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GUIDANCE NOTE FOR THE FUND'S POLICY ON MULTIPLE CURRENCY PRACTICES

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GUIDANCE NOTE FOR THE FUND'S POLICY ON MULTIPLE CURRENCY PRACTICES

EXECUTIVE SUMMARY

The new policy on multiple currency practices (MCPs), effective February 1, 2024, is a cornerstone of the Fund's legal and policy framework for exchange rates. The MCP policy elaborates on the provision in Article VIII, Section 3 of the IMF's Articles of Agreement ("Articles") which prohibits member countries from engaging or permitting their fiscal agencies (as defined in the Articles) to engage in MCPs unless authorized under the Articles or approved by the Fund. The policy was comprehensively reviewed in 2022 to take stock of the experience with its implementation since the 1980s and was modified to reflect the developments in foreign exchange markets since then. The main changes in the new policy focus on three areas: (i) an MCP will arise due to an official action that segments foreign exchange (FX) markets or increases or subsidizes the cost of certain FX transactions (e.g., exchange taxes), (ii) MCPs will be identified on the basis of a new country-specific market-based rule, and (iii) the new policy ensures better alignment of the MCP policy with other relevant IMF's policies.

This note provides operational guidance to staff, particularly country teams, on monitoring members' compliance with the new MCP policy by identifying impermissible exchange rate spreads that arise due to official actions and, thus, give rise to MCPs. It also provides guidance to staff on the criteria and processes for approval and removal of MCPs, modalities of engagement with the authorities, coverage of MCPs in country surveillance and program documents, and the relationship between the MCP policy and other relevant IMF policies.

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Glossary

AC	Assessment Criterion
AIV	Article IV
BPA	Bilateral Payments Arrangement
BOP	Balance of Payments
CB	Central Bank
CD	Capacity Development
CFM	Capitol Flow Management Measure
CMR	Cash Margin Requirement
DCA	Discriminatory Currency Arrangements
ECF	Extended Credit Facility
EFF	Extended Fund Facility
ERGS	Exchange Rate Guarantee Scheme
FCL	Flexible Credit Line
FX	Foreign Exchange
GDP	Gross Domestic Product
H/L	High/Low
IOSCO	International Organization of Securities Commissions
ISD	Integrated Surveillance Decision
IV	Institutional View on the Liberalization and Management of Capital Flows
LOI	Letter of Intent
MEEP	Memorandum of Economic and Financial Policies
MCP	Multiple Currency Practice
NDF	Non-Deliverable Forward
PC	Performance Criterion
PCI	Policy Coordination Instrument
QT	Quantitative Target
RCF	Rapid Credit Facility
RFI	Rapid Financing Instrument
RSF	Resilience and Sustainability Facility
SBA	Stand-By Arrangement
SLL	Short-term Liquidity Line
SMP	Staff-Monitored Program
SR	Staff Report
TA	Technical Assistance
TMU	Technical Memorandum of Understanding
UFR	Use of Fund Resources
URR	Unremunerated Reserve Requirement
WTO	World Trade Organization

INTRODUCTION

1. The policy on Multiple Currency Practices (MCPs) is a key element of the IMF's jurisdiction over the exchange rates. The Articles include an original provision (Article VIII, Section 3) stating that the IMF's member countries should refrain from engaging, or permitting their fiscal agencies (as defined in Article V, Section 1) to engage in MCPs, unless authorized under the Articles or approved by the IMF.[1,2] This provision is included in the Articles because MCPs can create distortions, impede trade and investment, and give a Fund member an unfair competitive advantage over other members (see Box 1). While the Articles introduced the concept of MCPs, they do not provide a specific definition. For this reason, the Executive Board has historically developed policies on MCPs that include a definition and has also adapted such policies to changing economic realities.

2. The new MCP policy,[3] effective February 1, 2024, reflects the significant changes in FX markets and in FX policies since its last review in the 1980s. The review aimed to make the policy and its application more relevant by adjusting it so that it continues to address policy actions that are objectionable but does not discourage good practices in FX markets. The review better aligned the MCP policy with other related Fund policies, most notably, the policy on exchange restrictions and the *Institutional View on the Liberalization and Management of Capital Flows* (IV).[4]

3. This note provides guidance to staff on the implementation of the MCP Policy. Elaborating on the two Board papers, Section II covers the definition of an MCP, including official action that can give rise to an MCP, and the methodology for measuring and identifying impermissible spreads. This section is complemented by Annexes II and V as well as a forthcoming monitoring tool and provides operational details to help staff and authorities to monitor exchange rates using the methodology. Section III elaborates on how MCPs are identified and their consequences and discusses engagement between the authorities and the IMF. Section IV discusses members' rights and obligations with regard to MCPs and provides guidance on the policies and operational considerations for the approval and removal of MCPs. Section V provides guidance to Fund staff on different stages of MCP assessments. Section VI clarifies the treatment of MCPs in the context of the use of Fund resources, including Fund arrangements and nonfinancial instruments.

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[1] Article VIII, Section 3 of the IMF's Articles of Agreement provides that "*[n]o member shall engage in, or permit any of its fiscal agencies referred to in Article V, Section 1 to engage in, any discriminatory currency arrangements or multiple currency practices [….] except as authorized under this Agreement or approved by the Fund*".

[2] Fiscal agencies of a member referred to in Article V, Section 1 of the IMF's Articles of Agreement are "*its Treasury, central bank, stabilization fund, or other similar fiscal agency*". The intention of this provision is that all parts of the member government, and, in particular, its various financial entities, should refrain from engaging in the proscribed behavior. The parts of the government covered are those that exercise governmental authority as commonly understood. See "Legal Aspects of Multiple Currency Practices Under Second Amendment" in SM/79/127 of May 15, 1979, page 17.

[3] The new MCP policy is laid out in policy papers "Review of the Fund's Policy on Multiple Currency Practices—Initial Considerations" (2019) and "Review of the Fund's Policy on Multiple Currency Practices—Proposals for Reforms" (2022).

[4] See "Liberalization and Management of Capital Flows: Institutional View" of 2012 and "Review of the-Institutional View on the Liberalization and Management of Capital Flows" of 2022.

Section VII discusses the relationship between the MCP policy and other Fund policies such as the policy on exchange restrictions and the IV. The final section provides guidance on the coverage of MCPs in staff reports.

Box 1. Why Does the Fund Need an MCP Policy?

The MCP policy is a cornerstone of the legal and policy framework for the Fund's jurisdiction over exchange rates. The term "multiple currency practice" is a misnomer. It is not concerned with the maintenance of more than one currency on a member's territory, but with the maintenance of multiple exchange rates on a member's territory. The obligation of member countries to refrain from engaging in MCPs is an original provision of the Articles. It has promoted the objective of maintaining orderly exchange arrangements and unified exchange rates.

The Fund's Articles prohibit members from engaging in MCPs in certain circumstances but do not define the term. They allow the Executive Board, through interpretation and by decision, to give content to the term through the MCP policy. While the content of the policy can be modified to reflect changing realities, the Fund cannot decide not to apply it. Given that the Articles prohibit members from engaging in MCPs, unless otherwise authorized therein, the Fund must apply this provision and enforce compliance with this obligation by its members.

The prohibition of MCPs was part of a larger effort by the Fund to eliminate restrictions on current international payments and transfers after the destructive trade wars of the 1930s. During this period countries frequently established different rates of exchange for selected commodities to stimulate exports and suppress imports. To preserve scarce supplies of FX, countries also concluded BPAs with each other using exchange rates that did not reflect market conditions. These measures disrupted trade, increased economic difficulties, and stimulated destructive spillovers and retaliatory measures between countries.

MCPs have historically been used for two main purposes. First, as an attempt to mitigate BOP pressures, including those associated with capital flow volatility, and, at least temporarily, to reduce pressure to tighten monetary policy while protecting the BOP during financial distress, where there may be a destabilizing transmission of external shocks to domestic activity. Second, to achieve non-BOP objectives—such as revenue mobilization or allocation of resources to specific entities or sectors—without having to resort to more direct methods of taxation or subsidies. As MCPs can, in some cases, be adopted by executive order or central bank regulation, they have often been used instead of other measures that require legislation.

However, MCPs are typically not the most effective or efficient means of achieving these objectives. They do not address fundamental reasons leading to BOP imbalances and only delay the impact of BOP pressures. When used for non-BOP purposes, MCPs tend to introduce unintended inefficiency in resource allocation and are less transparent than direct taxes or subsidies provided through the budget. MCPs can also invite rent-seeking behavior from interest groups pressing for favorable treatment.

Moreover, MCPs distort relative prices and domestic resource allocation, particularly over the medium and long term. Evidence suggests that MCPs have had adverse effects in the medium and long term, especially where these systems become a more permanent part of a country's exchange arrangement. MCPs have brought about expenditure reduction through implicit taxation, as well as expenditure switching through explicit changes in relative prices. For instance, an exchange rate spread that acts as a tax on exports and a subsidy on basic imports can undermine a country's exports and encourage the growth of inefficient import-substituting industries, resulting in resource misallocation and a loss of economic growth and job creation. MCPs have generally been associated with lower GDP growth, higher inflation, and lower trade volumes. Country experiences also confirm that MCPs can distort the current account because of asymmetric effects on imports and exports, although, given that countries that use MCPs tend to be in generally challenging macroeconomic situations, it is difficult to establish causality between MCPs and

Box 1. Why Does the Fund Need an MCP Policy? (concluded)

macroeconomic performance. In addition, MCPs may be considered a discriminatory trade practice, since, by acting de facto as a differentiated tariff, they can create competitive advantage, hamper international trade, and prompt retaliatory measures (for example, MCPs arising from export subsidies or exchange taxes are generally prohibited under the WTO[1] legal framework). Some MCPs, such as taxes on the purchase of FX for the remittance of profits, may also deter foreign investment.

The MCP policy provides a strong deterrent against the emergence of distortive exchange practices. The policy has contributed to a substantial decline in MCPs over the last few decades, especially among large countries. In its absence, there would be less protection against a re-emergence of exchange practices that undermine trade and investment.

