Germany's relations with the International Monetary Fund following the introduction of the euro

The transfer of monetary policy responsibility from the member states to the Community level and the introduction of the euro on January 1, 1999 will have repercussions on Germany's (and other euro area countries') relations with the International Monetary Fund. Germany continues to be a member of the IMF, and the IMF Articles of Agreement have not been amended, meaning that the rights and obligations defined therein continue to apply. Nonetheless, beyond the scope of this set of rules, there will be changes in the exercising of membership, in view of the responsibilities defined in the EC Treaty. This article will show what aspects play a role here and which concrete adjustments have been undertaken so far.

The IMF's mandate

The Articles of Agreement of the International Monetary Fund (IMF) were signed in Bretton Woods on July 22, 1944 and entered into force on December 27, 1945. The Federal Republic of Germany became a member in 1952 and translated the Agreement into national law by passing its IMF Act. According to Article I of the Agreement, the IMF has economic and monetary policy tasks. Among other things, it is to promote international monetary cooperation, to maintain orderly exchange arrangements among its member countries, to assist in the establishment of a multilateral payment system, and, as appropriate, to provide temporary balance of payments assistance. Conversely, Germany, like the other member countries, is obligated to provide financial resources to the IMF which are then used to provide assistance to countries with balance of payments difficulties through the IMF's facilities.[1]

Article IV stipulates that the Fund shall oversee the international monetary system in accordance with its mandate. The Fund is to ensure that the international monetary system functions smoothly and that its member states meet their commitments. In particular, it shall support its members' efforts to conduct an adequate monetary and exchange-rate policy. For their part, the member countries are required to support the IMF in its surveillance activities by providing it with the relevant information and to regularly hold bilateral consultations. In this manner, the economic and monetary situation of each member country is comprehensively monitored and, as appropriate, the relevant adjustment measures are recommended.

The IMF's relations with its member countries

The IMF Articles of Agreement provide only for sovereign states to become members, but not dependent territories or supranational unions or institutions such as the EC or currency areas such as the euro area. Each member nation is assigned a quota that is designed to broadly reflect the relative size of its economy in the world. It is on that basis that a country's financial rights and obligations within the IMF and its voting rights are determined. Germany's quota share in the IMF is currently 6.2 %. The 15 EU nations have a combined quota share of slightly over 30 %, and the 11 euro area countries a quota share of well over 23 %.

The supreme decision-making body of the IMF is the Board of Governors, in which all 182 member countries are represented. Among other things, it is responsible for admitting new members and determining or adjusting member quotas. The Board of Governors has transferred all powers that can be delegated to the Executive Board, which is thus practically charged with managing the IMF's day-to-day affairs. At present, the Executive Board is made up of 24 Executive Directors and the Managing Director. Five of the Directors are appointed by the five members having the largest quotas (the United States, Japan, Germany, France and the United Kingdom). This means twelve EU countries cannot appoint their own Executive Director. They, together with other EU and non-EU nations, are members of voting groups (constituencies) that together elect their Executive Director. In four of those constituencies, at present the Executive Director is a native of an EU country, which means there are currently a total of seven Executive Directors from EU countries.

Since 1970, the Bundesbank has been conducting the financial relations deriving from

1 The functions and operating method of the IMF are described in more detail in a special publication of the Bundesbank titled *"Weltweite Organisationen und Gremien im Bereich von Währung und Wirtschaft"*, Frankfurt am Main, April 1997 (available only in German).

Germany's membership in the IMF for its own account. The IMF Act provides for instructions to the German Executive Director to be given by the Federal Government or, more precisely, by the Federal Ministry of Finance. The Bundesbank is involved in the decision-making processes, especially when the financial rights and obligations incumbent upon the Bundesbank are involved. Further details are governed by an administrative agreement between the Federal Government and the Bundesbank.

The Communitisation of monetary policy

Upon entry into stage three of economic and monetary union (EMU) on January 1, 1999, responsibility for monetary policy was transferred from the euro area countries to the Community level. It is in the exclusive competence of the Community. The Treaties of Maastricht and Amsterdam divided competence in monetary and foreign exchange policy for the most part between the European System of Central Banks (ESCB) and the Council of Economic and Financial Ministers (the "Council"). Solely the ESCB is responsible for monetary policy (Art. 105 (2) of the EC Treaty). The Council, with the envisaged involvement of the European Central Bank (ECB), bears primary responsibility for the conclusion of formal exchange-rate agreements with non-Community countries and for general orientations for exchange-rate policy in relation to non-Community currencies (Art. 111 (1) and (2) of the EC Treaty). Yet only the ESCB is responsible for the implementation of exchange-rate policy; however, the ESCB's primary objective, to maintain price stability, must not be impaired. (The article numbers cited above refer to the Treaty of Amsterdam; see also the explanations on page 18.)

