasons, with more than 10 cases due to low levels of market development and about 5 cases for resource allocation.

a practice that determines the official exchange rate as the average of several previous days' market exchange rates given the specific FX market conditions would remain subject to the policy and might give rise to an MCP. If the Fund cannot temporarily approve such measures, they would always give rise to a breach by the member of its obligations under Article VIII, Section 3.

9. On balance, staff proposes to retain the possibility to approve MCPs maintained primarily for non-BOP reasons in limited circumstances.⁷ In particular, staff proposes that, while urging members to apply alternative policies not connected with the exchange system, the Fund would continue to be able to approve such measures if the existing criteria for temporary approval for non-BOP reasons are met and two additional conditions are satisfied, i.e., (i) the member commits to a credible strategy for the removal of the measure,⁸ and (ii) the MCP does not constitute an exchange restriction.⁹ The above two additional requirements as conditions for approval would help guard against unwarranted use of MCPs for non-BOP reasons. ***Proposed Decision, Paragraph 3(b).***

B. Addressing Noncompliance

10. In line with Directors' views expressed during the February 2019 meeting, staff proposes that the Fund continue its current cooperative approach to addressing noncompliance, with some enhancements. Staff concurs with most Directors that a remedial framework for unapproved MCPs is not necessary at this juncture, particularly given the substantial reform of the policy.¹⁰ Staff would instead propose that the Fund continue to urge members to eliminate unapproved MCPs, and to encourage policy reforms in members' exchange systems through surveillance and technical assistance, as well as via standard conditionality in Fund arrangements and instruments (which prohibits the introduction or modification of MCPs during a Fund-supported program), and, where warranted, specifically-tailored conditionality related to the elimination of MCPs.¹¹ Staff is of the view that a cooperative approach continues to be appropriate in helping countries eliminate unapproved MCPs, given that such reforms often require further development of the FX market and institutions that may take time. At the same time, the Board may

⁷ Staff does not propose any change to the criteria for approval of MCPs introduced or maintained primarily for BOP reasons as described in Paragraph 6.

⁸ Such a credible strategy would describe the policies and actions that the authorities intend to take and which can be reasonably expected to eliminate the MCP. While 'a credible strategy' for eliminating MCPs would not necessarily be time-bound, it should aim to support the elimination of MCPs within a reasonable period.

⁹ The overlap has not been a practical issue in recent years. None of the 12 MCPs that were approved for non-BOP reasons between 2000 and end-2017 were also exchange restrictions.

¹⁰ As discussed in *Initial Considerations*, [Supplement 1](#), while an unapproved MCP is a breach of a member's obligations under the Articles and could lead to the imposition of sanctions under Article XXVI, Section 2(a), so far the Fund has opted for a cooperative approach and has refrained from applying sanctions.

¹¹ All Fund arrangements (except for FCL and SLL arrangements) and non-financial monitoring instruments (PSI, PCI) currently include a standard continuous performance criterion (PC) (for arrangements), continuous assessment criterion (AC) (for PSIs), or continuous quantitative target (QT) (for PCIs) that prohibits the introduction or modification of MCPs.

always revisit the need for a more comprehensive remedial framework during subsequent reviews of the new MCP policy, if the proposed approach is deemed insufficient.

11. Nevertheless, there is scope to enhance the current cooperative approach to increase transparency and accountability. In particular, staff proposes the following additional steps. While information about MCPs is included in the Informational Annex to Article IV consultation reports, (occasionally, in UFR reports) and sometimes also in the main text of the report,¹² going forward, staff reports would cover identified MCPs more prominently and extensively. For both approved and unapproved MCPs, staff would be expected to report more consistently on the existence of such measures, including their actual or expected economic impact, as well as on the advice provided to the authorities on removal, and the authorities' plans regarding the measures.¹³ Moreover, where temporary approval of the MCP is requested by the member, the staff appraisal will continue to include staff's recommendation on approval or non-approval of the MCP. When a new MCP finding is made by staff, the views of the authorities on such finding should always be sought for inclusion in the Article IV consultation staff report even when the authorities accept the staff's finding, but especially when there is disagreement. Consistent implementation would be ensured through the interdepartmental review process. The forthcoming guidance note on the new policy would help countries better understand the scope and implications of the policy and would set forth requirements for coverage of MCPs in staff reports. In addition, a list of all approved and unapproved MCPs drawn from staff reports would be circulated to the Executive Board for information on an annual basis.

12. Compliance with the MCP policy and Article VIII, Section 3 would therefore be promoted through a broad range of tools, including: (i) more transparent coverage of MCPs in staff reports consistent with best practices to be identified in the forthcoming guidance note, (ii) urging members with unapproved MCPs to eliminate them, (iii) technical assistance on the elimination of MCPs and broader FX market reforms to countries that request such assistance, (iv) continued monitoring under Fund-supported programs of the standard continuous PC on the non-introduction and non-modification of MCPs, as well as specific conditionality directed towards the elimination of MCPs, where warranted, and raising awareness of countries about the standard

¹² When finding an MCP for the first time, staff must include in the staff appraisal its finding of the MCP and recommendation for approval or non-approval. The [Guidance Note for Surveillance under Article IV Consultations](#), provides guidance to country teams on the presentation of issues related to MCPs in the context of Article IV consultation reports.

¹³ Board Decision No. 6790-(81/43), adopted on March 20, 1981 (the "1981 Decision") provides: "To assist the Board in reaching a decision concerning approval or non-approval of a multiple currency practice subject to approval under Article VIII, Section 3, the reasons underlying the practice and its effects will be analyzed in reports on Art. IV consultations or in other staff papers dealing with exchange systems." This requirement, however, has not been consistently implemented. Further, BUFF/85/34 provides that Fund members should continue to provide the Fund with specific and full information on capital controls and multiple currency practices applicable solely to capital transactions, and a full assessment of such practices and an assessment of their economic consequences should continue to be provided, in the framework of the Fund's surveillance activities, by the staff in the Article IV consultation staff reports.

continuous performance criterion, and (v) an annual reporting to the Board on current MCPs and their approval status across the membership.