[1] MCPs are also relevant under other legal frameworks, such as the World Trade Organization (WTO). MCPs arising from export subsidies or exchange taxes are generally prohibited under the WTO legal framework. However, if an MCP is maintained by a country in accordance with its obligations under the IMF Articles of Agreement, i.e., it is temporarily approved by the Fund under Article VIII or maintained under the transitional arrangements of Article XIV, it would not be subject to discipline under the WTO legal framework. For more details, see "Review of the Fund's Policy on Multiple Currency Practices—Initial Considerations—Historical Development and Legal Framework of the MCP—Background Paper I" in SM/18/208, Supplement 1, of August 15, 2018.

WHAT IS AN MCP? DEFINITION

4. Article VIII, Section 3 prohibits members from engaging in MCPs, but it does not define an 'MCP'. Rather, this definition is established through decisions of the IMF Executive Board. Executive Board Decision No. 17292-(22/63), adopted on July 1, 2022, defines the MCP as follows:

> "As a general principle, Official Action should not cause exchange rate spreads to differ unreasonably from those that arise from the normal commercial costs and risks of exchange transactions. Therefore, a multiple currency practice would arise in the circumstances set forth in this paragraph 1.
>
> a. Official Action causes an Effective Exchange Rate for a Spot Exchange Transaction to exceed the Spot Permissible Spread.
>
> b. Official Action causes an Effective Exchange Rate for a Non-spot Exchange Transaction to exceed the Non-spot Permissible Spread.
>
> Notwithstanding the above, a multiple currency practice would not arise if the Effective Exchange Rate for an Exchange Transaction caused by Official Action is calculated as follows:
>
> (i) the Effective Exchange Rate is derived solely from the weighted average of transaction exchange rates in a member's wholesale foreign exchange market or, in the absence of a wholesale foreign exchange market, as the weighted average of the transaction exchange rates between intermediaries and their clients, or a

combination of the two if the wholesale foreign exchange market is not representative of the member's foreign exchange market, and

(ii) the only transactions included in the calculation of the Effective Exchange Rate occurred on the business day immediately preceding the day on which such Effective Exchange Rate is to be used."

Since only exchange spreads arising from official action of the member or its fiscal agencies can give rise to MCPs, an exchange spread that arises without official action does not give rise to MCP.

5. In light of the above definition, an MCP would arise if all the following conditions are met:

- *An "official action" that segments* the member's FX market or increases or subsidizes the costs of certain FX transactions (e.g., an exchange tax or subsidy) has been taken by the authorities.
- *The official action relates to an "exchange transaction",* i.e., transaction whereby the currency of one member is exchanged for another member's currency.[5] Based on the global financial market standards for settlement dates, the policy distinguishes between spot and non-spot transactions (as discussed in paragraph 14).
- *The exchange transaction takes place on the territory of the member engaging in the official action.* This includes not only the member's metropolitan territory, but also any other territories of the member.[6] Exchange transactions that take place in offshore FX markets are not considered exchange transactions for the purposes of the MCP policy.[7]
- *The official action results in an actual exchange rate spread that* differs unreasonably from the normal commercial costs and risks of exchange transactions (exchange rate spreads which are not considered "commercially reasonable"), i.e., exceed the permissible margins,[8] specified in the MCP policy. A single such deviation is sufficient for an MCP to arise.

A. Official Actions That Can Give Rise to MCPs

6. The concept of official action, i.e., action taken by the authorities, is a core element of the MCP policy. Official action encompasses:

[5] See "Review of the Fund's Policy on Multiple Currency Practices—Proposals for Reform—Proposed Decision" in SM/22/129, Supplement 1, of June 27, 2022. A member may adopt another member's currency as its own.

[6] See "Review of the Fund's Policy on Multiple Currency Practices— Initial Considerations" in SM/18/208 of August 15, 2018, ("Initial Considerations").

[7] While most exchange transactions happen on-shore, currencies can also be traded off-shore either for convenience (e.g., the most traded currencies such as the euro, the dollar, the Japanese yen, and others outside of on-shore market business hours) or due to restrictions imposed by the FX regulation.

[8] In this Guidance Note, the terms "permissible spread" and "permissible margin" are used interchangeably.

(i) any action by the authorities that segments FX markets and results in an exchange rate being available only for (a) a specific intermediary and/or end-user or a limited group of intermediaries and/or end-users and/or (b) for a limited range of purposes, and

(ii) any action by the authorities that increases or subsidizes the cost of certain FX transactions (e.g., an exchange tax or subsidy).

For purposes of the MCP policy the term "authorities" refers specifically to the member itself or any of its fiscal agencies referred to in Article V, Section 1 of the Articles (i.e., the Treasury, central bank, stabilization fund, or other similar fiscal agency).

Exchange rates used in such exchange transactions will be assessed according to the methodology (as outlined later in this section), and an MCP would arise if the transaction exchange rate is outside of the permissible margins.

7. Official actions that may result in MCPs include but are not limited to:

- *Direct engagement in foreign exchange transactions by the authorities*, for instance, central bank's FX transactions with the government, or FX transactions conducted by the authorities at a particular exchange rate with selected wholesale FX intermediaries or end-users, or for specific purposes (i.e., earmarked transactions) results in a segmentation of the FX market and are considered official action.[9] The authorities often sell and purchase foreign exchange through FX auctions; the treatment of FX auctions is explained immediately below and in paragraph 8.

- *Multiple—and single—price foreign exchange auctions* that segment the FX market. While a FX auction would generally be considered as official action when it is established or operated by the authorities (e.g., the central bank), FX auctions organized according to best practices (described in paragraph 8) are not considered to segment the FX market.

- *Official actions bringing about a multiplicity of exchange rates* at which market participants can make exchange transactions, for instance, establishing different exchange rates for different transactions conducted by market participants, dual and multiple legal FX markets in a single jurisdiction, or bilateral payment arrangements that provide for the use of a special exchange rate for covered transactions.[10] Dual and multiple exchange markets that are segmented due to official action, such as, for example, capital controls applying to one FX market but not another

[9] When the authorities purchase foreign currency, this also applies if the purchase is from specific segments, i.e., selected intermediaries, sources, or FX sellers.

[10] Central banks may enter into agreements to settle current transactions (e.g., imports and exports) between the two or more countries on pre-defined dates at specific exchange rates. It has been the practice of the Fund to assess agreements between central banks that are structured as bilateral payment agreements to determine whether they are consistent with the members' obligations under Article VIII, Section 2(a) and 3 of the Articles of Agreement (see Annex III).

on the member's territory, may result in an exchange spread on exchange transactions with a member's currency in different segments of the member's exchange market.

- *Direct imposition of costs/provision of subsidies on FX transactions*, for instance, exchange taxes, exchange rate guarantees schemes provided by the authorities, or other mandatory costs and subsidies. The new MCP policy broadly provides continuity for the treatment of exchange taxes, and other costs and subsidies imposed by official action. However, their treatment under the new policy differs depending on whether they are imposed on exchange transactions using market exchange rates or exchange transactions where the exchange rate is determined by official action. (See paragraph 16 and Annex I).

- *There could be other examples of official actions, too.* Official action can take more subtle forms, like *informal guidance or moral suasion* that influences the exchange rate and causes impermissible spreads.[11]

8. The following official actions will <u>not</u> give rise to an MCP:

- *FX transactions between the authorities and FX intermediaries, which do not segment the FX market*. Consistent with Fund's long-standing practice, FX transactions by the authorities (other than FX auctions, discussed below), that are (a) open to all FX intermediaries in good standing either directly or indirectly through market markers; and (b) do not restrict the use of the foreign currency purchased by intermediaries to specific purposes or end-users, will not be considered as segmenting the FX market and, thus, will not give rise to an MCP.[12] Such FX transactions ("intervention") 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.[13,14]

- *FX transactions between the government and the central bank which do not segment the FX market*. Such transactions do not segment the market if they are conducted at market exchange rates.

- *Exchange rates used solely for evaluation or accounting purposes*, and not used for actual exchange transactions.

- *FX auctions, i.e., auctions for the purchase and sale of FX between the authorities and FX market intermediaries, which are not for earmarked purposes and organized in line with best practices.* FX

[11] In this case, staff would also rely on information from market participants and other third parties, and staff should be able to substantiate any evidence. These cases require the exercise of judgment.

[12] In the case of buying transactions, the central bank should not restrict its purchases of FX from specific segments, i.e., intermediaries, sources, or FX sellers.

[13] The term "intervention" as used in this Guidance Note is without prejudice to any concept of intervention in any other Fund policies.

[14] If FX transactions by the authorities take place only through FX auctions, the provisions of the MCP policy on FX auctions would apply.

auctions (single- or multi-priced) would not be considered to segment the market if all the following criteria are met:

(i) access to bid at the auction is granted to all intermediaries in good standing,[15] *in the country's wholesale FX market,*[16] *either directly or indirectly through market makers,*[17] *so that they can all sell or make purchases of FX for themselves and on behalf of their clients;*

(ii) the exchange rate of the bid submitted by participants is the only criterion used to determine allotment;[18] *and*

(iii) no constraints are imposed on the range or level of the exchange rates that can be submitted.[19]

If any of these criteria are not met, an MCP would arise if impermissible spreads can be observed from the FX auction, as determined under the methodology described below.

- *Spreads arising between exchange rates used in FX transactions in a member's formal FX market(s) and illegal parallel market(s).* Parallel markets will be considered "illegal" if transactions conducted in such markets are prohibited under national law.[20]

[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 requirements). The concept of "all intermediaries" means all intermediaries that are authorized to participate in exchange transactions in the member's territory.

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

[17] 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.

[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.

[19] 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.