The fact that the Community is solely responsible in internal relationships, i.e. with its member states, means that the Community, to that extent, is also responsible for external relations. As a subject of international law, the Community can maintain relations with third countries and international organisations. In principle, it also has the right to conclude treaties under public international law within the confines of its external competencies.

The implementation of external competence in monetary policy

As regards the implementation of the external competence in monetary policy which was transferred to the Community with effect from January 1999, one must bear in mind that the IMF Articles of Agreement have not been amended. The rights of third countries and international organisations – including the IMF – and the corresponding obligations of the member states towards these countries and organisations deriving from valid international-law agreements are, in principle, not affected by subsequent Community legislation – such as the Treaty of Maastricht or the Treaty of Amsterdam. Article 307 (1) of the EC Treaty translated this principle into Community law as follows:

The Treaties of Maastricht and Amsterdam

The Treaty of Maastricht (the EU Treaty), which entered into force on November 1, 1993, marks the beginning of the European Union (EU). The EU Treaty is an overall treaty containing basic statements on, amongst others, the Union's objectives, its commitment to basic rights, and the principle of subsidiarity. It refers to the existing individual treaties (the EC Treaty, the ECSC Treaty, and the EAEC Treaty), which have been supplemented and further developed in large parts. The most important new element is the objective of an economic and monetary union (EMU), with the important rules and the necessary further integration steps having been defined in order to realise this union. Moreover, the EU Treaty regulates, as new elements, cooperation in a common foreign and security policy and in the fields of justice and home affairs.

The Treaty of Amsterdam, signed in October 1997 and in force since May 1, 1999, has developed the Treaty of Maastricht further, particularly with respect to a common foreign and security policy and the fields of justice and home affairs. Moreover, the primary preconditions have been established for the upcoming enlargement of the Union. The provisions governing EMU have remained unchanged. This set of agreements, which has simultaneously been simplified and recodified, now constitutes the presently valid legal framework for the Union, together with the annexed protocols and declarations.

Deutsche Bundesbank

"The rights and obligations arising from agreements concluded before January 1, 1958 or, for acceding States, before the date of their accession, between one or more Member States on the one hand, and one or more third countries on the other, shall not be affected by the provisions of this Treaty."

The same principle is contained in Article 31.1, read in conjunction with Article 23 of the ESCB Statute. The provisions empower the national central banks to perform the appropriate transactions in order to fulfil their obligations towards international organisations. In this context, it is particularly important to note that as regards the IMF the Community did not automatically become the legal successor of the member states that entered into monetary union. The mere fact that not all EU countries introduced the euro from the outset would have been enough to make this problematic. Moreover, the Community is not able to assume responsibility anyway for areas such as economic policy, which continue to be the responsibility of the individual member countries – even if the Council has coordination responsibilities here.

However, under Community law the member states are required to eliminate any inconsistencies between their legal relationships with international organisations (and third countries) and Community law and to comply with the Community's jurisdiction when exercising their rights. Accordingly, rules were needed to govern the various types of relations with the IMF so that the IMF Articles of Agreement and the responsibilities resulting from them could be consistently complied with, and also so that the previous work in international monetary policy could be continued in an efficient manner.

Representation of the ECB in the IMF

Against this background, in accordance with Article 111 (4) of the EC Treaty, the Council (ECOFIN) shall unanimously decide upon the Community's external representation in monetary policy issues on a proposal from the Commission and after consulting the ECB. According to the exact wording of the Treaty, the Council must take account of the Community's internal allocation of powers, meaning that, according to Article 105 of the EC Treaty, the ESCB is responsible for monetary policy, and that according to Article 99 of the EC Treaty, the member states retain responsibility for their individual economic policies. As regards those tasks conferred upon the ESCB, it is then up to the ECB Governing Council to decide on how to distribute responsibility between the ECB and the national central banks (Art. 6.1 and 12.5 of the ESCB Statute).