SUMMARY OF THE PROPOSED NEW MCP POLICY

Set out below is a summary of the key elements of the new MCP policy which are reflected in the proposed decision. This summary should be read in conjunction with “Initial Considerations” and its background papers. In particular, the proposed assessment of certain types of MCPs will be as set out in Supplement 3 to “Initial Considerations” with further elaboration provided in this paper. References to paragraphs in the Decision are included to guide the reader.

A. Concept of Official Action

13. In the context of the February 2019 discussion, Directors agreed that the scope of official action should be clarified to focus primarily on action that segments FX markets. In this regard, segmentation would be considered to exist where, official action, i.e., any action by the authorities,¹⁴ results in an exchange rate being available only for (i) a specific intermediary and/or end-user or a limited group of intermediaries and/or end-users and/or (ii) for a limited range of purposes. Official action will also continue to cover cases where the authorities’ actions directly increase or subsidize the cost of certain FX transactions in a manner that causes permissible spreads to be exceeded (e.g., an exchange tax or subsidy). In addition to such direct forms of official action, more subtle forms, such as informal guidance or moral suasion to influence the exchange rate will continue to be included in the concept. ***Proposed Decision, Paragraph 2(a).***

14. With the changes to the concept of official action, the concept of “potentiality” will be eliminated. Under the current policy, official action that has the potential to give rise to an impermissible spread results in an MCP. Under the new policy, an MCP would only arise if the official action actually gives rise to an impermissible spread, calculated as per the methodology set out below. Table 1 in Paragraph 30 summarizes the overlap between the existing and proposed policy.

Foreign Exchange Auctions

15. In light of the definition of official action under the new policy, multiple and single-price FX auctions would give rise to MCPs only if they segment the FX market. An auction that is not for earmarked purposes/specific end-users, would be considered not to segment the market if all of the following criteria are met:

¹⁴ “Authorities” in this context refers to a member or any of its fiscal agencies referred to in Article V, Section 1 of the Articles of Agreement. For a further discussion of official action, see *Initial Considerations*, in particular paragraphs 7 and 29.

- **Access** to bid at the auction is granted to all intermediaries in good standing,¹⁵ either directly or indirectly through market makers,¹⁶ in the country's wholesale FX market¹⁷ so that they can all sell or make purchases of FX for themselves and on behalf of their clients.
- **No constraints** are imposed on the range or level of the exchange rates that bidders can submit, as this may segment the auction from the rest of the FX market.
- **Allotment** at the auction is determined solely on the basis of the bid prices submitted by participants to buy or sell FX. Bids should be ranked according to their exchange rates, from the best to the worst rates from auctioneer point of view, and FX awarded to the bids according to their ranking starting with the best exchange rate up to the bid for which the cumulated amount of bids corresponds to the intended allotment.¹⁸

If an FX auction fails to meet the above criteria, an MCP would arise if the auction exchange rate exceeds the permissible margin per the below methodology (see Section B). **Proposed Decision, Paragraph 2(a).**

Use of Official Exchange Rates with One-Day Lagged Calculation

16. As agreed by Directors, an official exchange rate calculated on the basis of the preceding day's market rates will not give rise to an MCP. As explained in *Initial Considerations*, such practices are often implemented in countries with less developed FX markets, where the authorities cannot compute market exchange rates before the close of the FX market. In that regard, under the revised policy, official exchange rates computed using market exchange rates of the preceding business day will not give rise to an MCP, provided that they are computed based on the following specific criteria: (i) the lagged official exchange rate is calculated as a weighted average of transaction exchange rates in the wholesale FX market and, in the absence of a wholesale FX market, as the weighted average of the transaction exchange rates between intermediaries and their clients or a combination of the two if the wholesale FX market is not representative of the FX market; and (ii) the transactions included in the calculation occurred on the business day immediately preceding the day when the official exchange rate is to be used. **Proposed Decision, Paragraph 1.II.**

¹⁵ The concept of "good standing" covers intermediaries that are not suspended from participating in the FX auction or interventions due to non-compliance with any rule or regulations (e.g., prudential regulations or AML/CFT).

¹⁶ An institution is considered as a market-maker, by being either part of a formally established market-maker agreement or an active institution offering to buy, sell or quote tradable two-way competitive prices of comparable lot-size (standard amount) on a regular basis.

¹⁷ The wholesale FX market is the market in a country that includes central bank, commercial banks, FX dealers and other FX intermediaries.

¹⁸ The allotment rules are similar in both single- and multiple-priced auctions, the only difference is the exchange rate at which the amount is allocated.

Illegal Parallel Markets

17. As agreed by Directors, illegal parallel markets would be removed from the scope of the revised MCP policy but would continue to be captured under the Fund’s policy on exchange restrictions, where relevant.¹⁹ As noted in *Initial Considerations*, MCP findings arising from spreads in illegal parallel markets give rise to conceptual issues in application, as these markets are legally prohibited and as such, not a result of official action. In cases where the illegal parallel market arises from rationing, prioritization or other forms of official action that result in shortages of FX for current international transactions, any restrictions on the availability of FX for the making of payments and transfers for current international transactions would be expected to continue to be captured under the Fund’s exchange restrictions policy (Article VIII, Section 2(a)). However, Directors stressed that this be complemented by reasonable efforts by country authorities to eliminate such markets and a stronger emphasis on exchange restrictions in Fund surveillance. In that vein, staff will continue to be expected to discuss illegal parallel markets in staff reports for Article IV consultations (or UFR staff reports), identify exchange restrictions, if any, that give rise to them and their implications, and identify how the underlying policies or distortions that fuel these markets can be removed. Further guidance will be provided in the guidance note to staff on the new MCP policy.

Broken Cross-Rates

18. Broken cross-rates would not be considered MCPs under the revised MCP policy. Since reliance on such practices has almost disappeared, they are no longer economically relevant at this juncture. If such practices were to re-emerge, they could be brought under the MCP policy again.