[20] Illegal parallel markets are excluded from the scope of the new MCP policy, but these will continue to be captured, where relevant, under the Fund's policy on exchange restrictions. For example, in cases where the illegal parallel market arises from rationing, prioritization or other forms of official action that result in shortages of foreign exchange, restrictions on the availability of foreign exchange for the making of payments and transfers for current international transactions would be captured under the Fund's exchange restrictions policy (Article VIII, Section 2(a) of the IMF's Articles of Agreement). In addition, reasonable efforts should be taken by country authorities to eliminate such markets and staff should put a stronger emphasis on exchange restrictions in Fund surveillance. Staff should continue to (a) discuss illegal parallel markets in staff reports for Article IV consultations (and/or UFR staff reports), (b) identify exchange restrictions, if any, that give rise to them and their implications, and (c) identify how the underlying policies or distortions that fuel these markets can be removed. See Decision No. 1034-(60/27), adopted June 1, 1960.

- *Broken cross rates.*[21] The MCP policy reflects current realities and since broken cross rates have virtually disappeared, they are not considered as giving rise to MCPs.

- *Official exchange rates based on market exchange rates with one day lagged calculations.*[22,23] One day lagged official exchange rates are often used by the authorities, or are required by the authorities to be used, in FX transactions in countries with less developed FX markets when the authorities cannot compute market exchange rates before the close of the FX market due to unavailability of the relevant data during the day. In that regard for purposes of the MCP policy, official exchange rates computed using market exchange rates of the preceding business day will not give rise to an MCP, provided that: (a) the lagged official exchange rate is calculated as a weighted average of all transaction exchange rates in the wholesale FX market during the day/operating hours of the wholesale FX market and, in the absence of a wholesale FX market, as the weighted average of the exchange rates used in transactions between intermediaries and their clients (see paragraph 12 of Annex V) or a combination of the two if the wholesale FX market is not representative of the FX market; and (b) all the transactions included in the calculation occurred on the business day immediately preceding the day when the official exchange rate is to be used. If the lagged official exchange rate does not meet the above-mentioned criteria, staff will assess whether it gives rise to an MCP under the methodology described below.

B. Effective Exchange Rate

9. In identifying MCPs, the Fund examines the effective rate of exchange. This is the exchange rate that includes the nominal exchange rate (or when the nominal exchange rate is not determined by official action as described in paragraph 16, the mid-point of the High/Low range) plus the aggregate of any additional mandatory costs or subsidies (e.g., exchange taxes, commissions, fees, margin requirements) that are related to the exchange transaction closely enough to be considered as part of the effective exchange rate.[24] Whether an additional mandatory cost or subsidy is "so closely related to the exchange transaction as to be considered part of the

[21] "Broken cross rates" refers to the following provision of the 1981 MCP policy: "Action by a member or its fiscal agencies which results in midpoint spot exchange rates of other members' currencies against its own currency in a relationship which differs by more than 1 percent from the midpoint spot exchange rates for these currencies in their principal markets would give rise to a multiple currency practice. If the differentials of more than 1 percent in these cross rates persist for more than one week, the resulting multiple currency practice would become subject to the approval of the Fund under Article VIII, Section 3." See Executive Board Decision No. 6790-(81/43), adopted on March 20, 1981, as amended.

[22] Official exchange rates for this purpose are understood to include any exchange rate calculated by the authorities based on market exchange rates and published for market participants (e.g., a reference rate) if its use in FX transactions is mandatory.

[23] When calculating the official exchange rate for spot transactions, only exchange rates of spot transactions should be included. For this purpose, the spot leg of FX swap transactions does not fall in this category and should not be included.

[24] The notion of an "effective exchange rate" was discussed in "Legal Aspects of Multiple Currency Practices Under Second Amendment" in SM/79/127 of May 15, 1979, at page 13, and was further developed through the application of the MCP policy.

effective exchange rate" requires a comprehensive assessment based on all the relevant circumstances. In making this assessment staff should consider, among others, the nature of the measure under which the costs or subsidies are imposed, its effects, and the procedures followed for applying it. To be considered part of the effective exchange rate, the mandatory cost or subsidy should be sufficiently closely related to an exchange transaction and not to the underlying transaction, e.g., trade, invisible or capital transaction.

10. Examples of costs/subsidies arising from official action that have been considered to form part of the effective exchange rate for exchange transactions are the following:[25,26]

(a) **Exchange and other mandatory taxes and fees.** Taxes, other charges, or fees imposed by the authorities and levied on an exchange transaction are directly connected with the exchange transaction and this cost is considered to be part of the effective exchange rate. Examples include commissions and fees levied on the currency conversion conducted by the authorities (e.g., central bank sales of FX on which a commission or fee is charged) and commissions, fees and taxes on exchange transactions mandated by the authorities (e.g., taxes applied to the currency conversion for outward remittances and stamp duties levied on all currency conversions above a certain amount). Sometimes a tax or charge/fee is not levied directly on the currency conversion, but they may be so closely related to the currency conversion that they need to be considered as part of the effective exchange rate. Examples of such taxes could be transfer taxes, withholding taxes levied on payments abroad or receipts from abroad and financial transaction taxes. In those cases, it needs to be assessed whether an exchange transaction is an indispensable part of the payment or receipt and if the tax or other mandatory charge is so closely related to such an exchange transaction that it should be considered as part of the effective exchange rate despite the tax/charge/fee levied on the payment or receipt instead of the exchange transaction. The assessment is based on the specific circumstances and the manner the tax/charge is levied. For example, some income tax systems require the payor to withhold or pay income tax on any amount of income distributed to a non-resident, and the amount of the tax is often collected at the time when foreign exchange is purchased with which the payment is made. If the tax is withheld from all payments to non-residents, it has been considered to be solely an application of the income tax. If, however, liability for the tax is incurred only if the amount is to be remitted abroad, the tax, depending on the circumstances, could be considered as a part of the effective exchange rate and also as an exchange restriction. (See Annex I.)

[25] These examples are not exhaustive.

[26] Some measures have not been considered to be part of the effective exchange rate for the MCP assessment. For example, tariffs on the importation of goods, or taxes on contracts for goods and services have not been factored in to determine the effective exchange rate and have not been considered to give rise to MCPs, as they are not directly related to the purchase and sale of foreign exchange, although they increase the costs of the commercial transactions. Taxes/fees that are not closely related to an exchange transaction have also not been considered to constitute part of the effective exchange rate.

(b) **Import deposit and cash margin requirements.** Certain systems require an import deposit or cash margin deposit to be made before, for example, a letter of credit is opened or FX is purchased. If, as a result of the authorities' decision, interest on the deposits is not paid or is lower than the prevailing market interest rate, this results in a loss of interest that could be earned if the amount of the import deposit or cash margin deposit is deposited at a financial institution that pays market interest on such deposit. The lost interest is considered an additional cost of the FX transaction and should be considered as a part of the effective exchange rate for the exchange transaction related to, e.g., the import. See also Box 2.

(c) **Unremunerated reserve requirements (URR).** If the authorities require an URR (for example, at the central bank), and the URR is closely related to the exchange transactions on which it is imposed (for instance, the URR is on the purchase and/or sale of FX on non-spot basis), such requirement may give rise to an MCP.[27] In this case the unremunerated nature of the RR results in a loss of interest that could be earned if the amount of the URR is deposited at a financial institution that pays market interest on such deposit. The lost interest is considered as an additional cost of the FX transaction and should be considered as a part of the effective exchange rate of FX transactions that are subject to the URR.

Box 2. Further Considerations on the Calculation of the Effective Exchange Rate: The Impact of Higher Interest Rates and Inflation

The calculation of the effective exchange rate takes into account the opportunity cost in the case of certain official actions, for example, unremunerated import deposit and cash margin requirements (CMR) and unremunerated reserve requirements (URR), closely related to an exchange transaction.[1] Similar considerations apply in the case of reimbursable exchange taxes.

- The unremunerated nature of the CMR or URR results in a loss of interest that would be earned if the amount of the cash margin or URR were to be deposited at a financial institution that pays market interest on such deposit. The lost interest (opportunity cost) for the period of the mandatory cash margin or URR is an additional cost of the FX transaction and is added to the nominal exchange rate (or when the nominal exchange rate is not determined by official action, the mid-point of the High/Low range) to determine the effective exchange rate of FX transactions that are subject to the CMR or URR.
- When market interest rates rise dramatically (for instance when inflation suddenly increases), the official action that previously resulted in an effective exchange rate that remained comfortably within the permissible margins, may suddenly lead to an MCP. It is useful to be mindful that such changes may result in an MCP even if the official action itself remains unaltered.

[1] The considerations in this box apply also if the authorities mandate payment of interest rates at less than market interest rates.

(d) **Exchange rate subsidies.** For measures such as subsidies, it is necessary to examine the facts closely to establish whether a measure is applied exclusively to the underlying transaction (e.g., trade) or to the exchange rate used in the FX transaction. To determine if the subsidy should be considered as part of the effective exchange rate, it may be relevant

[27] If the URR applies to the underlying transaction, e.g., external borrowing, and not on the exchange transaction (or is not sufficiently closely related to the exchange transaction to consider it part of the effective exchange rate) the URR would not be considered under the MCP policy.

to determine if a subsidy is calculated on the amount of the FX received/purchased, or the amount of a subsidy is based on the amount of the export/import in quantitative terms. An indication that the subsidy should be part of the effective exchange rate could be that the provision of the subsidy is linked to changes in the exchange rate (e.g., the subsidy to exporters is provided when the exchange rate appreciates beyond a certain level). Another fact to be considered is whether the subsidy is paid on all exports of the goods or is paid only if FX is surrendered. In some cases, the trade and payment aspects may be so interlocked that a measure directly affects both.[28]

(e) **Exchange rate guarantees.** Exchange rate guarantees provided by official action can be considered as a subsidy of the rate that applies to exchange transactions covered by the scheme. The guarantee reduces the FX risks (and accordingly the costs) that are assumed with respect to future exchange transactions. When these schemes are akin to options or forwards, they will be analyzed as such and the effective exchange rate of the transaction under the scheme will be the aggregate of the market or theoretical option price and the strike price of the option, or the market or theoretical forward exchange rate respectively. Exchange rate guarantee schemes that are self-financed, but merely administered by the member, are not considered an official action under the MCP policy. In self-financed schemes, the FX risks are not subsidized by official action (e.g., by governmental funds) rather they are effectively pooled among the participants or subsidized by third parties.

