



# Handbook for the use of Special Drawing Rights SDRs for Fiscal Purposes

# **Handbook for the use of Special Drawing Rights (SDRs) for Fiscal Purposes**

## **Edition by:**

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# Presentation

For over a year, social organizations, think tanks and political sectors around the world have insisted on the need to resort to a global financing mechanism in order to help overcome the economic and social crisis deepened by the Covid-19 pandemic. The slowness and lack of force in public resources that should have been used as fiscal support caused 45 million people in Latin America to fall into poverty, and the region suffered the largest gross domestic product drop compared to the rest of the world.

The strongest response consisted in opening credit lines to address some urgent situations, but with a significant setback in terms of inequality, gender equity and the progress needed to face climate change, among others. To top it all, countries that significantly increased their debt relative to GDP were also forced to increase their debt service, with a very rapid reaction from the International Monetary Fund (IMF) towards fiscal austerity measures. The findings are overwhelming: in exchange for IMF loans, countries such as Colombia have established fiscal austerity measures of 7% of GDP between 2021 and 2026, Costa Rica of around 2% of GDP by 2024, Peru of 2.2% of GDP between 2022 and 2023.

Without any fiscal income it will be impossible for the region to reactivate its economy in order to obtain the necessary resources for the social, health and environmental care of its population. Multilateral organizations coincide in a new lost decade, even more so when it is calculated that by 2022 emerging countries will no longer have any additional fiscal support to address the crisis.

In this scenario, the decision to issue US 650 billion in Special Drawing Rights (SDR) is bittersweet news: on the one hand, it is the recognition of the seriousness of the crisis and the need for a unified plan on the international agenda, but on the other hand it leaves the unpleasantness of being insufficient, untimely and with prospects of deepening inequality if other corrective measures are not taken. For example, 2/3 of these resources will be directed to countries that do not need them, so they should be reallocated.

However, on this occasion, we want to focus on one particular point. At Latindadd we have worked with the Ecuadorian economist Andrés Arauz to build a manual that will guide countries on how to use the issuance of SDR. It is widely believed that the only possibility is to save these resources as international reserves, which would not be of great help to countries at the moment. We have worked together with Andrés to make other possibilities visible, so that these resources can be used instead as fiscal spending.

We hope that governments, congresses and social organizations will use this manual according to their needs and interests, in favor of a faster and more sustainable recovery.

# Handbook for the use of Special Drawing Rights (SDRs) for Fiscal Purposes

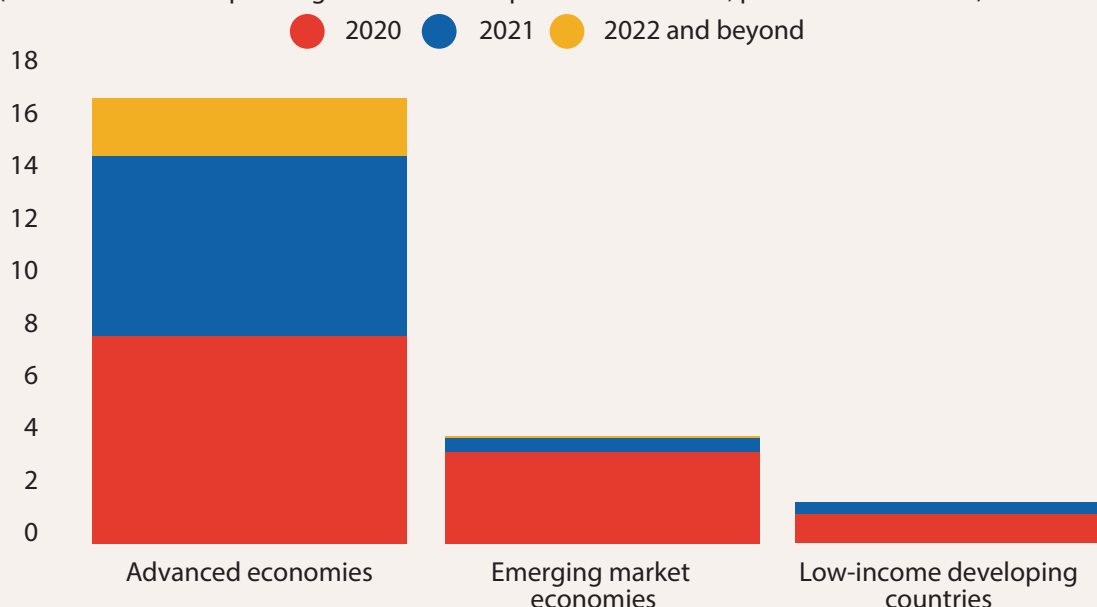
## 1

### Introduction

The pandemic crisis showed us the richest countries' extraordinary capacity for monetary creation. The rich countries' central banks created trillions of dollars, euros and pounds, much of which made it into their fiscal budgets. The US Federal Reserve provided unlimited dollars through currency swaps for its closest monetary allies: the European, English, Japanese, Swiss and Canadian central banks. For a second group of nine allied countries, limited swaps were offered. The United States, the privileged five and the nine beneficiaries add up to 33 countries (the eurozone is 19 countries), which represent only 17.7% of the world population.