As far as the representation of the ESCB in the IMF is concerned, the euro area countries, the ECB Governing Council and the IMF Executive Board and Management, after weighing various options and following extensive discussions among the euro area countries and with the IMF, ended up reaching the pragmatic conclusion that the ECB should be represented in the Executive Board of the IMF by an observer. The European Council in Vienna had also advocated this solution in mid-December of 1998, endorsing the view of the Council that solutions should be sought which do not require an amendment to the IMF Articles of Agreement. Accordingly, the Executive Board of the IMF decided on December 21, 1998 to give the ECB observer status at its meetings. The modalities of this observer status are as follows:

– The observer is invited to attend Executive Board meetings where euro area monetary policy is concerned. The subjects are explicitly stated in the "Observer Decision": Article IV consultations on monetary or exchange rate policy of the euro area countries as a whole; Article IV consultations with individual euro area countries; the role of the euro in the international monetary system; the World Economic Outlook; international capital markets report; and world economic and market developments.

– Moreover, the ECB observer is invited on a case-by-case basis whenever deemed appropriate by the ECB and the Fund.

– The observer will be able to address the Board with the permission of the Chairman on matters within the responsibility of the ECB.

– The Fund communicates to the ECB the agenda for all Board meetings and, in addition, the documents for those meetings to which the ECB observer has been invited.

– The observer status shall be reviewed within a year at the latest (before January 1, 2000).

The ECB observer has no right to vote in the IMF Executive Board (the IMF Articles of Agreement do not permit this). Only Executive Directors of the IMF have voting rights (except whenever a tie-breaking vote is needed, in which case the Managing Director has a deciding vote).

As an alternative to observer status, other options were studied but eventually rejected. For instance, it would have been conceivable for Community interests in euro area monetary policy to be represented by one of the Executive Directors of the euro area countries. However, owing to the composition of the constituencies, in some cases this could have led to a conflict of interest.

Consultations on euro area monetary policy

The introduction of the euro also directly affects the consultations provided for in Article IV of the IMF Articles of Agreement. Since the individual euro area countries are no longer solely responsible for all aspects of economic and monetary policy, the consultation procedure with the IMF had to be modified.

Here, too, the key was finding a pragmatic solution. A consultation procedure with the euro area in its own right was out of the question for legal reasons, Article IV consultations only being possible with member countries of the Fund. Supranational and international institutions or organisations, not being able to be a member of the IMF, have no special rights or obligations towards the IMF.

The euro area countries, as IMF members, must be able to ensure that the Fund can completely fulfil its surveillance responsibilities under Article IV. To this end, an agreement was reached whereby the IMF regularly holds consultations on monetary and exchange-rate policy and other relevant policy areas with the ECB, the European Commission and, as appropriate, with other European institutions. However, these "supranational" consultations are considered to be legally part of the Article IV consultations with the individual euro area countries. The details of the arrangement are as follows:

– The consultations with the individual euro area countries are continued at the same intervals as in the past, i.e. generally every twelve months. It is envisaged that this rotation will be reassessed at a later date.

– European monetary policy and other issues for which the Community is responsible are to be discussed with the competent EU institutions every six months and independently of the country consultations. These discussions are considered to be an integral part of the consultations with the individual euro area countries.

– Staff Reports are to be written, and an annual Board discussion to be held, on the euro area countries' monetary and exchange-rate policy. Other economic aspects will be incorporated, too, provided this is necessary to assess monetary policy properly.

– A comprehensive public information notice, or PIN, agreed with the euro area countries, will be published containing the results of these consultations.

The first round of consultations on the euro area's monetary and exchange-rate policy was held at the beginning of 1999 and completed at the end of March. The above described procedures passed the test.

Consultations on other economic policy areas

The ESCB's sole responsibility for monetary policy and the resultant exclusive right, embedded in Community legislation, to external representation in European monetary policy has been duly taken into account in the aforementioned changes in the relations with the IMF. Moreover, the Council, in accordance with Article 111 of the EC Treaty – as mentioned above – has certain competences regarding exchange-rate policy and the coordination of general economic policy, though the latter remains the responsibility of the member nations.

On issues pertaining to external representation, the European Council, at its meeting in Vienna on December 11 and 12, 1998, gave a comprehensive statement. In its conclusions, it favoured observer status for the ECB in the IMF. In addition, on external representation at the IMF regarding issues not related to monetary policy, the Council states:

"... the views of the European Community / EMU would be presented at the IMF Board by the relevant member of the Executive Director's office of the Member State holding the Euro 11 Presidency, assisted by a representative from the Commission."