(f) **Cost or subsidy arising from non-deliverable forwards (NDFs).** NDFs are transactions under which the parties settle the difference between the exchange rate of a forward purchase or sale of FX and the spot exchange rate at maturity in local currency. As NDFs do not involve an actual exchange of a member's currency for another member's currency, they would give rise to an MCP only if the NDFs (i) result from official action (e.g., entered into by central banks or other official entities, or by another party at their direction), (ii) are made available only to a specific intermediary/end-user or a limited group off intermediaries/end-users or earmarked for specific transactions, therefore segmenting the market, (iii) are closely related to acquiring or selling FX, and (iv) the effective exchange rate of such exchange transaction exceeds the permissible margins. The determination of whether an NDF would be considered to be closely related to the buying or selling of FX will be made based on the assessment of all relevant circumstances.[29] When 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 should be considered as part of the

[28] See "Legal Aspects of Multiple Currency Practices Under Second Amendment" in SM/79/127 of May 15, 1979.

[29] As an example, when a CB sells NDFs at a preferential rate to banks which need to buy FX to repay external FX loans for specific purposes, the subsidy arising from the NDF at preferential rate would be considered as part of the exchange rate at which banks buy FX.

effective exchange rate of the FX transactions to which the NDF is closely related.[30] All other NDFs are excluded from the policy.

C. Identifying Impermissible Spreads

11. The new MCP policy maintains the longstanding principle that an MCP arises 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). In assessing whether the "commercial reasonableness" standard has been met, the methodology provides that an MCP will arise where official action gives rise to an exchange rate for an exchange transaction that exceeds the permissible spread i.e., a country specific market-based norm and a tolerance margin. The exchange rate of the transaction that is assessed is the effective rate of exchange, as described in paragraph 9.

D. Methodology for Measuring Spreads

12. The new MCP policy relies on a country specific market-based norm and a tolerance margin to determine if the official action gives rise to an MCP.[31] The country specific market-based norm is defined as the range between the highest and lowest exchange rates of the given day in the wholesale FX market of the country implementing the official action, with a tolerance margin of +/- 2 percent of the midpoint of the high-low ("H/L") to avoid capturing minor deviations, as illustrated in Figure 1.

13. The methodology can be described by the following condition:

$$\text{Min}\ \{LOW_t\,;\ M_{(H/L)t} - 2\%\} \leq R_t \leq \text{Max}\ \{HIGH_t\,;\ M_{(H/L)t} + 2\%\}$$

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,

The mid-point of the High/Low range is defined as:

$$M_{(H/L)_t} = \frac{HIGH_t + LOW_t}{2}$$

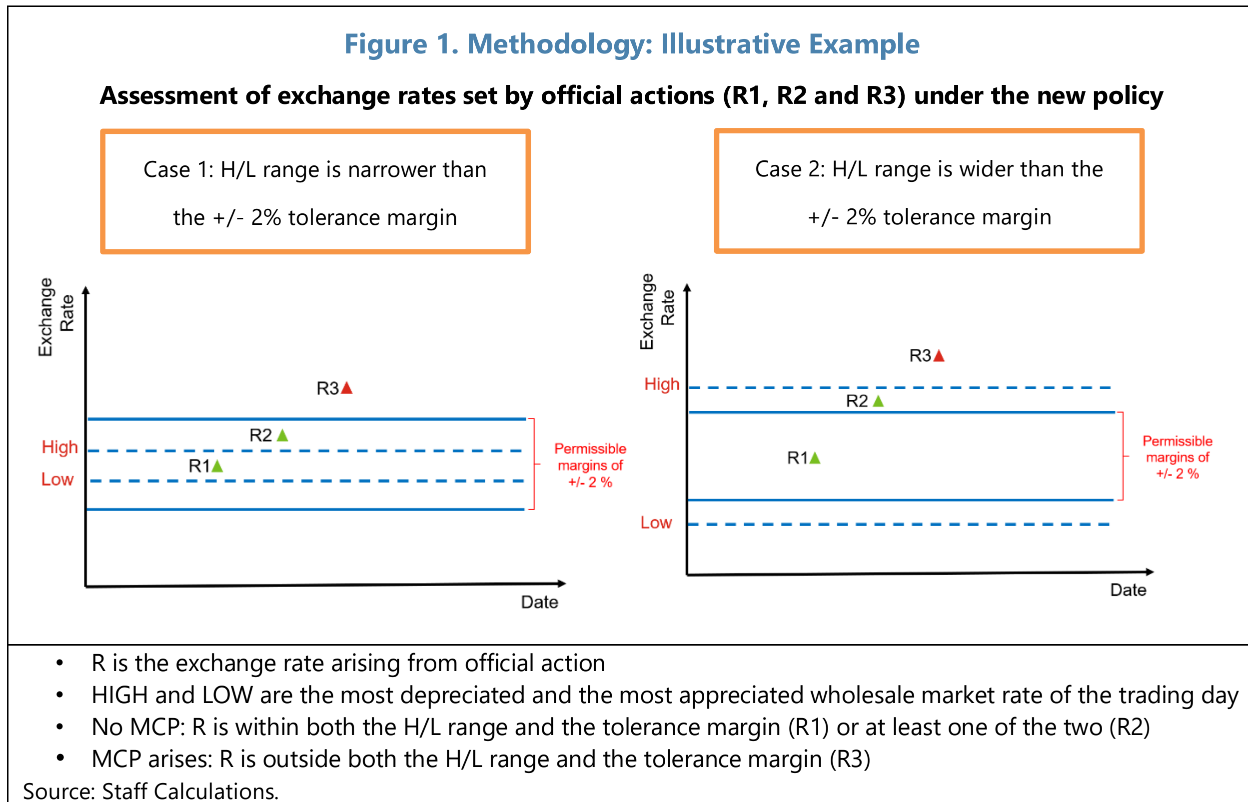
R_t is the exchange rate arising from official action, and t is a given trading day.

[30] This is 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.

[31] The previous MCP policy defined a uniform spread of more than 2 percent between buying and selling rates for a *spot transaction* as giving rise to an MCP.

Figure 1. Methodology: Illustrative Example

Assessment of exchange rates set by official actions (R1, R2 and R3) under the new policy



- R is the exchange rate arising from official action
- HIGH and LOW are the most depreciated and the most appreciated wholesale market rate of the trading day
- No MCP: R is within both the H/L range and the tolerance margin (R1) or at least one of the two (R2)
- MCP arises: R is outside both the H/L range and the tolerance margin (R3)

Source: Staff Calculations.

14. The methodology for assessing MCPs applies to both spot and non-spot FX transactions, with some supplementary requirements for specific non-spot transactions. This follows the market practice according to which the classification of exchange transactions on the FX markets depends on the settlement date of the transactions. 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 transactions).[32] The methodology will be further refined and additional guidance will be provided as experience is gained with application of the methodology to non-spot transactions (see Box 3).

15. The exchange rate data provided by LSEG Eikon (formerly Refinitiv Eikon) and Bloomberg will be used to determine the wholesale market H and L. LSEG Eikon is the primary data source and Bloomberg is the secondary source (see the forthcoming monitoring tool for data retrieval).[33] For non-spot transactions the methodology may also rely on theoretical prices, see Annexes II and V.

[32] 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.

[33] With regards to data retrieval from LSEG Eikon/Bloomberg and subsequent sharing of data with internal and external audiences, Fund staff must abide by all obligations and usage restrictions in accordance with the Fund's contracts with both data providers. More information on permissions and limitations is available on the intranet.

Box 3. Identifying MCPs in Spot and Non-Spot Transactions

Spot Transactions

Spot: Any FX transaction that settles at or less than t+2 days is considered a spot transaction. Any spot transaction exchange rate arising as a result of official action (R_t) is compared with the wholesale spot FX market H_t and L_t (where *t* is the trading day) and the tolerance margin of +/-2 percent of the mid of the H_t/L_t (denoted $M(H/L)_t$) to conduct the MCP assessment. An MCP arises if the spot exchange rate is not within either the H_t/L_t of the wholesale market rates or the tolerance margin, i.e., +/- 2 percent of $M(H/L)_t$. As an example, a central bank may require exporters to sell their FX proceeds either partly or wholly at a specific exchange rate (R_t) to commercial banks (surrender requirement). In this case R_t is compared with the wholesale market H_t and L_t and the tolerance margin of +/-2 percent of the $M(H/L)t$ to conduct the MCP assessment.

Banknote transactions: The banknote transaction exchange rate, R_t, either set by the authorities or otherwise affected by official action, is compared with the H_t and L_t of the wholesale spot FX market, and the tolerance margin of +/- 2 percent of the $M(H/L)_t$ to assess if it gives rise to an MCP. If the authorities can provide representative data on banknote rates in their FX market, such data could be used to apply the methodology. Staff will compare the results of the methodology using the H/L data provided by the benchmark providers and the data on banknote rates provided by the authorities, and the finding would be based on the data that results in the more favorable treatment for the member.

FX auctions: The FX auction conducted by the authorities which fails the criteria specified in the policy (see paragraph 8) will be evaluated for MCPs, using the weighted average exchange rate for multiple price auctions or the marginal rate for single-price auctions as the exchange rate resulting from official action. The weighted average exchange rate ($R^w{}_t$) in the case of multiple price auction or the marginal price ($R^m{}_t$) in the case of single price auctions are compared with the H_t/L_t of the wholesale spot FX market, and the tolerance margin of +/- 2 percent of the $M(H/L)_t$ where *t* is the trading day on which the FX auction was held.