**Figure 1. Divergences in policy support<sup>1</sup>**

(Total revenue and spending measures in response to COVID-19; percent of 2020 GDP)



Sources: IMF Fiscal Monitor database of Country Fiscal Responses to COVID-19; and IMF staff calculations

1 Drawing Further Apart: Widening Gaps in the Global Recovery. IMF. July 27, 2021. <https://blogs.imf.org/2021/07/27/drawing-further-apart-widening-gaps-in-the-global-recovery/>

The rest of the countries, those that are not at the top of the monetary pyramid, which represent 82.3% of the world population, are left with monetary multilateralism, that is, the International Monetary Fund (IMF). The IMF made many loans and generated billions in profits in the pandemic. But developing countries needed more funds, not more debt. Although calls were made since March 12, 2020<sup>2</sup> and the IMF's Managing Director, Kristalina Georgieva, showed early will, there was no endorsement from the United States, an indispensable vote, to approve an extraordinary and significant issuance of Special Drawing Rights.

The issuance was finally approved in August 2021, 17 months after the World Health Organization declared Covid-19 a pandemic and 7 months after the change in the White House. It is regrettable that the delay in the approval of the issuance was, among other issues, to prevent the allocation from reaching a South American country<sup>3</sup>.

In the coming months, the world will experience a great opportunity for monetary discussion. Citizens will wonder where does this free money come from? How can it be created for free? Why do almost two-thirds of the allocation go to the richest countries, the same ones that have already created trillions for themselves? Why did it take so long to create? Why then isn't it used to eradicate hunger, fight climate change, or fund universal public health?

This manual intends to tackle this last question, in a national focus. Conventional voices will respond that Special Drawing Rights can only be used for international transactions between central banks and that they cannot be used by governments for spending. It is true SDRs are international assets, but regarding spending, they are wrong or seek to mislead. In general, they are the same voices that said that the Special Drawing Rights are debt and that they are of no use to countries. This has already been denied. This manual seeks to provide sufficient technical knowledge to government authorities, finance ministers and civil society leaders to promote the fiscal use of Special Drawing Rights based on proven experiences, perfectly legal and in strict compliance with international treaties, national laws, and conventional accounting standards.

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- 2 Time for a SDR injection, March 12, 2020. Financial Times. <https://www.ft.com/content/b20f781c-842f-49c7-9939-f7390a90c01b>, It's time to end the Fed's monetary triage, March 23, 2020. The Nation. <https://www.thenation.com/article/economy/economy-fed-imf/>, Farma-colonialismo y triaje monetario, March 26, 2020. El Diario.es [https://www.eldiario.es/murcia/murcia-y-aparte/farma-colonialismo-triaje-monetario\\_132\\_1001412.html](https://www.eldiario.es/murcia/murcia-y-aparte/farma-colonialismo-triaje-monetario_132_1001412.html), G20 should call for IMF to issue 3 trillion SDRs. March 28, 2020, CEPR <https://cepr.net/press-release/g20-should-call-for-imf-to-issue-3-trillion-sdrs-cepr-economists-say/> and LatindaddAmérica Latina necesita acceder a recursos sin generar deuda, Latindadd. July 1, 2020. Latindadd <http://www.latindadd.org/wp-content/uploads/2020/07/América-Latina-necesita-acceder-a-recursos-sin-generar-deuda-DEG-Latindadd-.pdf>
- 3 Venezuela cut off from share of IMF's \$650 billion new reserves. Bloomberg. April 16, 2021. <https://www.bloomberg.com/news/articles/2021-04-16/venezuela-cut-off-from-share-of-imf-s-650-billion-new-reserves>

## 2

# Background

## 2.1 What are SDRs?

Special Drawing Rights (SDR) are an international reserve asset created by the International Monetary Fund (IMF) in 1969. The unit of account value is based on the US dollar, the Japanese yen, the British pound, the euro and the Chinese renminbi. The purpose for which it has been created and used historically is to enhance international reserves: access more financing, increase foreign investment and contribute to the stability of the purchasing power of the national currency.

Between 1970 and 2009, the IMF's SDR department has issued SDRs four times for a total amount of USD 318 billion. Most of this asset has been held as international reserves. The IMF specifies that members can “sell or use part or all of their allocations”, exchanging them for “freely usable currencies.” Countries are permitted to

1. “buy and sell SDRs both spot and forward;
2. borrow, lend, or pledge SDRs;
3. use SDRs in swaps; or
4. use or receive SDRs in donations”<sup>4</sup>.

SDRs are not loans, they are not debt, and they do not have to be repaid to the IMF. When exchanged for freely usable currencies, countries incur in a significantly low annual interest rate, which today is 0.05%<sup>5</sup>. Their use depends on other countries wanting to accept them and deliver the aforementioned currencies in exchange. However, if there are not enough countries willing to accept SDRs in exchange for free usable currency, the IMF can designate which members without balance of payments problems should mandatorily accept SDRs.