Exchange Taxes, Other Mandatory Costs and Subsidies

19. The new policy will broadly provide continuity for the treatment of exchange taxes, and other costs and subsidies imposed by official action²⁰ However, their treatment under the new policy will differ depending on whether they are imposed on market exchange rates or exchange transactions where the exchange rate is determined by official action.

- As described in *Initial Considerations*, exchange taxes and other costs or subsidies imposed by official action on exchange transactions where the exchange rate is not determined by official action would be deemed to be levied on the midpoint of the range between the most appreciated and most depreciated wholesale exchange rates on a given day (H/L) and compared with the H/L of the same day and the 2 percent tolerance margin (whichever is wider).²¹ This implies that exchange taxes (and other costs or subsidies) that alone or in the aggregate, do not

¹⁹ As noted in paragraph 39 of *Initial Considerations*, parallel markets would be considered “illegal” if transactions conducted in such markets are prohibited under national law.

²⁰ The treatment of exchange taxes under the new policy as described in this paper will generally apply to other mandatory costs and subsidies closely related to exchange transactions and introduced by official action. See also Section II.A paragraph 24 and 26 *Initial Considerations, Supplement 3*. Taxes, other costs and subsidies imposed by official action, but which are not closely related to an exchange transaction do not fall within the MCP policy.

²¹ See the description of the new methodology identifying MCPs including the tolerance margin in Paragraphs 2.4-28.

exceed 2 percent would not be considered MCPs.²² Conversely, it would also imply that for those member countries with a H/L permanently wider than 2 percent, exchange taxes (or other costs or subsidies) may not give rise to an MCP even though they exceed 2 percent alone or in the aggregate.²³

- Where a tax, other cost or subsidy is imposed on an exchange transaction with an exchange rate arising from an official action (e.g., a rate determined by the authorities), an exchange tax as well as any other mandatory cost or subsidy imposed on the exchange transaction by official action will be considered part of the effective exchange rate²⁴ that will be compared to the permissible spread under the new methodology. As a result, in such cases, the mandatory cost, including an exchange tax, or subsidy less than 2 percent in itself or in aggregate could give rise to an MCP. Conversely, an exchange tax (and/or other mandatory costs or subsidy) of more than 2 percent, including in the aggregate, would not necessarily result in an MCP if the effective exchange rate remains within the H/L of the day.

Proposed Decision, Paragraphs 2.b. and 1.1.a.

20. This proposed approach reflects a range of considerations. First, it would allow the application of the new country-specific market-based methodology to exchange taxes and similar costs and subsidies.²⁵ Second, by not considering exchange taxes applied to exchange transactions where the exchange rate is not determined by official action to be MCPs if the rate of the tax is below 2 percent (assuming no other governmental costs or subsidies are imposed on exchange transactions), it would provide a degree of certainty to the treatment of exchange taxes that is important for fiscal policy making. Finally, this approach would allow, to the extent compatible with the new methodology, countries that have built the 2 percent concept into their exchange tax regimes to continue using this practice. Staff will closely monitor the implementation of the new policy with regard to exchange taxes, and other mandatory costs and subsidies, and be prepared to propose adjustments to this approach if necessary.

21. Exchange taxes and other mandatory costs that do not give rise to MCPs would also not give rise to exchange restrictions. Exchange taxes may currently also give rise to exchange restrictions.²⁶ Due to the current absence of a generally applicable *de minimis* rule for exchange

²² Historically, the MCP policy has allowed members to impose minor taxes (i.e., less than or equal to 2 percent) on exchange transactions without giving rise to an MCP, recognizing the limited impact of such taxes on world commerce. As such, this treatment would generally be maintained.

²³ Since the H/L may change over time, taxes higher than 2 percent could give rise to MCPs if the H/L becomes narrower than the 2 percent tolerance margin.

²⁴ As a continuation of the longstanding practice, an effective exchange rate includes not only the nominal exchange rate, but also any additional costs e.g., taxes or other mandatory costs, or subsidies that have been imposed by official action and are so closely related to the transaction that they should be considered as part of the effective exchange rate.

²⁵ As discussed in Box 4 of *Initial Considerations*, by applying the methodology to exchange taxes without an adjustment even negligible taxes could trigger MCP findings.

²⁶ See *Initial Considerations*, paragraphs 7, 23, Box 4.

restrictions, and for coherence between the two policies, it is proposed that exchange taxes and other costs that do not give rise to an MCP under the new methodology would not give rise to an exchange restriction.²⁷ **Proposed Decision, Paragraph 4.**

Foreign Exchange Transactions by the Authorities

22. Foreign exchange purchases and sales by the authorities (aside from auctions that are addressed above) that do not create market segmentation will be excluded from the scope of the policy. Such FX transactions (loosely referred to as “intervention”²⁸) typically involve the sale or purchase of foreign currency by the authorities to/from intermediaries at a particular rate or by accepting offers from them.²⁹ Such transactions will not give rise to an MCP as long as they: (a) are open to all intermediaries in good standing, either directly or indirectly through market makers; and (b) do not restrict the use of the foreign currency purchased by intermediaries for specific purposes/end-users.

23. However, such FX transactions conducted by the authorities in a manner that makes foreign currency available at a particular exchange rate only to or from selected wholesale intermediaries or for specific purposes/end-users (i.e., through the use of earmarked transactions) will be assessed under the policy. As such type of FX transactions results in a segmentation of the FX market, it would be considered official action under the revised policy. Exchange rates used in such FX transactions will be assessed according to the new methodology, and an MCP would arise if the transaction exchange rate is outside of the permissible margin. This approach is consistent with the Fund’s approach to FX intervention under the current MCP policy.

²⁷ As discussed above, there may be cases where the member-specific H/L is wider than the plus/minus 2 percent tolerance band. In such cases, exchange taxes and other mandatory costs and subsidies greater than 2 percent (alone or in aggregate) may not give rise to an MCP, and therefore, would not be considered to give rise to an exchange restriction.