FX Interventions: As FX intervention typically involves the authorities offering to purchase or sell foreign currency at a particular rate to all FX intermediaries or by accepting offers from them, it does not give rise to an MCP as long as it does not segment the FX market (see paragraph 8). However, where such transactions are conducted in a manner that makes FX available at a particular rate only to/from certain selected FX intermediaries, or for specific purposes/end-users or from selected intermediaries/sources/end providers, the exchange rate at which such FX purchases and sales are made would be assessed under the MCP policy, as it involves a form of market segmentation caused by official action. In such cases, the FX intervention rate (R_t) is compared with the H_t/L_t of the wholesale spot FX market, and the tolerance margin of +/- 2 percent of the $M(H/L)_t$ where *t* is the trading day on which the FX intervention took place.

Non-Spot Transactions

Non-Spot: Any FX transaction that settles at more than t+2 days is considered a non-spot transaction. Similar to spot transactions, non-spot exchange rates will be considered under the MCP policy if they arise from official action (e.g., authorities use them in FX transactions or require that FX intermediaries/end-users use them) and if the official action creates market segmentation. The rates in the spot and non-spot markets cannot be directly compared due to the settlement date affecting price formation, hence additional computations may be required for the assessment of the non-spot transactions. Since the non-spot wholesale market exchange rate is not as widely available as the spot exchange rate, the MCP assessment would have to rely occasionally on comparing the non-spot exchange rate resulting from official action with the +/-2% tolerance margin of the theoretical price of the non-spot transaction. For the calculation of the theoretical price, see Annexes II and V. However, there are drawbacks in using theoretical price for non-spot

Box 3. Identifying MCPs in Spot and Non-Spot Transactions (concluded)

transactions. Based on experience, staff will continue to work on refining the methodology to better assess when such exchange rates exceed the permissible margin.

Forwards: In a forward contract the parties commit to buy/sell a currency against another currency for a set price at a future date.[1] An MCP arises if the forward exchange rate arising from official action (R_t) is not within either the H_t/L_t of the wholesale forward market rates for the same maturity or the tolerance margin, i.e., +/- 2 percent of the $M(H/L)_t$ where *t* is a respective trading day. When interdealer forward rates are not available, the theoretical forward rate for the same maturity has to be calculated.[2] An MCP would arise if the forward exchange rate resulting from official action (R_t) were to exceed the +/- 2 percent tolerance margin of the theoretical price. Non-deliverable forwards (NDFs) are assessed under the MCP policy only if they are (a) provided or mandated by the authorities, (b) are made available to a subset of intermediaries or end-users or are earmarked for specific transactions, thus segmenting the market and (c) are so closely related to an exchange transaction that the benefit/cost arising from the NDF must be considered as part of the effective exchange rate of the exchange transaction.

Swaps: FX Swaps consist of a spot sale (or purchase) of one currency and the forward purchase (or sale) of the same currency and are frequently used for liquidity management and funding both in FX and local currency. Official action that either determines or otherwise affects exchange rates in FX swaps can give rise to an MCP. The assessment requires comparing the exchange rate of the swap's spot leg with the wholesale market spot exchange rates, while the exchange rate of the forward leg is compared with the market exchange rate for forwards of the same maturity. When wholesale market interdealer rates for forwards of the same maturity are not available, the theoretical price of the forward should be calculated. Both the spot and forward exchange rates of the FX swap arising from the official action should remain within the respective permissible margins, i.e., the spot exchange rate in the permissible margin of spot wholesale transactions and the forward exchange rate in the permissible margins of forward wholesale transactions to avoid an MCP. If either one or both exchange rates are outside the respective permissible margins, an MCP arises.

Options: FX options allow the holder the right (but not the obligation) to buy or sell FX from the option seller at or by a certain time in the future, for a set price.[3] If exercised, options arising from official actions will be assessed by comparing them with market transactions of similar terms at inception (see Box 2). If a market exists in the country for options with similar terms, the effective exchange rate of the option, R_t should remain within the H_t/L_t of the comparable option prices (strike rate plus option premium) or the +/-2 percent tolerance margin around the $M(H/L)_t$ of the comparable wholesale option market rates to avoid an MCP. If market prices are not available, staff will need to calculate a theoretical option price using LSEG Eikon (or Bloomberg) option price calculator and in this case, an MCP would arise if the option prices resulting from official action were to exceed+/- 2 percent tolerance margin of the theoretical option price.

[1] FX forwards are mostly used by end-users to hedge exchange risk and fund FX transactions.

[2] As described fully in Initial Considerations, Supplement III, if representative market data from alternative sources are not available, staff propose utilizing a theoretical forward rate, which is computed by adding the difference between the domestic and foreign interest rate for the given maturity of the forward to the wholesale market rate. Staff may use alternative data from the domestic market if considered more representative of the funding rate than that used by the benchmark providers for a given maturity. For ease of use, the forthcoming monitoring tool enables users to calculate theoretical forward prices by inputting the H_t and L_t wholesale spot market rate and the respective domestic and foreign interest rate.

[3] Two types of exercisable variations are generally offered; ones exercisable at any point before expiration, or ones that can be exercised only at time of expiration date.

16. When exchange taxes and other mandatory costs or subsidies are imposed on exchange transactions, the effective exchange rate will depend on whether the transactions' exchange rate is market-determined, and the effective exchange rate and the permissible spreads are determined as follows:

(a) Exchange taxes and other mandatory costs or subsidies imposed by official action on exchange transactions where the exchange rate is not determined by official action (i.e., the market exchange rate) would be deemed to be applied 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). This implies that exchange taxes (and other mandatory costs or subsidies) that alone or in the aggregate, do not exceed 2 percent would not give rise to MCPs. Additionally, it would also imply that for those member countries with a H/L permanently wider than 2 percent, exchange taxes (or other mandatory costs or subsidies) may not give rise to an MCP even though they exceed 2 percent alone or in the aggregate. As FX markets develop, the H/L may narrow below the +/-2 percent tolerance margin; in such case taxes that in aggregate exceeded 2 percent which previously did not give rise to an MCP may result in an MCP. In cases when there is no wholesale FX market and the tax applies on the bank-client exchange rates, the tax is deemed to be levied on the mid of the H/L of the bank-client rates.

(b) Where an exchange tax, other mandatory 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), it will be considered part of the effective exchange rate to be compared to the permissible spread (see discussion on effective exchange rate above). As a result, in such cases, the tax, other mandatory cost or subsidy even if less than 2 percent alone or in the aggregate could give rise to an MCP. Conversely, an exchange tax (and/or other mandatory costs or subsidy) of more than 2 percent, included in the aggregate, would not necessarily result in an MCP as long as the effective exchange rate remains within the H/L of the day.

E. Methodology for Monitoring Spreads

17. The methodology relies on a predefined order of data sources to limit the risk arising from excessive reliance on a single data source. Market exchange rates for both spot and non-spot wholesale market exchange rates will be primarily collected from two reputable data providers: LSEG Eikon is the primary source and Bloomberg is the secondary source. For guidance on sourcing market exchange rates from these data providers, see Annexes II and V.

18. Wholesale FX market data may not always be available or reliable. In rare cases where spot and/or non-spot wholesale FX market data are unavailable from both LSEG Eikon and Bloomberg or the data available from both data providers is manifestly irregular or inaccurate, staff should rely on other sources to obtain exchange rate data which are representative of the FX market. Alternative data sources staff could use include: (i) publicly available independent data

sources; (ii) publicly available data from the authorities; or (iii) data obtained directly from the authorities.[34] Staff is expected to determine whether the alternative data are representative of the FX market in each case by assessing whether they have been computed in compliance with the IOSCO principles for the computation of financial benchmarks (see Annex II Box 1). For further information on members' data provision requirements under the MCP policy, see Section VII.D. If representative data for spot exchange rates cannot be obtained, the MCP assessment cannot be conducted. For non-spot transactions the assessment can be concluded even in the absence of representative market data if the theoretical price of the non-spot transaction can be calculated.

19. The wholesale FX market data available from the primary and secondary data sources are considered representative unless staff has reasonable evidence to the contrary. When staff or the authorities have evidence that the exchange rate data from the primary and secondary data sources are manifestly irregular or inaccurate and as such are not representative of the wholesale FX market, staff will use alternative representative data sources (see paragraph 18). Such cases are expected to be rare.

20. The representative wholesale FX market is where the price formation of the currency takes place, without constraints by the authorities. In cases described in paragraph 18, in order to consider the wholesale market as representative of the country's FX market, staff should ascertain that (i) the market trades are not concentrated between a few participants, (ii) the market trades on a daily basis, and (iii) two-way executable quotes are available and trades are executed. If all of these are missing and/or there are official constraints (regulatory or through moral suasion) on intermediaries' quotes in the wholesale market stifling wholesale market operations, the wholesale market cannot be considered as representative of the FX market and staff should use data from alternative market segments that are representative.

21. Retrieval of market exchange rates for the assessment of MCPs involves several operational steps and consideration of specific official actions. When retrieving market data staff must ensure that the FX market in the corresponding country has closed for the day before extracting the highest and lowest exchange rates. This will prevent the retrieval of market data while FX transactions, which could alter highest and lowest rates, are still taking place. Second, if official action has established certain circumstances such as, e.g., legal dual FX markets, use of lagged official exchange rate or official dollarization, special considerations need to be made when retrieving market exchange rates. For more detailed instructions and specific step-by-step examples, please refer to Annex V and the forthcoming monitoring tool.

- **Currency Pairs:** If an official action results in market segmentation for multiple currency pairs, the MCP assessment is performed on the dominant currency pair first. If an MCP is found for the dominant currency, staff do not need to identify MCPs in other currency pairs to avoid multiple MCP findings arising from the same official action. In case there is no MCP finding for the

[34] For further information on additional data sources see Annex II, section B.

dominant currency pair, staff must assess if there is an MCP in the other currency pairs resulting from the official action for which information is available on LSEG Eikon or Bloomberg.