## 2.2 The 2009 issuance

The largest SDR issuance to date was authorized in August 2009, following the global financial crisis. The issuance corresponded to USD 250 billion, of which about USD 100 billion went to emerging and developing countries, of which only USD 18 billion went to low-income countries.

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4 Questions and Answers on Special Drawing Rights (SDRs). IMF. July 12, 2021. <https://www.imf.org/en/About/FAQ/special-drawing-right#Q1.%20What%20is%20an%20SDR>

5 Rates Query Output. June 13, 2021. IMF. <https://www.imf.org/external/np/fin/data/queryoutput.aspx?origin=imf-finance>



## 2.3 The 2021 issuance

For August 2021, an SDR issuance of USD 650 billion is estimated. High-income countries will receive 67% of the SDR allocation, middle-income countries 32%, and low-income countries 1%. Latin America would receive approximately USD 51.5 billion, corresponding to 8% of the total amount issued.

In July, the IMF's Executive Board approved the allocation and on August 2, the Board of Governors took the final step for its approval. On August 23, member countries will receive the allocation

## 2.4 The pandemic and the needs of low- and middle-income countries

According to estimates by the United Nations Conference on Trade and Development (UNCTAD), developing countries would require between USD 2 and 3 trillion until December 2021 to respond to the fall in tax revenues and avoid a lost decade<sup>6</sup>. The richest countries have implemented measures for USD 13 trillion, which has allowed them a faster recovery but has also widened the inequality with low- and middle-income countries.

Before the pandemic, the United Nations had estimated that developing countries faced a funding gap of USD 2.5 trillion per year to achieve the Sustainable Development Goals<sup>7</sup>.

With a projected 7.1% fall in the 2020 Gross Domestic Product (GDP) for Latin America, the highest in the world and 45 million new poor, a fiscal effort of just 4.6% of GDP for that same year has been insufficient. The prospects for fiscal austerity, starting as soon as in 2021, when Latin America continues to be the epicenter of the pandemic, predict a slower recovery, which according to the Economic Commission for Latin America and the Caribbean (ECLAC) could take - at least - a decade<sup>8</sup>. Table 1 shows measures considered by select countries in the region, some of which are included as recommendations for the loans recently granted by the IMF.

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6 COVID 19: UNCTAD warns of lost decade if austerity becomes countries' winning policy mindset. UNCTAD. September 22, 2020. <https://unctad.org/press-material/covid-19-unctad-warns-lost-decade-if-austerity-becomes-countries-winning-policy>

7 Arrested development: International Monetary Fund lending and austerity post Covid-19. Briefing Paper. Eurodad. October 2020. <https://d3n8a8pro7vhmx.cloudfront.net/eurodad/pages/1063/attachments/original/1608122652/arrested-development-FINAL.pdf?1608122652>, World Investment Report. UNCTAD. 2014. [https://unctad.org/system/files/official-document/wir2014\\_en.pdf](https://unctad.org/system/files/official-document/wir2014_en.pdf)

8 Fiscal panorama: Latin America and the Caribbean. ECLAC, April 22, 2021. <https://www.cepal.org/en/publications/46809-fiscal-panorama-latin-america-and-caribbean-2021-fiscal-policy-challenges>



**Table 1. Fiscal austerity measures: selected countries**

Country	Size of the fiscal adjustment	IMF program in force
Ecuador	5.5% of GDP for 2022	Extended Facility: USD 6.5 billion
Colombia	7% of GDP between 2021 and 2026	Flexible Credit Line: USD 12.2 billion
Costa Rica	Primary budget surplus of 1% of GDP for 2023 and 1.7% for 2024	Extended Facility: USD 1.7 billion
El Salvador	4% of GDP for 2021	Extended Facility: USD 300 million
Peru	2.2% of GDP between 2022 and 2023	Flexible Credit Line: USD 11 billion

Sources: IMF staff reports <sup>9</sup>

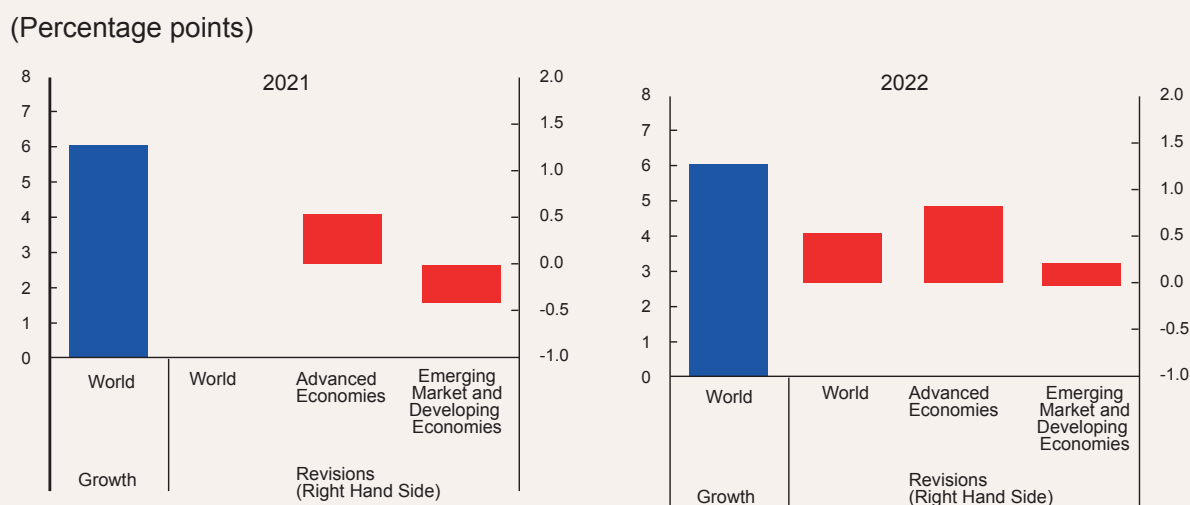
The outlook seems to indicate a slow recovery. An inertial recovery will bring the region slowly to the levels of 2019, but it will not contribute with solutions to inequality and social discontent that prevailed before the pandemic. The region requires funding that allows its states to invest in health and economic recovery with equality in mind, within the framework of the Sustainable Development Goals.