²⁸ “Intervention” as used in this paper is without prejudice to any concept of intervention in any other Fund policies.

²⁹ FX transactions by the authorities may take place through FX auctions. In such cases, the provisions of the MCP policy on FX auctions would apply.

Box 2. Non-Deliverable Forwards and Agreements between Central Banks

Non-deliverable forwards (NDFs)

Staff propose that NDFs entered into by the authorities only be considered under the MCP policy if closely related to acquiring or selling foreign exchange. This proposed treatment reflects the long-standing principle of the MCP policy that for an MCP to exist, there needs to be an official action and an exchange transaction (i.e., an actual exchange of a member's currency for another member's currency). Since NDFs do not involve an actual exchange of a member's currency for another member's currency, they can be considered under the MCP policy only if they result from official action (e.g., entered into by central banks or other official entities, or by another party at their direction) and the NDFs are (i) made available only to a subset of intermediaries or end-users or are earmarked for specific transactions, therefore segmenting the market, and (ii) closely related to acquiring or selling foreign exchange.^{1/} All other NDFs would be excluded from the policy. If the NDF resulting from official action is sufficiently closely related to acquiring or selling foreign exchange, the additional cost or subsidy resulting from the NDF could be considered as part of the effective exchange rate (of the FX transactions to which the NDF is closely related) which will be assessed under the proposed methodology. This would be consistent with the principle that additional costs or subsidies related to an exchange transaction arising due to official action may give rise to an MCP.^{2/}

Agreements between Central Banks

Staff proposes to continue its current practice with respect to agreements between central banks. It has been the practice of the Fund to assess agreements between central banks that are structured as bilateral payments arrangements (BPAs) to determine whether they are consistent with members' obligations under Article VIII, Section 2(a) and 3 of the Articles of Agreement. Staff does not assess agreements between central banks that are not structured like BPAs (e.g., swaps for liquidity support or for reserve management purposes).^{3/4/} While continuing with the current approach, staff will monitor developments to determine whether further adjustments to this approach would be warranted in the context of subsequent reviews of the MCP policy. Instances where the funds from a CB swap are passed on through official action to domestic foreign exchange market intermediaries and end-users in a manner that causes market segmentation and exchange rate deviations in excess of the permissible spread are covered by the proposed new methodology.

^{1/} An assessment of whether these conditions are satisfied will be made based on all the relevant circumstances, similar to assessments of an effective exchange rate in other cases

^{2/} Staff acknowledge that the proposed approach will exclude from the MCP policy NDFs entered into by the authorities that are explicitly linked to the exchange rate but settled in local currency (unless they are sufficiently closely related to an exchange transaction) since they would not involve an actual exchange of a member's currency for another member's currency. Such NDFs are often used for intervention. That said, official intervention through NDFs can still be addressed as part of Article IV discussions of a members' exchange rate policies.

^{3/} The current approach has been to assess central bank agreements that include features found in official payments arrangements and official clearing arrangements. For example, an official payment or clearing arrangement would generally give rise to an MCP if it provides for the use of exchange rates that effectively are not the same as the rates that are used in the market. An official arrangement would also give rise to an exchange restriction if it provides for the settlement of balances between central banks (arising from current international transactions) less frequently than every three months. See *Review of Bilateral Payments Arrangements, 1976-81*, SM/82/169, 8/17/82; and *Official Clearing and Payments Arrangements: Temporary Exemption from the Three-Month Rule*, SM/94/188, 7/14/94. Provisions of central bank agreements that include similar features could therefore give rise to exchange restrictions and/or MCPs.

^{4/} Agreements between central banks which are structured as collateralized lending would not be considered under the policy. This reflects the long-standing principle of the MCP policy that it applies to the purchase and sale of FX. Lending, even if it is denominated in FX, is not a transaction for the purchase and sale of FX. Collateralized lending denotes a lending transaction that is secured by the provision of collateral to the lender.

B. New Methodology: Identifying and Eliminating MCPs³⁰

Spot Transactions³¹

24. As Directors agreed, under the new policy, MCPs will be assessed using a methodology that is more market based and country-specific than the current framework. As under the current policy, an MCP will arise when official action gives rise to exchange rate spreads that differ unreasonably from the normal commercial costs and risks of exchange transactions (i.e., the “commercial reasonableness” standard).³² In assessing whether the “commercial reasonableness” standard has been met, the new methodology provides that an MCP will arise where official action gives rise to an exchange rate for a spot exchange transaction that exceeds the permissible margin, which is defined by the following condition ***Proposed Decision Paragraph 1.I(a)***:

$$\text{Min} \{ \text{LOW}_t ; M_{(H/L)_t} - 2\% \} \leq R_t \leq \text{Max} \{ \text{HIGH}_t ; M_{(H/L)_t} + 2\% \}$$

where,

HIGH_t is the highest (i.e., the most depreciated) wholesale exchange rate,

LOW_t is the lowest (i.e., the most appreciated) wholesale exchange rate,

$M_{(H/L)_t} = \frac{\text{HIGH}_t + \text{LOW}_t}{2}$, is a mid-point of the High/Low range,

R_t is the exchange rate arising from official action, and

t is a given trading day.

25. The permissible spread will thus be determined by a country-specific market-based norm on a given trading day (the High/Low range), and a tolerance margin of +/- 2 percent around the mid-point of the High/Low range, whichever is wider.³³ This is illustrated in Figure 1. The purpose of the tolerance margin is to avoid capturing relatively minor deviations from the market-based norm.³⁴ For official action that imposes additional costs or subsidies on the spot

³⁰ The proposed operation of the new methodology is described in more detail in *Initial Considerations* paragraphs 50-53, and in [Supplement 3](#) to *Initial Considerations*. As noted in *Initial Considerations*, the new methodology requires, as a first step, the identification of an exchange rate arising from official action.