- **Dual or multiple legal FX markets in a single jurisdiction:** In the case of dual or multiple FX markets within a member's jurisdiction, i.e., when the authorities establish separate legal markets for the exchange of currencies in which participants conduct exchange transactions without arbitrage, the exchange rates on such distinct markets may exceed the permissible margin and must be quantitatively compared.[35] For the MCP assessment, the primary wholesale market (i.e., largest by volume and/or participants, used as benchmark, used by the authorities to intervene, etc.) determines the market H/L range. The mid-point of the H/L in the secondary market is considered as the exchange rate arising from the official action. In case the H/L is unavailable for the secondary market, staff should use the most representative exchange rate available from the secondary market for the assessment. Only FX markets in the same jurisdiction are considered. FX markets established outside of the country are not considered legal markets for the purposes of the MCP assessment.

DETERMINING THE EXISTENCE OF AN MCP AND ITS CONSEQUENCES

22. Compliance with the obligations under Article VIII, Section 3 of the Articles of Agreement regarding MCPs is the responsibility solely of Fund members. Accordingly, members shall ensure that they do not engage, or allow their fiscal agencies to engage, in MCPs as defined by the MCP policy. If a member engages in such practices without the approval of the Fund, the member would be in breach of its obligations under the Articles. For this reason, it is important that members gain understanding of the MCP policy and ensure compliance with it. In addition to the members' responsibilities to comply with their obligations under the Articles regarding MCPs, members' compliance with the MCP policy is also monitored by IMF staff.

23. Effective and timely communication between staff and the authorities is crucial to identify official actions, set expectations about monitoring of specific exchange rates and spreads, and act when impermissible spreads have been observed. The current policy envisages continuous monitoring of relevant exchange rate spreads in cases where official action (covered under the MCP policy) is identified. This will require timely identification of official actions that can give rise to an MCP and any changes to such action, continuous monitoring of the effective exchange rates arising from that official action, and timely communication of any observed impermissible spreads.

24. Engagement between staff and the authorities on official action is the critical first step that involves the sharing, requesting, and receiving information related to official actions

[35] Two legal exchange markets can coexist, for example, where there are different trading infrastructures (with some transactions having to be conducted exclusively on specific platforms) or where capital controls effectively segment the legal FX market.

covered under the MCP policy. The authorities should inform staff (country teams) about new official actions that can give rise to MCPs and changes in the existing measures. Staff should also remind the authorities to share such information. Typically, staff would request such information in the context of Article IV consultations[36] or program reviews, but staff can also request information at other times if they become aware of possible official actions or if they are informed by the authorities of an official action. If an official action is identified, staff will request relevant information from the authorities to determine the effective exchange rates arising from such official action and to monitor whether they are within the permissible margins. When an official action that segments the FX market is identified, the authorities may decide to remove the action to avoid an impermissible spread from arising.

25. It is important that staff and the authorities have clear understandings about the scope and periodicity of provision of data and information necessary for MCP assessments. For countries with Fund supported programs, such understandings would normally be reflected in a Technical Memorandum of Understanding (TMU). For other cases, and if additional information is needed for MCP assessment/monitoring during programs, these understandings should preferably be in writing. If a member's provision of data and information for MCP assessments is limited by capacity constraints, or if data or information is not provided for any other reasons, staff should discuss these issues with the authorities. These discussions may be included in the assessment of data adequacy for surveillance as per the relevant guidance, and/or mentioned in staff reports when warranted.[37]

26. The long-standing practice of the Fund has been that staff discusses with the authorities any issues concerning MCPs during Article IV consultations and/or program review missions. These discussions include any official action of the member or its fiscal agencies, particularly its design, purpose, and actual or potential economic impact and ways to remove the official action or the MCP arising from it. Once an MCP has been identified, the authorities should share with staff their intentions to request approval of the retention of the MCP or remove it, through one of the modalities discussed in Section IV.B. Discussions during the mission should also consider that an impermissible spread can arise any time, including the day before the Board meeting and preparations should be made for that eventuality. Staff should also seek the authorities' views on new MCP findings for inclusion in the Article IV consultation staff report.

27. When an impermissible spread is observed and thus an MCP has arisen, this should be immediately communicated.[38] As soon as staff observes an impermissible spread arising from an official action, it should inform the authorities immediately about the MCP. In this context, the authorities will need to decide whether to request the approval of the retention of the MCP or take

[36] Under the Integrated Surveillance Decision (ISD) paragraph 26, in principle, Article IV consultations 'comprehend' consultations under Articles VIII and XIV, which include discussions of MCPs and exchange restrictions.

[37] Shortcomings in the provision of data required under Article VIII, Section 5 unrelated to a member's capacity constraints will also be addressed under the applicable remedial framework. See Section VII.D of this Guidance Note.

[38] Staff will share information on the results of monitoring periodically if requested by the authorities.

the necessary actions to eliminate it. Staff will discuss with the authorities' potential ways of eliminating the MCP or advise them on the criteria and procedures for approval of MCPs (see Section IV.B). Staff will recommend approval to the Board if requested by the member, if staff is of the view that the relevant conditions for approval are met. Where an MCP arises and approval is not requested, staff will advise on the ways to remove the MCP.

28. If the authorities decide to request approval of the retention of the MCP, this can be done on a stand-alone basis or in the context of an Article IV consultation or program review. Procedures for approval of MCPs are described in Section IV.B. Any modifications to the existing MCPs (including those previously approved the Board) are subject to the Board approval under the same procedures applied to the introduction of the new MCP. If the Board does not approve the MCP, the determination of the existence of the unapproved MCP will be made through the Summing Up of the relevant Article IV consultation Board meeting, or Board decision adopted upon completion of an Article IV consultation on a lapse-of-time basis, where the Board endorses staff's appraisal.

29. Staff could assist the authorities on MCP-related issues via its capacity development work. At the authorities' request, and subject to Fund's policies on capacity development (CD), staff can provide technical advice on various aspects necessary to remove an MCP or remove or adjust an official action in a manner that it does not give rise to an impermissible spread in the future (see also paragraph 41).

MEMBERS' OBLIGATION REGARDING MCPS

30. Fund members shall not engage in MCPs, unless such practices are authorized under the Articles of Agreement or are approved by the Fund. If the member engages in MCPs outside the transitional arrangements of Article XIV (see next paragraph), in order to maintain such practices in a manner consistent with its obligations under Article VIII, Section 3, the member should request approval of the Fund, i.e., the Executive Board. The procedures for obtaining approval for the introduction, modification, and retention of MCPs as well as the modalities that can be used by the member to remove MCPs are discussed in Sections IV.B and IV.C.

A. Maintaining MCPs Under Transitional Arrangements of Article XIV

31. Transitional arrangements under Article XIV allow members to maintain MCPs or exchange restrictions in place at the time at which they join the Fund.[39] A member availing

[39] The provision authorizes a member that avails itself of such transitional arrangements to "*maintain and adapt to changing circumstances the restrictions on payments and transfers for current international transactions that were in effect on the date on which it became a member*". For purposes of Article XIV, the reference to "restrictions" includes both exchange restrictions and MCPs, because Article VIII, Section 3 states that if a member is engaging in multiple currency practices on the date when it joins the Fund, the member concerned must consult with the Fund as to their progressive removal "*unless they are maintained or imposed under Article XIV, Section 2, in which case the provisions of Section 3 of that Article shall apply*".

itself of Article XIV may maintain those MCPs or exchange restrictions that were in effect on the date on which it became a member, and consult with the Fund annually with respect to their retention.[40] An adaptation of any MCP maintained under Article XIV also requires consultation with and approval of the Fund.[41] Article XIV consultations are required only if the member maintains measures under the transitional arrangements of Articles XIV. Any measures put in place by the authorities after the member joins the Fund are not protected by Article XIV, Section 2 (and in such case no consultation would be required under Article XIV) and will give rise to a breach of Article VIII, Section 3, unless approved by the Fund. While the Fund may call on members maintaining MCPs under Article XIV to remove such measures in exceptional circumstances, in practice it has not done so. Rather, the Fund has historically adopted a collaborative approach encouraging members to remove measures maintained under Article XIV, including through conditionality under Fund-supported programs and technical assistance.[42]

B. Approval of MCPs

32. Maintaining an MCP that is approved by the Fund is in compliance with the member's obligations. The Fund can approve MCPs maintained both for BOP and primarily for non-BOP reasons provided that the relevant approval criteria established by the Executive Board are met (Box 4). The assessment as to whether the MCP is introduced (maintained) for BOP or primarily for non-BOP reasons is made at the time of the approval request and is based on the circumstances at that time. Changes to the existing MCP require an approval of the Fund and are subject to the same approval criteria applicable to the introduction of a new MCP (see paragraphs 33–34). Staff should determine, after consultation with the authorities, whether the MCP is imposed or maintained for BOP or primarily for non-BOP reasons.[43] For a MCP to be considered as being introduced (maintained) for BOP reasons, the measure should be considered as needed to address the BOP difficulties of the member. It is not sufficient for a member to have BOP difficulties for a measure to be assessed as being introduced (maintained) for BOP reasons. Therefore, a measure that was initially considered to be for BOP reasons and was approved on that basis may, as conditions

[40] Article XIV consultations are, in principle, included in Article IV consultations. See paragraph 26 of the Integrated Surveillance Decision. Decision No. 15203-(12/72), adopted on July 18, 2012.

[41] The duty to consult with the Fund and obtain its concurrence in a proposed change flows from the combined effect of Article XIV, Section 2 and Article IV. See "Legal Aspects of Multiple Currency Practices Under Second Amendment" in SM/79/127 of May 15, 1979", page 23.

[42] See "Review of the Fund's Policy on Multiple Currency Practices—Initial Considerations—Historical Development and Legal Framework of the MCP—Background Paper I" in SM/18/208, Supplement 1, of August 15, 2018 , paragraphs 26-28. Such conditionality has included measures requiring members either to accept the obligations of Article VIII, Section 2, 3 and 4, or to remove specific exchange measures maintained under Article XIV. Acceptance of Article VIII, as a practical matter, encourages the removal of all measures maintained by the member under Article XIV.