Additionally, economic recovery will not be the same for all countries. The IMF has estimated that there is a high risk of divergent growth between advanced economies and the rest of the world, as the former will emerge from the crisis much earlier, as shown in Figure 2. In the very short period between April and July 2021, the IMF had to adjust the expected growth of advanced economies upward and adjust the expected growth of developing countries significantly downward. A similar phenomenon occurred for the 2022 forecasts.

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9 Latest Country Staff Reports. IMF. <https://www.imf.org/en/Publications/CR/Issues/2020/12/23/Ecuador-First-Review-Under-the-Extended-Arrangement-Under-the-Extended-Fund-Facility-and-49980>, <https://www.imf.org/en/Publications/CR/Issues/2021/03/23/Colombia-2021-Article-IV-Consultation-Press-Release-Staff-Report-and-Statement-by-the-50301>, <https://www.imf.org/en/Publications/CR/Issues/2021/03/01/Costa-Rica-2021-Article-IV-Consultation-and-Request-for-an-Extended-Arrangement-Under-the-50136>, <https://www.imf.org/en/Publications/CR/Issues/2020/04/16/El-Salvador-Staff-Report-Request-for-Purchase-Under-the-Rapid-Financing-Instrument-Press-49333>, <https://www.imf.org/en/Publications/CR/Issues/2021/03/24/Peru-2021-Article-IV-Consultation-Press-Release-Staff-Report-and-Statement-by-the-Executive-50305>

**Figure 2. Growth perspectives for advanced economies and the rest.**



Source: IMF <sup>10</sup>

In terms of vaccination, by mid-2021 advanced countries have covered 40% of their population, while emerging countries have covered only 11%. The slower this process, the slower the recovery, with added risks that advanced economies' central banks may increase interest rates prematurely, slowing down the recovery even more and causing capital outflows from developing countries.

Faced with these clear divergences between advanced economies and developing countries and considering the enormous inequality in the allocation of SDRs, one of the discussion topics is the recycling or donation of SDRs, from rich countries that do not need these reserve assets, to low- and middle-income countries that do.

## 2.5 SDRs: save or spend?

The other big discussion after the issuance is regarding the use of resources. The prevailing narrative has been that it's useful to "save" them, that is, to strengthen central banks' international reserves. Indeed, SDRs are directly allocated from the IMF's SDR Department to countries' international reserves, generally managed by central banks.

Conventional voices have argued that SDRs are only reserve assets and should only be used (exchanged) exceptionally for balance of payments purposes, exclusively by central banks. However, it is appropriate to incorporate them into the government budget and also use them as fiscal resources. If in the budget, it becomes a sovereign decision, and not one of the central bank, in what proportion they should be saved or spent.

Fortunately, in increasingly explicit terms, IMF authorities have leaned to the

<sup>10</sup> Drawing Further Apart: Widening Gaps in the Global Recovery. IMF. July 27, 2021. <https://blogs.imf.org/2021/07/27/drawing-further-apart-widening-gaps-in-the-global-recovery/>

position that favors spending. In the context of the vaccination and economic recovery needs of emerging and developing countries, the IMF published that “a general allocation of Special Drawing Rights (SDR) ... should be completed quickly so as to provide liquidity buffers for countries and **help them address their essential spending needs.**”<sup>11</sup> This language is echoed in statements by IMF spokesman Gerry Rice, who stated that the IMF would advise countries how best to use SDRs to strengthen the reserves of a country; **create room for urgent priority spending**; and, support better policies<sup>12</sup>. The same language was present in a recent speech by the IMF Managing Director: “Lebanon would receive about \$860 million of SDRs at this critical moment to strengthen the country’s depleted reserves and also to **help with the many urgent needs of the Lebanese people.** ... This is a precious resource. It must be deployed for the maximum benefit of the country and **its people.** How to use SDRs, of course, is a **sovereign decision.**”<sup>13</sup>

If SDRs are managed solely as exclusive property of central banks, governments would lose the opportunity to use the amount equivalent to SDRs for priority health and vaccination expenditures or other investment needs. It is worth emphasizing that the fall in tax collection and the forecasts of slow economic recovery do not have their origin in monetary or exchange rate phenomena, but rather in biological and health phenomena, which is why governments should be the main users of SDRs.