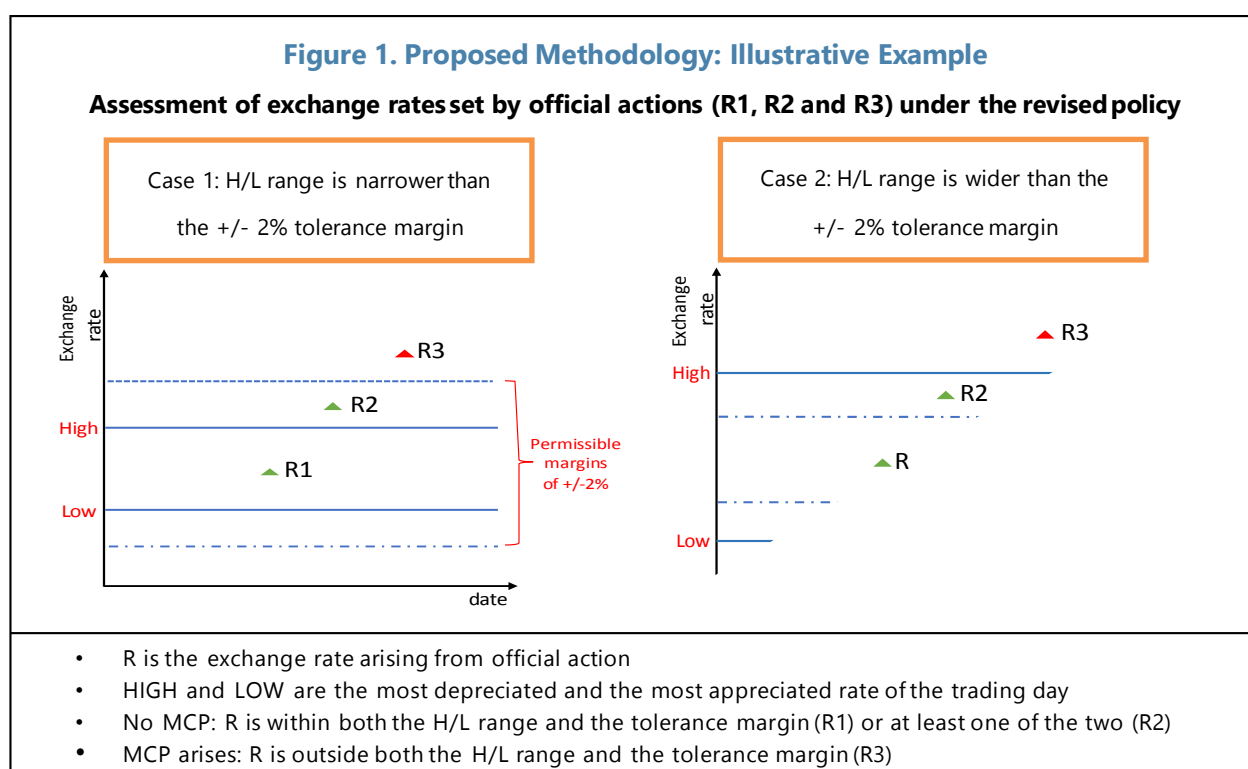
³¹ As per the global financial market standard for settlement dates, the two types of FX transactions are: (a) those that settle at or less than t+2 days (spot); and (b) those that settle at more than t+2 days (non-spot). The definition of spot transactions can be found in the Model Code of the Association Cambiste Internationale, which is the standard benchmark for global FX and OTC markets. (<https://acifma.com/Why-The-Model-Code>). Thus, banknote transactions are assessed as spot transactions as further described in *Initial Considerations* [Supplement 3](#).

³² As under the current policy, if an exchange rate arising from official action exceeds the spread permissible under the new policy, an MCP would arise regardless of whether such rate is actually used in exchange transactions. This would be the case, for example, if the authorities established an exchange rate that can be used infrequently for specific transactions or for a specific group of market participants.

³³ In countries with no separate legal tender, the permissible spread will be based on the wholesale market exchange rate in the country which is the issuer of the currency used as a legal tender of the country with no separate legal tender.

³⁴ The rationale behind the choice of +/- 2 percent as the tolerance margin is more fully described in paragraphs 51 and 52 of *Initial Considerations*.

exchange transactions (e.g., margin requirements, commissions, fees, taxes or subsidies prescribed by the authorities on certain FX transactions) that are sufficiently closely related to an exchange transaction, the effective exchange rate resulting from official action should be computed and used in the assessment.³⁵ In cases where such additional costs or subsidies are imposed by an official action on exchange transaction in which the exchange rate is not determined by official action, the effective exchange rate will be determined by applying such cost or subsidy to the midpoint of the range between the most appreciated and most depreciated wholesale exchange rates on a given day (H/L).^{36, 37} This rate will then be compared against the H/L and the tolerance margin, whichever is wider and if the rate falls outside of this range, an MCP will arise. In cases where such costs or subsidies are imposed on an exchange rate that arises from other official action (e.g., a rate determined by the authorities), the effective exchange rate will be calculated by applying such cost or subsidy to that exchange rate.



26. Market exchange rate data including the daily High/Low range will be primarily collected from reputable third-party providers. Staff consulted with Thomson Reuters and Bloomberg on the revised MCP policy and the proposed use of exchange rate data to assess MCPs.

³⁵ For a detailed discussion of the methodology to be used for spot transactions, see *Initial Considerations—Methodology to Assess Multiple Currency Practices*, [Supplement 3](#), pages 12-15.

³⁶ See Ft. 1 of Appendix III of *Initial Considerations*, Supplement 3.

³⁷ All mandatory costs or subsidies applicable to the same exchange transaction will be combined for purposes of calculating the effective exchange rate.

Staff's view is that these data are comprehensive and reliable.³⁸ In the context of the subsequent review of the MCP policy (expected in five years), staff would intend to confirm the continued comprehensiveness and reliability of such data, in light of experience.