[43] 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. As an example, a non-BOP objective could include MCPs for tax revenue mobilization and allocation of resources to specific sectors.

change, subsequently be viewed as being maintained primarily for non-BOP reasons, or vice versa.[44] This determination is important to establish which criteria apply for the Executive Board to temporarily approve the MCP. MCPs that apply solely to capital transactions do not require Fund approval.[45]

33. MCPs maintained for BOP reasons can be approved if the following criteria are met: (i) the measure is temporary[46] and is being applied while the member is endeavoring to eliminate its BOP problems; (ii) it does not give the member an unfair competitive advantage over other members; and (iii) it does not discriminate among members. For the MCP to be considered temporary, the authorities should normally indicate a firm timetable for its removal. If a country has a Fund-supported program, the MCP may be considered temporary, i.e., implemented for the duration of the program, if the program includes reforms that will allow the member to eliminate MCPs by the end of the program. In some cases, it might not be possible to eliminate the official action causing an MCP immediately. For example, sometimes multiple exchange rates need to be phased out in steps in the context of the gradual liberalization of the FX market allowing for the development of better market price discovery, and a firm timetable for removing MCPs may not be feasible. Thus, in certain cases, approval of the MCP(s) could be requested if the member is taking the necessary steps to eliminate it, e.g., the member commits to a credible strategy (as described in paragraph 34) for their removal.

34. The Fund may also approve MCPs imposed or maintained primarily for non-BOP reasons. Approval for such MCPs may be granted if the practices (i) do not materially impede the member's BOP adjustment, (ii) do not harm the interest of other members, (iii) do not discriminate among members, (iv) do not constitute an exchange restriction, and (v) the member commits to a credible strategy for the removal of the measure. 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 removal of MCPs within a reasonable period.[47] The strategy would be country-specific and would consider the country's characteristics and capacity to manage risks that may arise if the MCP is removed.

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[44] Assessing whether the MCP is introduced/maintained for BOP or primarily for non-BOP reasons may require judgment. In making such judgment, staff should give the benefit of any reasonable doubt to the representation of the authorities as to the purpose for which the measure is used. However, the Fund will make an objective assessment based on all relevant circumstances.

[45] Historically, the Executive Board declined to assert jurisdiction over MCPs that apply solely to capital transactions, See the Board paper on "Multiple Currency Practices Applicable Solely to Capital Transactions" in SM/85/19 of January 16, 1985; the Chairman's Summing Up at the Conclusion of the Discussion on Multiple Currency Practices Applicable Solely to Capital Transactions in BUFF/85/34, of February 25, 1985; and the Minutes of the Board meeting 85/23 in EBM/85/23 of February 13, 1985.

[46] The notion of "temporary" for purposes of approval is different from "temporary" as grounds for a waiver of nonobservance of a performance criterion in a Fund arrangement. (See Section VI.)

[47] Eliminating certain MCPs may require a longer transition period to avoid macroeconomic disruptions and may be conditions-based. In Fund supported programs, the timeframe for removal is frequently by the end of the program.

Box 4. Summary of MCP Approval Criteria[1]	
MCPs maintained for BOP purposes can be approved if the MCPs:	**MCPs maintained primarily for non-BOP purposes can be approved if the MCPs:**
are temporary;	do not materially impede the member's BOP adjustment;
are being applied while the member is endeavoring to eliminate its balance of payments problems;	do not harm the interest of other members;
do not give the member an unfair competitive advantage over other members; and	do not discriminate among members;
do not discriminate among members.	do not constitute an exchange restriction; and
	the member commits to a credible strategy for the removal of the MCP.
[1] All listed criteria should be met for an approval of an MCP.	

35. MCPs that also constitute exchange restrictions can be approved if the relevant approval criteria are met. The Fund can grant temporary approval for exchange restrictions if the measures are imposed or maintained for BOP reasons, are temporary, and do not discriminate among Fund members.[48]

36. A request for approval, with a statement of the reasons for the request, should be made by the authorities in writing[49] to the country team or in program documentation (LOI or MEFP). Members typically seek approval after the MCP is identified.[50] Where the authorities inform staff that they are considering introducing a measure (official action) that could give rise to an MCP, or where an MCP has been identified, the country team should inquire whether the authorities intend to seek the temporary approval of the MCP. If the authorities inform staff of their intent to seek approval of the MCP, staff will assess whether the approval criteria as described in paragraphs 33-34 are met and advise the member whether approval can be recommended. If staff is of the view that the relevant approval criteria are met, staff's recommendation concerning approval shall be included in the Staff Appraisal section of the relevant staff report. To assist the Board in assessing the MCP and reaching a decision concerning approval or non-approval, the staff report will analyze the reasons underlying the MCP and its effects. If approval is requested on a stand-alone basis, a short Board paper would be issued to the Board containing the members' request and the staff's recommendation for approval. If the finding of the MCP is made in the context of an Article IV consultation or a program review, the member can decide to request Fund approval of the retention

[48] According to Executive Board Decision No. 1034-(60/27), adopted on June 1, 1960, the Fund will grant approval of exchange restrictions imposed for balance of payments reasons "*only where it is satisfied that the measures are necessary and that their use will be temporary while the member is seeking to eliminate the need for them*".

[49] Rule H-4 of the IMF By-Laws, Rules and Regulations.

[50] While the requirement for approval under Article VIII, Section 3 has been considered to require approval prior to the introduction of a measure that could give rise to an MCP, it has been recognized that the Fund can also grant approval ex post, i.e., after the measure is introduced. Under the new MCP policy, an MCP arises only when impermissible spread emerges.

of the MCP at the time of the conclusion of the consultation or completion of the review. If staff recommends Board approval, the staff report should explain whether the approval criteria are met, and the relevant staff report will include a proposed Board decision to approve the MCP.[51] Where approval is not sought by the authorities, the staff report should normally urge elimination of unapproved MCPs (see footnote 99).

37. Approval of MCPs is normally granted for a one-year period or until the next Article IV consultation (whichever is earlier), to provide for regular review by the Executive Board in the context of Article IV consultations. Approval is granted from the date of the adoption of the Board decision. One exception to the usual one–year period is where the MCP is maintained for existing arrangements and for a specified period, for instance, in cases where legal commitments are in place and must be carried out in spite of the decision to discontinue the practice. MCPs could be approved for longer periods on a case-by-case basis e.g., in cases of expired forward cover schemes where approval has been requested until the maturity of the remaining contract or in cases of exchange rate guarantee scheme which may exceed one year.[52]

38. Unapproved MCPs are inconsistent with members' obligations under the Articles. A finding of a breach of the obligation may trigger sanctions, specified in Article XXVI. In practice, the Fund has followed a cooperative approach in dealing with unapproved MCPs or exchange restrictions. Under such an approach the Fund, through its surveillance, program conditionality, and technical assistance, encourages member countries to eliminate unapproved MCPs.

C. Removal of MCPs

39. MCPs that are inconsistent with members' obligations should be removed. An MCP may be removed in one of the following ways:

(i) When the authorities remove the official action that gave rise to the MCP, for example, through the abolition of the requirement to use an official exchange rate that causes an impermissible spread, or the repeal of a law or regulation that implement the use of multiple exchange rates.

(ii) Where the authorities choose to keep the relevant official action in place, in certain circumstances the MCP could still be considered eliminated if the authorities take credible measures to bring the spread back within permissible margin and ensure that such action will not, in the future, give rise to spreads that fall outside of permissible margins. If an impermissible spread arises again in future, a new MCP would be found.

(iii) Even if the authorities take no action to eliminate the MCP, it would still be considered eliminated if based on the monitoring of the exchange rates by staff over an "observation

[51] See also the "Guidance Note on Surveillance under Article IV consultations", paragraph 93.

[52] See the Board paper on the "Approval Period for Multiple Currency Practices" in SM/98/102 of May 18,1998, paragraph 5. In all cases, the condition of temporariness of the measures will have to be assessed, while allowing this condition to be applied in a flexible manner in particular circumstances.

period" of 12 months after the emergence of the impermissible spread, an impermissible spread has not recurred. The MCP would remain in place during the observation period and would be noted in Article IV or URF staff reports. The reemergence 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 spreads before the MCP is considered eliminated.[53]

40. The removal of an MCP will be mentioned in the relevant AIV or UFR staff report. The staff report should include details on the removal of the MCP, including the modalities for removal and the date on which the MCP was considered removed. In particular, when the MCP is removed through option (ii) in paragraph 39, the measures taken by the authorities to remove the MCP should be described in the staff report.

41. The Fund has encouraged members to remove unapproved MCPs through surveillance, programs, and capacity development (CD). Such assistance is in line with the Fund's basic objective of unifying exchange rates in multiple rate systems.[54] CD on removing MCPs is often part of Fund's assistance on broader FX market reforms, which provides comprehensive guidance on changes and improvements in monetary policy, FX market regulations and operations, necessary to support the unification of the exchange rate.

OPERATIONAL GUIDANCE FOR STAFF

A. Assessment of Official Actions

42. Staff assess measures imposed by authorities to determine if these constitute official actions, as defined by the MCP policy. Information about measures that may constitute official actions under the new MCP policy may come from the authorities or from staff. In this regard, staff will assess and determine the jurisdictional implications[55] of the authorities' actions or measures impacting the member's exchange system.

43. Area department staff are expected to notify relevant functional department staff and provide the relevant information once they observe, or if they are informed by a member that it has introduced, is considering, or has modified measures that may be considered an "official action". This should be done as soon as staff become aware of any such measures and not only in policy notes or during the policy consultation process. Staff will then assess whether the

[53] For instance, if an impermissible spread was observed on March 17, 2023, the observation period will finish on March 16, 2024. However, if an impermissible spread is again observed in September 2023, the 12-month observation period would recommence immediately and, if there were no further impermissible spreads, end in September 2024 and the MCP would be considered removed in September 2024. In this example, an impermissible spread observed after September 2024, would constitute a new MCP.

[54] See Executive Board Decision No. 649-(57/33), adopted on June 26, 1957.