Some voices propose that SDRs be used to pay or prepay pre-existing government external debt. However, even if government debt is to be paid with these new resources, the SDRs or their equivalent amount must first become part of the fiscal budget.

There is a solution: countries can deposit all the SDRs received with their own central banks. This would increase the short-term fiscal capacity of governments and would also strengthen the level of international reserves.

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11 Drawing Further Apart: Widening Gaps in the Global Recovery. IMF. July 27, 2021. <https://blogs.imf.org/2021/07/27/drawing-further-apart-widening-gaps-in-the-global-recovery/>

12 IMF Press Briefing. July 15, 2021. <https://www.imf.org/en/News/Articles/2021/07/15/tr071521-transcript-of-imf-press-briefing>

13 Kristalina Georgieva’s Speech. August 4, 2021. <https://www.imf.org/en/News/Articles/2021/08/04/sp080421-MD-remarks-Lebanon-conference>

### 3

## Past experiences of SDR uses for fiscal purposes

The next section presents successful experiences that took advantage of SDRs as fiscal resources. Due to unawareness, or acting on advice from external entities, the vast majority of countries did not incorporate SDRs in their fiscal budgets.

In the first nine months of the SDR allocation after 2009, only 18 of the 186 countries used more than 50% of their allocation. The countries that used these SDRs were: Armenia, Bosnia and Herzegovina, Cameroon, Chad, Central African Republic, Ecuador, Eritrea, Guyana, Mauritania, Moldova, Myanmar, Papua New Guinea, Serbia, Sri Lanka, Saint Vincent, Ukraine, Vanuatu, and Zimbabwe. Among these, according to available information and a report from the US Treasury Department based on reports from the International Monetary Fund, **we know that at least the following countries used them for fiscal purposes: Ecuador, Bosnia and Herzegovina, Mauritania, Moldova, Serbia, Ukraine and Zimbabwe**<sup>14</sup>. None of these countries has been sanctioned or belittled for making a fiscal use of SDRs.

Sri Lanka, Ecuador, Guyana and Moldova were the first countries to exchange their SDRs for dollars. As can be seen from this list of countries, the dollarized monetary regime was not a special-case condition for the SDRs to be used for fiscal purposes, so some analysts have claimed.

In the then current IMF programs with Romania, Hungary, Turkey, Pakistan, and Iceland, SDRs were recorded exclusively as reserve assets and were not used for fiscal purposes. In the case of Romania and Hungary, the IMF staff reports clearly establish that it was the countries that decided to give the SDRs this accounting treatment. Ukraine, which also had an ongoing program with the IMF, did use the SDRs for fiscal purposes because the IMF delayed disbursements for Ukraine. The IMF considered that the use of SDRs for budgetary purposes alleviated Ukraine's situation<sup>15</sup>.

### 3.1 Ecuador 2009

In the 2009 issuance, Ecuador received the equivalent of USD 402.45 million. These resources were deposited in the account of the Ministry of Finance. In this section we will review the legal and accounting procedures that were required to carry out this operation.

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14 According to the Treasury Department report to the US Congress. August 2010. <https://www.treasury.gov/about/organizational-structure/offices/International-Affairs/Documents/Report%20to%20Congress%20on%20SDR%20Use%20--%20August%202010.pdf>

15 Ukraine: Ex Post Evaluation of Exceptional Access Under the 2008 Stand-By Arrangement. IMF. November 2011. <https://www.imf.org/external/pubs/ft/scr/2011/cr11325.pdf>

The decision to issue SDRs was made by the IMF's Board of Governors. Ecuador's representative to the Board of Governors is the Ministry of Finance. Ecuador voted in favor of the issuance of the SDR. After the decision but before the SDRs were allocated and monetized, the Ministry of Finance, in its capacity as representative of the Republic of Ecuador, sent an official letter<sup>16</sup> to the Central Bank of Ecuador (BCE). In that letter, the Ministry stated that **“member countries”** are the ones who have the “right to receive an allocation from the SDR issuance”. The Ministry requested “on behalf of the Republic of Ecuador” that the central bank to follow “the processes that make it possible for, once the SDRs had been monetized, transfer” **to the Ministry of Finance's account at the Central Bank**<sup>17</sup>.

The IMF informed all member countries, via their central banks, that the SDRs had been allocated. In response to this communication, via SWIFT messages, the Central Bank of Ecuador immediately requested the IMF's SDR Department to exchange the SDRs for dollars. Once the transaction was executed, the Central Bank credited the corresponding amount in the Ministry of Finance's checking account.

The Ministry of Finance **registered the equivalent amount in dollars in the general government budget** as capital income<sup>18</sup>. As part of the budget revenue, they were used to finance fiscal expenditures.