It is still an open question how the European Council's views on representing the standpoints of the EC or the EMU on issues other than monetary policy can be specifically implemented. One must bear in mind that the primary responsibility for nearly all non-monetary policy issues, especially fiscal policy and labour market policy, remains with the individual member countries. The Executive Directors of the EU countries regularly coordinate their views "on site" within the framework of the instructions given to them by their home authorities.

The Bundesbank's role as a fiscal agent and a depository

The member countries, including Germany, maintain a variety of financial relations with the IMF that are regulated in detail in the IMF Articles of Agreement. In particular, the members provide the financial resources, but in some cases they are also borrowers. The Articles of Agreement specify, among other things, which currencies are to be used for which transactions.

For conducting financial transactions, every country designates a fiscal agent (that formally acts as the business partner of the IMF) and a depository (which holds the accounts). For Germany, the Bundesbank is both the agency for dealing with the Fund and the depository. This nationally assigned responsibility did not change upon the introduction of the euro. The individual euro area countries, as members of the IMF, are still responsible for the financial relations with the IMF. This is supported by the EC Treaty (Article 307 (1) of the EC Treaty). Incidentally, there is no economic or technical need (and, from the point of view of the euro area countries, at present no intention) to centralise the fiscal agent and depository functions in view of the introduction of the euro.

Subscriptions, financing and replenishment of funds

Every member country of the IMF must make subscription payments equal to its quota. Normally 25 % of these payments are made in special drawing rights (SDR) or convertible currency and the other 75 % in the national currency. Effective payment in national currency is made in the event of drawings by other countries or calling-up by the IMF. As the euro has been the national currency of the 11 euro area countries since January 1, 1999, these countries make national currency payments in euro. For instance, in February 1999 Germany made 75 % of the payment necessitated by the quota increase in euro.

Whether and to what extent the IMF member nations or their national currencies are used to finance IMF lending is based on principles set forth in the Articles of Agreement and on additional guidelines established by the Executive Board. The key factor in whether a member can be considered a creditor for the operational budget, in principle, is a sufficiently strong balance of payments and/or reserve position. Indicators of external strength such as reserve assets, current account balances and external indebtedness are taken into account. The introduction of the euro has led to two changes in the preparation of the operational budget at the beginning of 1999:

– In place of the former national currencies, the euro area countries now make euro balances available. It is, however, the national authorities who continue to be responsible for providing the funds.

– In addition, in order to gauge the level of the contribution to be made by the individual creditor countries to the operational budget, the reserve situation of the individual countries participating in the budget is no longer to be the key factor. Using the reserves as a yardstick makes no sense for countries that share a common currency. Due to the significance of the euro area countries, the IMF therefore changed its procedure for all participating countries. Since the turn of 1998-9, they have been drawn upon according to their IMF quota shares.

In order to raise currencies for lending to other member countries in addition to quota subscriptions, the IMF can also borrow from its members under certain conditions – for instance, under the New Arrangements to Borrow (NAB). Here, too, the euro has taken the place of the former national currencies of the euro area countries.

The euro area countries as borrowers

One of the key rights of IMF members is to draw on IMF financial assistance. The precondition is a balance of payments need. However, the euro area countries are quite unlikely to have such a need (the last time an EU country received balance of payments assistance from the IMF was in 1977). Therefore, the implications of the introduction of the euro for the procedures in the event a euro area country wants to make use of IMF credit have so far been discussed only in passing. This discussion revolved around the question of whether, and if appropriate, how such a "balance of payments need" of euro area countries can be ascertained and financial assistance be applied for.

It is widely held that there is no such thing as an individual balance of payments need for geographical parts of the euro area. These parts do not have a currency of their own, making the transactions of the individual euro area countries with foreign countries irrelevant. The euro has replaced the national currencies and defines the new currency area, which means that a balance of payments need can only exist for the euro area.

Notwithstanding this, it is conceivable that a single country might be able to trigger such a need, say, through excessive government indebtedness in foreign currency. Apart from that, only IMF member countries are entitled to request balance of payment assistance, i. e. only individual euro area countries – and, in particular, not the Community. Against this background, a pragmatic approach must be found that will enable euro area countries to request IMF financial assistance, if necessary, and to justify their need for credit – according to IMF rules. However, as the prospect of euro area countries needing to make use of these resources is quite unlikely, this issue is not urgent.