Non-Spot Transactions

27. As Directors agreed, the methodology will also be applicable to the assessment of official action involving a non-spot exchange transaction.³⁹ Accordingly, under this approach, where the exchange rate for non-spot transaction exceeds the permissible margin, an MCP would arise. The assessment of non-spot transactions may become more frequent under the new policy, as FX markets evolve and become more sophisticated. The evaluation may require supplementary information and computations, depending on the type of FX products associated with the official action—e.g., forwards, swaps and options—and the availability of market data.⁴⁰ When market data are available for non-spot FX products, the exchange rate arising from official action is compared with the market exchange rates of the same type of non-spot FX product with the same maturity.⁴¹

Proposed Decision, Paragraph 1.I(b)

28. If market data are unavailable, the non-spot market exchange rate will be computed using a theoretical model, and the exchange rate determined by an official action will have to satisfy the following condition to avoid an MCP finding:⁴²

$$T_t - 2\% \leq R_t \leq T_t + 2\%$$

where

R is the exchange rate arising from official action settling at more than $t+2$

T is the exchange rate calculated using the theoretical model described in *Initial Considerations*, and

t is a given trading day.

³⁸ While there would be a strong presumption for using data from Thomson Reuters DataStream and Bloomberg in the methodology, if data from these sources are not available, or the data that are available appear to be manifestly irregular or inaccurate, staff can use other exchange rate data which are representative of the FX market. Alternative data sources that could be used by staff would include the following: (i) publicly available independent data source, (ii) publicly available data from the authorities, or (iii) other data from the authorities. In all these cases staff would determine whether the data are representative of the market.

³⁹ See Box 5 of *Initial Considerations*, as well as [Supplement 3](#) to *Initial Considerations*, for a fuller description of the application of the proposed methodology to non-spot transactions.

⁴⁰ For a typical swap transaction, the forward leg is evaluated as a forward exchange rate and the spot leg is assessed like a spot exchange rate. The assessment of official action involving non-spot transactions will take into account the terms of the contract at inception. Options will be assessed only if they are exercised; staff recognize that the availability of an option to hedge exchange rate risk, in itself provides a value to the beneficiaries, even if the option is not exercised.

⁴¹ For a detailed discussion of the methodology to be applied to specific non-spot Transactions, see *Initial Considerations—Methodology to Assess Multiple Currency Practices*, [Supplement 3](#), pages 15-19.

⁴² As described more fully in *Initial Considerations*, [Supplement 3](#), Bloomberg and Reuters provide flexible calculators for computing theoretical forward exchange rates and option prices. When using a theoretical model, staff may use alternative data from the domestic market if considered more representative of the funding rate than that used by the benchmark data providers for a given maturity.

Finding and Eliminating MCPs

29. As under the current policy, an MCP will arise from a single deviation outside of the permissible margin. Once found, the MCP will be reported in the next Article IV consultation or program review report.⁴³ The identified MCP could be eliminated in one of the following ways:⁴⁴

- The authorities could eliminate an MCP by eliminating the official action that gave rise to the MCP. Given that it may take time to remove the relevant measures, approval of the MCP could be granted during this time period.⁴⁵ As under the current policy, such approval would normally be granted for a period not exceeding 12 months but could be extended, if conditions for the continued approval are met.
- Rather than eliminating the official action that gave rise to the impermissible spread and to an MCP, the authorities may choose to keep it in place and take other credible measures to bring the spread back within the permissible margin and ensure that the official action will not, in the future, give rise to impermissible spreads. In these circumstances, the MCP will be considered eliminated. Staff will assess the credibility of such measures based on all available information and, in conducting the assessment, will give the member the benefit of any reasonable doubt. If the MCP re-emerges, a new finding would be made.
- Finally, an MCP would be considered eliminated without any action being taken by the authorities if the member demonstrates over a specified “observation period” after the emergence of the spread that an impermissible spread had not recurred. Staff propose an observation period of 12 months. The MCP would remain in place during the observation period and would be noted in Article IV or UFR staff reports. The re-emergence of an impermissible spread during this period would “reset the clock”, and the observation period would start again. This would allow the Fund to be satisfied that the relevant official action is no longer giving rise to impermissible spread before the MCP is considered eliminated. ***Proposed Decision, Paragraph 5.***

30. The revised policy is expected to result in fewer MCP findings. Since the revised policy will not consider FX auctions that conform to best practices, official exchange rates calculated with one day lag, and illegal parallel markets as official actions, the number of MCPs under the revised policy is expected to be smaller (see Table 1).

⁴³ As further described in *Initial Considerations*, [Supplement 1](#), MCP findings are made by the Executive Board.

⁴⁴ See *Initial Considerations*, Box 2.

⁴⁵ Approval will be granted based on the criteria established by the Executive Board. See Section I.A.

Broad Taxonomy	Official actions	Current MCP Policy	New MCP Policy^{1/}
Different Exchange Rates for Different Transactions	Different rates for different transactions, except interventions that do not segment the FX market	✓	✓
	One-day lagged official exchange rate	✓	✗
	Other lagged official exchange rates	✓	✓
	Bilateral payment agreements (BPA)	✓	✓
	Exchange rate guarantee schemes	✓	✓
Foreign Exchange Auctions	FX auction conforming to best practices	✓	✗
	Other FX auctions	✓	✓
Dual or Multiple FX Markets	Dual or multiple FX markets in a single jurisdiction	✓	✓
	Illegal parallel exchange markets	✓	✗
Measures that increase (decrease) the cost of FX transactions and are considered part of the "effective exchange rate"	Import deposit requirements (margin requirement), non-interest-bearing blocked accounts, and non-interest-bearing deposits	✓	✓
	Taxes, other costs less than or equal to 2% imposed on market rates	✗	✗
	Taxes, other costs less than or equal to 2% on exchange rates arising from official action	✗	✓
	Other taxes, costs and subsidies	✓	✓

^{1/}Note that the new MCP policy proposes a different methodology for MCP assessment.