Accounting wise, the Central Bank recorded the new SDRs in the assets of the BCE and the equivalent amount in dollars in the account of the Ministry of Finance. After the exchange, the SDR assets decreased and cash assets increased, incurred a commitment to pay quarterly interest to the IMF's SDR Department. From then on, the IMF debits the balances of Ecuador in the SDR Department every three months<sup>19</sup>. The Central Bank has not recorded the principal corresponding to the SDRs exchanged on the liability side of its balance sheet.

Purely for statistical purposes<sup>20</sup>, as of January 2019, the total amount of SDRs, both from the 2009 issuance and the previous ones, is recorded as if they were external debt, even though repayment of the principal is not mandatory.

### 3.2 Paraguay 2021

On June 23, 2021, the Paraguayan government presented in Congress a bill to establish economic measures to deal with the pandemic crisis. The bill has already received half a sanction from the Senate.

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16 Oficio MEF-DM-2009-0253 DM 029 from August 25, 2009.

17 This is the path described in section 4.1.

18 Budget item 280106 Capital income from public financial entities.

19 In the BCE budget there is a record of commissions paid as “Charges for SDR allocations IMF USD-DSBI UIO”: <https://www.bce.ec/images/transparencia2021/financiera/gastosdiciembre2020.pdf>

20 Resolution No. MEF-2018-0134. [https://www.registroficial.gob.ec/index.php/registro-oficial-web/publicaciones/registro-oficial/item/download/10595\\_6ff4ee6719a70843ce6bfcdba562fb5a](https://www.registroficial.gob.ec/index.php/registro-oficial-web/publicaciones/registro-oficial/item/download/10595_6ff4ee6719a70843ce6bfcdba562fb5a)



The bill provides that “The Special Drawing Rights, to be allocated by the International Monetary Fund **to the Republic of Paraguay**, to cover the financing needs derived from the COVID-19 Pandemic, **will be allocated to the account of the public treasury as a financial asset**”<sup>21</sup>.

Additionally, it establishes that this allocation happens as an “exception to the provisions of Article 60 of Law No. 489/1995 ‘ORGANIC OF THE CENTRAL BANK OF PARAGUAY’”. Article 60 defines the composition of international monetary reserves in charge of the central bank; among them are the SDRs. **This exceptionality is unnecessary**, but it is included to provide greater legal certainty to the Central Bank of Paraguay.

Complementarily, the bill empowers the central bank to advance up to USD 250 million to the government while the SDRs arrive. Said advance would be authorized exceptionally as a national emergency.<sup>22</sup> Due to the time of expected approval of the law with regards to the issuance of the SDRs, such an advance will not be necessary.

The accounting treatment is also described in the bill: “**The Ministry of Finance may use, partially or totally, the financial resources** obtained through the operations and transactions authorized in article 35, which must be registered in the **government accounting** ... the **Ministry of Finance will be responsible for the payment of financial commitments that may arise...**”.



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21 File number S-211723. <http://silpy.congreso.gov.py/expediente/123761>. This is the path described in section 4.1, although according to our criterion, a law is not required. Lebanon is considering using the path described in section 4.1: Lebanon’s IMF SDRs: let us not waste another billion dollars! Kulluna Irada. [http://kullunairada.s3.amazonaws.com/issues/663\\_1626764403\\_ki\\_note\\_sdrs\\_en.pdf](http://kullunairada.s3.amazonaws.com/issues/663_1626764403_ki_note_sdrs_en.pdf). A group of Argentinian senators urged the government to use SDRs for fiscal purposes. La Política Online. <https://www.lapoliticaonline.com.ar/nota/133636-los-senadores-le-exigen-a-guzman-gastar-en-la-pandemia-los-usd-4-350-millones-que-girara-el-fmi/>.

22 This is part of the path covered in section 4.4.

## 4

# Legal-accounting paths for the use of SDRs for fiscal purposes

The next section presents four different paths to achieve the goal of using SDRs for fiscal purposes.<sup>23</sup> The first is for the finance ministry, on behalf of its country, to receive the SDRs and deposit the exchanged amount at the central bank. The second replicates the mechanism used by the US: that the ministry receives the SDRs and issues SDR certificates for the central bank to hold. The third is for the central bank to pay the equivalent amount in SDRs to the ministry as a dividend. And the fourth is for the central bank to grant financing to the ministry for an indefinite term, for an amount equivalent to that of the SDRs received. Details are presented below.

### 4.1 SDRs belong to the member country, not the central bank

The first path for SDRs to be incorporated into fiscal budgets has to do with the hierarchy of norms, known as the Kelsen pyramid. The Articles of Agreement of the IMF is an international treaty, which takes precedence over national legislation. Nowhere in the Articles of Agreement of the IMF does it say that SDRs be exclusively managed by central banks. In fact, articles XV.1 y XVII.1 of the Articles of Agreement expressly define<sup>24</sup> “member countries” as the entities that are the beneficiaries of SDRs. **The representation of the sovereign -in monetary or financial matters- usually corresponds to the ministries of finance. In fact,** the IMF frequently disburses loans to the ministries of finance rather than to the central banks.



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23 By no means is it proposed that central banks should reduce their roles in managing liquidity and contribute to regulate inflation once the government has decided to use the SDR-linked resources for fiscal purposes.