The new composition of the SDR

The SDR plays a crucial role in the IMF's accounts and as a unit of account in its financial relations with its members. The IMF defines the SDR as a basket of the five most important currencies, which are periodically adjusted in terms of their amount. Their shares in the basket are intended to roughly represent the external weight of these currencies (see also table on page 25).

Upon the introduction of the euro on January 1, 1999, the contents of the SDR basket needed to be changed, since it contained national currencies of euro area countries in addition to the US dollar, the pound sterling and the yen. The currencies contained in the basket up to the end of 1998 that were superseded by the euro have been replaced in the basket by their corresponding value in

Changes in the SDR basket with effect from January 1, 1999

Currencies	Amounts: up to December 31, 1998	Amounts: from January 1, 1999	Exchange rate vis-à-vis the dollar 1 on December 31, 1998	US dollar equivalents 2: on December 31, 1998	US dollar equivalents 2: on January 1, 1999
DM	0.446	–	1.67070	0.267	–
Euro (for DM)	–	3 0.2280	0.85422	–	0.267
FF	0.813	–	5.6033	0.145	–
Euro (for FF)	–	3 0.1239	0.85422	–	0.145
£ sterling	0.105	0.1050	1.6635	0.175	0.175
Yen	27.20	27.2000	113.66	0.239	0.239
US $	0.582	0.5821	1.0000	0.582	0.582
Total	.	.	.	1.408	1.408

1 For £ sterling: US $ to the £; for all others: currency units to the US $. The same rates apply to the calculation for January 1, 1999. — **2** Amounts rounded. — **3** The amounts of euro correspond to the amounts of national currencies previously used, based on the irrevocably fixed conversion rates (i.e. DM 1.95583 to the euro and FF 6.55957 to the euro).

Deutsche Bundesbank

euro. In concrete terms: the amounts for Deutsche Mark (DM 0.446) and for French francs (FF 0.813) were replaced by their corresponding amounts in euro (€ 0.2280 and € 0.1239, respectively), based on the conversion rates irrevocably fixed on December 31, 1998. As the countervalue was the same, the value of the SDR was not changed by the exchange of currencies. The pound sterling has remained in the SDR as a currency in its own right, since the United Kingdom did not introduce the euro on January 1, 1999. In 2000, the composition of the SDR basket is up for a scheduled review.

IMF relations and sovereignty of money creation

The exercising of financial rights and obligations of the euro area countries towards the IMF through national authorities implies a certain overlapping with the ESCB's monetary sovereignty or the sovereignty of money creation. In principle, the euro area countries – in keeping with the valid treaties – can continue their existing financial relations with the IMF as before. However, as far as the execution is concerned, expansionary or contractionary money creation effects could happen in the euro area.

Upon closer examination, the overlapping of national financial relations with the IMF with the ESCB's monetary policy responsibilities is not as serious as it may seem at first sight. It is true that the timing and the volume of transactions with the IMF are not always predictable over the longer term. However, sufficient provision has been made so that no uncontrollable developments can occur:

– The ECB is informed comprehensively of payments between the Bundesbank and the IMF. This applies both to routine transactions and to less common or particularly voluminous transactions (such as the subscription payment for the increase of the German quota in February 1999). If need be, the ECB should be informed of major transactions beforehand.

– The ECB is generally also informed of the situation in the run-up to unusual developments (such as the compilation of financial packages for crisis countries).

– The ECB can and will take into account large transaction volumes of the national central banks with the IMF in its liquidity management and, as appropriate, offset them.

– The problem of a potential influence of IMF transactions on the money stock or the money creation process is not new. Even in the past, financial transactions with the IMF had to be "digested", in monetary policy terms, by the Bundesbank at the national level. This never posed a danger to liquidity management, though.

Conclusions

The introduction of the euro has led to a number of changes in the euro area countries' relations with the IMF. These changes have been implemented in a pragmatic way, and the modified procedures have turned out to be quite workable. Further-reaching changes are not envisaged at present. On the whole, the transfer of monetary policy responsibility from the national central banks to the ESCB has led neither to temporary friction nor to fundamental difficulties in Germany's relations with the IMF.