C. Links with Capital Transactions and the Institutional View

31. In line with Board guidance during the February 2019 meeting, Fund approval will continue to be required only for MCPs that apply to current transactions. MCPs can apply to both current and capital transactions.⁴⁶ At the February 2019 Board meeting, most Directors

⁴⁶ Under Article XXX(d) of the Articles of Agreement, payments for current transactions mean payments which are not for the purpose of transferring capital, and include, without limitation: (1) all payments due in connection with foreign trade, other current business, including services, and normal short term banking and credit facilities; (2) payments due as interest on loans and as net income from other investments; (3) payments of moderate amount for amortization of loans or for depreciation of direct investments; and (4) moderate remittances for family living expenses.

reiterated the view that they were not prepared to endorse the position that MCPs applying solely to capital transactions fall within the Fund’s jurisdiction under Article VIII, Section 3. As a result, the current practice will remain in place—namely, that while MCPs applying solely to capital transactions would continue to be identified as MCPs in staff reports, they will not be subject to Fund approval.⁴⁷ In these circumstances it is necessary to clarify the relationship between the MCP policy and the IV.

32. The following linkages between the MCP policy and the IV are clarified. In line with the recent review of the IV, staff has amended the proposal set out in *Initial Considerations* (i) to better reflect the view that capital flow management measures (CFMs)⁴⁸ should generally not be designed in a way that gives rise to exchange restrictions and MCPs on current transactions, (ii) to confirm that the IV does not alter the Fund’s jurisdiction or policies under Article VIII, Sections 2(a) and 3, and (iii) to avoid potential inconsistencies from the application of both the Article VIII policies and the IV.^{49,50} Staff therefore propose that measures that give rise to MCPs and exchange restrictions and which are also considered CFMs because they relate to transactions that are capital in nature but considered as current under the Fund’s Articles of Agreement be assessed only under the criteria for approval under the respective Article VIII policy and will not be assessed for appropriateness under the IV. MCPs that apply solely to capital transactions (as per Article XXX(d)) are not subject to Fund approval and the appropriateness of these measures, if they are also considered to be CFMs, will be assessed only under the IV while they will continue to be identified in Article IV reports as MCPs.⁵¹ **Proposed Decision, Paragraph 6.**

D. Resource and Data Issues

33. The proposed policy changes would require limited additional resources once the policy is well-established. Indeed, as discussed above, the revised definition of official action is likely to reduce the number of cases to monitor. At the same time, the new policy envisages more consistent monitoring of actual exchange rate spreads in cases where official action is present, as the Fund would no longer make MCP findings based on potentiality. Preliminary testing by staff also suggests that the number of MCPs is likely to decline under the new policy, since it is focused on official action that segments markets, based on actual deviations of exchange rates and better anchored on country-specific market developments.⁵² As a result, staff anticipate that, over time, fewer resources will be required for the assessment of MCPs and do not expect that the new policy

⁴⁷ The Executive Board may revisit this issue at the next review of the MCP policy.

⁴⁸ The provisions of this paragraph will also be equally applicable to measures that are CFM/MPPMs.

⁴⁹ The IV provides that: “as the Articles define ‘payments for current transactions’ to include certain items that, from an economic perspective, are capital in nature, CFMs that restrict the making of payment and transfers for any of these transactions would continue to be subject to the Fund’s Article VIII jurisdiction and prior approval.” See [The Liberalization and Management of Capital Flows – An Institutional View](#), SM/12/250, Revision 1, 11/14/2012 (para. 62).

⁵⁰ Further, any MCP which is also a CFM, except for such MCPs applicable solely to capital transactions, will be only assessed under the MCP policy approval criteria.

⁵¹ See *Review of the Institutional View on Liberalization and Management of Capital Flow* (SM/22/42), paragraphs 59-63.

⁵² See *Initial Considerations*, [Supplement 3](#).

would increase the workload of staff or the authorities compared with the current policy, with the understanding that in the initial phases of operationalization, additional resources may be required.

34. The continuation of the daily monitoring of exchange rate data by the country team is not foreseen to be resource-intensive and will be needed only after staff has identified an official action by the authorities on the FX market, as is the current practice. Market data are generally available from the main data sources, Reuters and Bloomberg, and existing Fund subscriptions to these data providers are adequate. The monitoring will be performed on automated templates, after the data have been downloaded from the providers and, where necessary, included from the authorities.

35. The new policy does not introduce new data provision requirements, but clarifies the current requirements further as follows.⁵³ With respect to market exchange rates, the revised policy would rely primarily on exchange rate data compiled by reputable third-party data providers. Information may also need to be provided by a member country, for example, when data is not available from the third-party data providers.⁵⁴ In that regard, members are already obliged to provide, to the best of their ability, exchange rate data necessary for the assessment of MCPs, as indicated in the *Initial Considerations*. Namely, Article VIII, Section 5 requires each member to provide information on “buying and selling rates for foreign currencies” and also on “exchange controls”, i.e., a comprehensive statement of exchange controls in effect at the time of assuming membership in the Fund and details of subsequent changes as they occur.^{55,56} As part of this existing obligation, members must provide information on the exchange rates arising from official action, such as: (i) unpublished exchange rates used in transactions by the authorities that segment the market, including auction exchange rates⁵⁷ for auctions not conforming to best practices; (ii) market exchange rates if not available from public sources or third party providers; (iii) exchange rates in legal parallel markets; (iv) taxes, fees, other costs and subsidies related to exchange transactions; and (v) exchange rates set forth in official payment arrangements. Moreover, members have generally also provided other information necessary for staff to conduct an MCP assessment, including, for example, any relevant laws, regulations, or agreements (such as bilateral payment arrangements), and would be expected to continue to do so. While members would be expected to provide such documents/information as part of the Fund’s cooperative approach to addressing MCPs, if problems arose in the provision of such documents/information and were members to refuse to do so, consideration could be given to expanding Article VIII, Section 5 in the future to

⁵³ For discussion of data provision to the Fund, see “*Review of Data Provision to the Fund for Surveillance Purposes*,” SM/22/35.