24 IMF Articles of the Agreement. <https://www.imf.org/external/pubs/ft/aa/index.htm>



## Articles of Agreement of the International Monetary Fund

### Article XV

#### Special Drawing Rights

##### Section 1. Authority to allocate special drawing rights

(a) To meet the need, as and when it arises, for a supplement to existing reserve assets, the Fund is authorized **to allocate special drawing rights in accordance with the provisions of Article XVIII to members** that are participants in the Special Drawing Rights Department.

(b) In addition, **the Fund shall allocate special drawing rights to members** that are participants in the Special Drawing Rights Department in accordance with the provisions of Schedule M. (...)

### Article XVII

#### Participants and other holders of Special Drawing Rights

##### Section 1. Participants

Each **member** of the Fund that... undertakes all the obligations of a participant in the Special Drawing Rights Department in accordance with its law and that it has taken all steps necessary to enable it to carry out all of these obligations **shall become a participant in the Special Drawing Rights Department** (...)

In general, the monetary legislation of countries contains a definition with a list of the types of assets that make up international reserves. The list includes gold, foreign exchange and SDRs. This list of assets is misused by central bank officials or by analysts linked to financial capital to argue that the SDRs belong to the central bank, since they are part of international reserves. This argument does not hold: there is foreign exchange deposited in the central bank and this does not mean that the central bank was the prior owner of that foreign exchange. Same case with gold. The fact that the SDRs held by the central bank are part of the central bank's liquid assets does not mean that the original owner of the SDRs is the central bank.

A central bank is generally the fiscal agent of the Republic. In other words, it is the bank where the finance ministry manages its resources. This does not mean that the central bank substitutes the Republic or the finance ministry.

Prior to the arrival of the allocated SDRs, the finance ministry, **on behalf of the member country, must officially notify its central bank that, when the SDRs arrive, they be credited in favor of the ministry** and that the corresponding accounting and financial procedures be executed by the central bank. This does not differ from what currently occurs when, for example, the IMF grants a loan to the ministry: the ministry anticipates to the central bank that a loan will arrive and instructs to which account these resources must be credited.

Only in the adverse political scenario that the central bank has an opposing political position, the ministry should reaffirm its position with binding legal opinions that sustain the primacy of the Articles of Agreement of the IMF over secondary norms interpreted by the central bank. If necessary, a regulation may be issued to clarify that SDRs are property of the Republic and not of the central bank. This in no way alters the role of the central bank as fiscal agent, including with regard to the SDRs.

### **If SDRs were gold bars**

In order to be even clearer, we present an illustrative example. Let's imagine that SDRs are bars of gold. Before the bars are shipped, the finance ministry realizes that it does not have a vault and contacts the central bank to indicate that it is going to deposit those bars. The central bank accepts the deposit, but accounting rules prevent it from denominating deposits in ounces of gold; once the ministry deposits the bars, the value in dollars (or in national currency) of the gold deposited will be recorded in the account. The ministry of finance's account increased its balance. As gold - by law - is an international reserve asset, the central bank's international reserves have also increased.

At this point, the ministry, which was the holder of the gold, has ceased to be so, but is now the holder of dollars (or local currency) in an amount equivalent to the gold deposited. Aware that now it has more money, the ministry decides to buy vaccines. The central bank needs to sell that gold in the international market in order to get dollars and make international transfers on behalf of the ministry.

Just as it happens with gold bars, the same goes for SDRs. Initially they are owned by the country (ministry of finance). When the SDRs arrive (via electronic messages) at the central bank, the ministry requests that the corresponding amount in dollars or national currency be credited to the account that the ministry has at the central bank. From then on, the ministry will be able to dispose of that money.

## **4.2 Exchange Stabilization Fund SDR Certificates**

A second path to incorporate SDRs into the budget could be the establishment of a fiscal or parafiscal instrument identical to the Exchange Stabilization Fund (ESF) of the US Department of the Treasury<sup>25</sup>. In the case of the US, it is the Treasury's fund that is the direct holder of the SDRs.

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25 ESF Audited Financial Statements. <https://home.treasury.gov/system/files/206/ESF-Annual-Audit-FY2020.pdf>

Once the SDRs are received, the ESF issues securities denominated in SDRs, called “SDR certificates”. The ESF sells these securities to the Federal Reserve Bank of New York (NY Fed). Following this transaction, the ESF receives dollars in its account at the NY Fed and the NY Fed remains the holder of the SDR certificates.

This design can be replicated in any other country. However, domestic monetary legislation can become an impediment to opting for this path. While no legal reform is required for ministries to be the original recipients of SDRs, it will most likely need a legal reform or legal interpretation to allow ministries to issue SDR certificates that are to be acquired by the central bank.

In this way, the ministry could have liquidity from the central bank denominated in foreign or local currency to carry out budget expenses. In this scenario, the original SDRs are not exchanged abroad.

Beyond the institutional-accounting design of the ESF, this shows us that there is no international law that prevents a ministry (and not necessarily the central bank) from being the direct holder of the Special Drawing Rights. In that respect, the design of the ESF is identical to the Exchange Equalization Account of the UK Department of the Treasury and the Exchange Fund Account of the Canadian Department of Finance.

### **4.3 Dividend based on extraordinary income**

A third path to incorporate SDRs into the budget is through a sequence of accounting steps. If the path of legal hierarchy or the issuance of a fiscal instrument similar to that issued by the Exchange Stabilization Fund does not prosper, or if there is political objection from the national central bank to opt for such paths, there are more options.

If the national central bank insists on an incorrect but common legal argument that the SDRs are assets and exclusive property of the central bank and not of the Republic, then when the SDRs are credited there will be a significant increase in the equity of the central bank.

According to current monetary laws, the central bank’s profits at the end of the year are transferred to the ministry of finance given that, in the vast majority of cases, the central banks are entirely state-owned.

Therefore, the central bank’s accounting must record such an equity increase as a consequence of extraordinary income in the central bank’s income statement, in such a way that, by the end of 2021, an equivalent net income can be transferred, as a dividend, to the Ministry of Finance for fiscal year 2022.

If there is the will, an agreement can be made between the central bank and the ministry of finance to make a dividend advance in September 2021.

## 4.4 Monetary financing

A fourth path would imply that the central bank refuses to recognize that SDRs are property of the republic and that it would not be willing to record them as income in its budget. This scenario is almost implausible, but in central banks with a tradition of misunderstanding autonomy, or at the suggestion of certain external entities, it is unfortunately possible.

There remains a mechanism: financing from the central bank to the finance ministry. Through commonly used monetary financing mechanisms, central banks can purchase securities issued by ministries of finance.

In this case, the central bank would receive the SDRs on the asset side of its balance sheet and increase its equity. The central bank would then buy securities from the finance ministry in dollars or in national currency for the amount equivalent to the SDRs received. The combination of these transactions would increase the international reserves of the central bank and also increase the internal assets of the central bank. The finance ministry would be indebted to the central bank. Since SDRs are indefinite, the debt between the finance ministry and the central bank could also be indefinite. Interest rates on those funds should not be more onerous than what the SDR department charges.



## 5

### External debt statistics methodology

One of the significant changes in the Sixth Manual of Balance of Payments Statistics of the International Monetary Fund had to do with the definition of public debt.

Before, debt was defined as a commitment to repay principal and interest in the future. With the new version of the statistical manual, it is defined as a commitment to repay capital or interest in the future.

Given that according to the Articles of Agreement of the IMF, the principal of the SDRs can remain unpaid indefinitely, except if the country leaves the IMF, **in the real world, the SDRs are not debt**. But because of this unlikely and unfeasible exception, the statistical manual recommends that it be included in statistical publications as debt.

When SDRs are exchanged for dollars, a liability does arise. Although there is no legal obligation to repay the dollars to return to SDRs, the country that holds a deficit position of SDRs with respect to the originally allocated amount, must pay interest on a quarterly basis. As principal does not have to be repaid, but interest must be paid, according to the new definition, it is argued that it should be included in the statistics as debt.

In any case, the **Manual of Balance of Payments Statistics has no legal or binding force**. The countries decide the financial-accounting treatment that they want to give to the SDRs regardless of the statistical treatment. According to International Financial Reporting Standards, the original allocation of SDRs cannot be recorded as liabilities of the central bank<sup>26</sup>. The principal of the exchanged SDRs should not be recorded as a liability either. However, the interest corresponding to the SDR Department should be recorded as an account payable.



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26 Please see Notes to the Central Bank of Ecuador's Financial Statements. pp. 14, 41, 52. [https://www.bce.fin.ec/images/transparencia/informacion\\_financiera/documentos/estadosfinancieros/nef2020.pdf](https://www.bce.fin.ec/images/transparencia/informacion_financiera/documentos/estadosfinancieros/nef2020.pdf)



## 6

# Conclusions

This handbook has provided sufficient technical knowledge to government authorities on the legal, financial and accounting steps for the use of Special Drawing Rights for fiscal purposes. The main conclusion is that **there is no obstacle for the SDRs to contribute to the fiscal budget. It is essential, however, that the governments of the countries receiving the SDRs act promptly.**

The past experiences of the 2009 issuance documented by the IMF in European, African and Latin American countries are evidence that it is possible for SDRs to be used for fiscal purposes. It was not a special case related to the dollarization monetary regime in Ecuador. The institutional designs of the United States, Canada, and the United Kingdom demonstrate that there is no international restriction for ministries to be holders of SDRs. Paraguay is already acting in advance, with an unnecessary law, but on the right track. The Lebanese treasury will receive the resources as well, apparently with no need for legislative amendments.

In case central banks insist SDRs are their exclusive property, conventional accounting standards allow SDRs to be recorded as extraordinary income in the central bank's income statement and to subsequently transfer the equivalent dividend to the ministry. As a last resort, the central bank can provide internal financing to the ministry through conventional instruments.

The most specific destination of spending, understood as investments in health, care or payments of debt, corresponds to each country according to its needs, priorities and current legislation. Beyond the legal or accounting details, it is imperative that countries become aware of the real possibility of using these resources to save lives and foster a social recovery, in the worst economic crisis of the last hundred years.