⁵⁴ See *Initial Considerations*, [Supplement 3](#).

⁵⁵ Article VIII, Section 5(x) and 5(xi).

⁵⁶ Rule H-6 of the Fund’s Rules and Regulations provides that “the Fund shall arrange through the fiscal agencies of members that frequent and regular information as to the market rates of members’ currencies bought and sold in their territories is made available to the Fund” Also, under Article IV, Section 2(a), Fund members must “notify the Fund promptly” of any changes to their exchange arrangements.

⁵⁷ Auction exchange rate in multiple price auctions for this purpose means the weighted average rate of the successful bids. See Paragraph 55 of *Initial Considerations*, [Supplement 3](#).

encompass the provision of such information within that framework. ***Proposed Decision, Paragraph 7.***

TRANSITIONAL ARRANGEMENTS

A. Application of the New MCP Policy

36. Transitional arrangements should be in place to ensure the smooth implementation of the proposed new MCP policy. After consideration, staff propose that the new policy becomes effective nine months following the Board meeting, subject to the exceptions discussed in Paragraph 38 below.⁵⁸ As of the effective date, the 1981 decision on the current MCP policy and other relevant Board decisions will be repealed.

37. Delayed entry into effect of the new MCP policy would provide time for members to adjust their policies accordingly, and for the Fund to prepare additional guidance on the implementation of the new policy. Delayed entrance into effect of the new policy would enable members to implement any adjustments needed to ensure that their exchange systems are compliant with the new MCP policy. The transition period also provides time for staff to establish the new monitoring system and prepare the guidance note.

38. To facilitate a smooth transition, two exceptions to the delayed entry into effect of the new MCP policy are proposed. First, staff propose that the revised definition of official action becomes effective immediately upon approval of the new MCP policy as follows: During the transitional period, no MCPs will be found where (i) official action takes the form of an official exchange rate calculated with a one day lag (Paragraph 16), or a foreign exchange auction consistent with specified criteria (see paragraph 15), or (ii) an MCP results from exchange rate spreads arising in an illegal parallel market (Paragraph 17). Second, staff also propose that the elimination of the provision on broken cross rates becomes effective immediately upon the approval of the new MCP policy. Accordingly, no MCP findings based on broken cross rates will be made during the transition period. ***Proposed Decision Paragraph 10.***

39. Following the publication of the Board paper and decision, staff will reach out to country authorities on the revised MCP policy. The outreach will aim to ensure that the new policy is well understood, including with respect to data provision requirements and the implications of the new methodology and to facilitate policy adjustments to the extent necessary.

⁵⁸ Staff also considered an alternative option under which the new policy would enter into effect immediately upon its adoption. The main advantage would be that the existing policy would be immediately repealed and replaced with the revised policy and all existing MCP findings based on the current MCP policy would be automatically deemed eliminated, subject to assessment under the new policy. However, the immediate entry into effect may not provide sufficient time for members to adjust their policies and for the Fund to provide additional guidance on the implementation of the new policy.

B. Status of Existing and New MCP Findings

40. During the transition period, the current policy would continue to apply with some exceptions. Given that the existing MCP policy articulates the obligations under Article VIII, Section 3, it would not be permissible for the Fund not to apply this policy during the transition period. As such, with the exceptions mentioned in paragraph 38 above, during the transition period, the current policy, including the existing criteria for approval of MCPs, would remain in effect, and members would be expected to comply. Where possible, staff will discuss with the authorities the likely treatment of any existing and newly identified measures under the new policy. Staff will liaise with country teams undertaking Article IV consultation and UFR missions during the transition period to provide them with guidance in respect of the implications of the new policy. Staff will also liaise with authorities to obtain exchange rate data including on exchange rates arising from official action necessary for the monitoring of exchange rate spreads once the new policy becomes effective.

41. During the transitional period:

- No new MCP will be found where (i) official action takes the form of an official exchange rate calculated with a one-day lag (Paragraph 16), broken cross rates (paragraph 18), or a foreign exchange auction consistent with specified criteria (see paragraph 15), or (ii) an MCP results from exchange rate spreads arising in an illegal parallel market (Paragraph 17) as discussed in paragraph 38. Existing MCPs based on the types of official action that will no longer be covered under the MCP policy will be considered eliminated as of the approval date of the new policy.⁵⁹ The elimination of the MCP will be reflected in the first Article IV consultation report issued after the approval of the new policy. Subject to the above, in Article IV consultations concluded during the transitional period, staff will assess under the current policy whether any new MCP has arisen or the previously identified MCP continues to exist and will recommend approval where warranted.
- Other existing MCPs will continue to be in place until considered eliminated as of the effective date of the new policy (see paragraph 42).

42. As of the effective date of the new policy:

- All existing MCPs will be considered eliminated as of the effective date of the new policy. The monitoring modalities under the new policy will become operational and staff will monitor whether official action (as defined under the new policy) gives rise to impermissible spreads under the new policy. If impermissible spreads emerge, an MCP will be found, and approval can

⁵⁹ In particular: for MCPs arising from FX auction staff will assess whether the auction meets the criteria specified in paragraph 15. For MCPs arising from an illegal parallel market, staff will confirm with the authorities that the parallel market is indeed illegal. For MCPs arising from exchange rate calculated with one-day lag staff will assess whether that exchange rate is computed based on the criteria specified in paragraph 16.

be granted pursuant to the revised approval policy in the context of the subsequent Article IV consultation or program review.

- If the same official action that gave rise to an MCP under the current policy gives rise to an MCP under the new policy either as of the date of effectiveness of the new policy or later on when an impermissible spread emerges, it will not be considered the “introduction” of an MCP for purposes of the standard continuous performance criterion on non-introduction and non-modification of MCPs under an IMF arrangement or monitoring instrument in place on the effective date of the new policy.

Proposed Decision