[55] "Jurisdictional implications" or "jurisdiction" refers to an assessment of whether a particular policy measure falls under the scope of members' obligations respecting MCPs under Article VIII, Section 3.

measure constitutes official action under the MCP policy, whether it applies to current payments and transfers or financial account transactions, and, whether the measure may also constitute an exchange restriction or capital flow management measure (CFM)[56]. If the measure is assessed to constitute an official action for the purposes of the MCP policy, the country team should initiate immediately exchange rate spread monitoring to determine whether it gives rise to an MCP. Initial data analysis should normally assess all observations from the date of the official action to confirm whether an MCP has already arisen or for the past 12 months, whichever is shorter. For official actions introduced or changed during a Fund-supported program the initial data analysis should cover the entire period from the date of the official action.

B. Communication with the Authorities

44. Staff must notify the authorities about the identification of a measure as an official action under the MCP policy. This communication will normally involve a short note outlining the details of the measure and the basis for staff's assessment. Staff will also provide the authorities with specific details of any required FX monitoring, including ticker codes, etc., such that the authorities have sufficient information to conduct similar monitoring. When needed for monitoring purposes, staff will request that the authorities provide exchange rate data on a regular basis (see Section VII.D).

C. Monitoring Exchange Rates

45. Area department staff are responsible for the ongoing monitoring of the relevant exchange rates. Monitoring of exchange rates arising from official action should be undertaken continuously and, in particular, should be done daily during the period after the mission and before Board meetings. Frequent monitoring will ensure that authorities are promptly informed when MCPs arise, and that the Board can be fully informed and, in the case of programs, is in the position to assess compliance with the program conditionality. When impermissible spreads arise after a staff report is issued to the Board and before the Board meeting, a Supplement to the staff report should be issued. Area department teams are expected to maintain records of daily exchange rates and spreads according to the IMF's framework on records management. For the purposes of the MCP policy, it would be useful for departments to maintain records for at least five years.

46. When an impermissible spread is observed, the area department team should promptly alert relevant functional departments staff, who can confirm that an MCP has arisen. Once the occurrence of impermissible spread is confirmed, the authorities should be notified. The identified MCP should be discussed in the next staff report or, if the authorities request approval of the measure on a stand-alone basis, in the document requesting Board approval.

[56] Identifying a measure as a CFM and assessment of its appropriateness under the Institutional View on the Liberalization and Management of Capital Flows is conducted by the interdepartmental capital flow group in accordance with IV.

D. Coverage of Official Actions and MCPs in Policy Notes

47. During the policy consultation process, area department teams should confirm that no impermissible spreads have arisen since the last Board consideration of a given member. Policy notes should discuss any official actions that could give rise to an impermissible spread and note whether there have been impermissible spreads observed. Where there is a new MCP or there is an existing MCP finding, the policy note should include staff's assessment of the economic impact of the measures and any policy advice, in line with the expected coverage in the staff report (see Section VIII). Where there are unapproved MCPs, staff are expected to urge their elimination (also see footnote 99). If staff anticipate that the authorities will request approval of an MCP, the policy note should discuss whether the measure is for BOP or non-BOP purposes and whether the approval criteria are likely to be met or would continue to be met in the case that the MCP was previously approved.

TREATMENT OF MCPS IN FUND-SUPPORTED PROGRAMS AND EMERGENCY FINANCING

48. The Fund promotes compliance with the MCP policy and Article VIII, Section 3, by continued monitoring under Fund-supported programs of the standard continuous PC on the non-introduction and non-modification of MCPs. All Fund arrangements[57] (except for FCL, SLL and RSF arrangements) and non-financial monitoring instrument, PCI) include a standard continuous performance criterion (PC) (for arrangements), or continuous quantitative target (QT) (for PCIs) that prohibits the introduction or modification of MCPs at any time during the period of the arrangement.[58] The standard PCs on MCPs and exchange restrictions are not required for SMPs.[59] References to MCPs in Fund decisions relating to UFR do not include MCPs applying solely to capital transactions, except if otherwise provided.[60] Another standard continuous PC prohibits the imposition or intensification, at any time during the arrangement, of exchange restrictions. It is best

[57] Executive Board Decision No. 10464-(93/130), adopted on September 13, 1993, as amended, sets out the standard terms for SBA and EFF arrangements which provide for the standard continuous PCs on the non-introduction and non-modification of the MCPs, and non-introduction and non-intensification of exchange restrictions. Other Fund's arrangements (except FCLs, SLLs and RSFs), as well as PCIs include these clauses by analogy.

[58] The present Guidance Note refers to PCs, ACs, and QTs interchangeably.

[59] See paragraph 15 of the "Updated Operational Guidance Note for SMP" ("*While not specifically applicable to the SMP, continuous adherence to exchange system obligations under Article VIII of the Fund's Articles of Agreement is an obligation of all Fund members and compliance should therefore be encouraged at all times*").

[60] As the Executive Board declined to assert jurisdiction over MCPs that apply solely to capital transactions, it also did not support the inclusion of such MCPs in the scope of the standard PC. See the Board paper on "Multiple Currency Practices Applicable Solely to Capital Transactions" in SM/85/19 of January 16, 1985; the Chairman's Summing Up at the Conclusion of the Discussion on Multiple Currency Practices Applicable Solely to Capital Transactions in BUFF/85/34, of February 25, 1985; and the Minutes of the Board meeting 85/23 in EBM/85/23 of February 13, 1985.

practice to include all standard continuous PCs in the tables of PC and structural conditionality attached to an LOI or in a TMU.[61]

49. In addition to the standard PCs on MCPs and exchange restrictions, Fund arrangements and non-financial monitoring instruments can include specific conditionality, directed towards the elimination of MCPs (and exchange restrictions). This could include, for example structural benchmarks and/or prior actions, where such measures are necessary for the achievement of the objectives of the program or for the implementation of specific provisions of the Articles or policies adopted under them.[62]

50. If a member with a Fund arrangement or PCI, introduces a measure that gives rise to a new MCP, or modifies an existing MCP at any time during the arrangement/PCI, the member will be in breach of the standard continuous PC/target, respectively. In such case, the review under the arrangement can only be completed, if the Executive Board grants a waiver of non-observance of that PC. Where an MCP also gives rise to an exchange restriction, both PCs/ACs would have to be assessed and waivers of nonobservance of both PCs/ACs would be required. For the PCI, the nonobservance of the continued target does not require a formal waiver but the completion of a review is subject to the Board's judgment that there are compensating factors. [63]

- If the MCP was introduced or modified after *the arrangement was approved but prior the completion of the ongoing review*, a waiver of nonobservance of the PC will be required for the review to be completed. If an MCP was introduced or modified in the period leading to completion of an earlier review at which a purchase or a disbursement was approved, and it was not reported to the Fund at the time of that review, not only a waiver of nonobservance of the standard PC would be required, but misreporting may also arise under the applicable misreporting frameworks.[64]

[61] The two other standard continuous PC provide that a member: (i) will not conclude bilateral payment agreements that are inconsistent with Article VIII and (ii) will not impose or intensify import restrictions for balance of payment reasons.

[62] Under paragraph 7 (a)(ii) of the Conditionality Guidelines, conditionality may include measures "*necessary for the implementation of specific provisions of the Articles or policies adopted under them*".

[63] Under the PCI a failure to meet a standard continuous target on non-introduction or modification of MCP does not trigger the need for a formal waiver. Rather, deviations from targets serve as indicators that the PCI might no longer be on track for successful implementation. Completion of the review in such a case requires a judgment by the Board that there are compensating factors (e.g., that missed targets are assessed to be the result of minor or temporary factors, or corrective actions have been taken). See para 33-34 of the PCI Operational Guidance Note.

[64] See "Misreporting and Noncomplying Purchases in the General Resources Account—Guidelines on Corrective Action" in Executive Board Decision No. 7842-(84/165), adopted on November 16, 1984, as amended, and the "Provisions on Corrective Action for Misreporting and Noncomplying Disbursements in Arrangements under the Poverty Reduction and Growth Facility and the Exogenous Shocks Facility" (in Appendix I of the Instrument to Establish the Poverty Reduction and Growth Facility and Exogenous Shocks Facility Trust annexed to Executive Board Decision No. 8759-(87/176), adopted on December 18, 1987, as amended).

- If the MCP was introduced or modified *prior to the approval or after the expiration of a Fund arrangement/PCI*, it has no impact on the observance of the standard PC.

51. The member with a Fund arrangement/PCI is responsible for providing information to the Fund to assess compliance with the conditions established by the Executive Board. The authorities thus should consult with staff in advance of taking action to ensure that it would not give rise to a new MCP, or a modification of an existing MCP, to avoid delays in completing program reviews. During the negotiations for a new arrangement/PCI, and during the period of the arrangement, staff should proactively seek information from, and understandings with, the authorities on policies that may give rise to MCPs.

52. The assessment of the standard PC on the non-introduction and non-modification of MCPs will be guided by following:

- ***An MCP would be considered "introduced"*** *if*, following the date of approval of the arrangement//PCI, an impermissible spread arises from*:*

  (i) a new official action that did not exist prior to the approval of the arrangement/PCI;[65] or

  (ii) a change during the arrangement/PCI to official action that was adopted prior to the approval of the arrangement/PCI;

If an impermissible spread arises during the arrangement/PCI solely from an official action taken prior to, and not changed during the arrangement/PCI, an MCP would arise (and therefore the member should request Board approval) but the MCP would not be considered as introduced for the purposes of the continuous PC.

- ***An MCP would be considered "modified"*** if the authorities make any change in the official action(s) underlying a previous (existing) MCP finding (unless changes constitute removal of the MCP).

53. If the same official action that gives rise to an MCP under the previous MCP 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 PC 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.[66]

54. In exceptional cases, the standard PC can be modified to exclude from its scope certain MCPs already in place or expected to be introduced during the program. This can be

[65] Such a new measure (official action) could also be combined with another official action that pre-dates the approval of the arrangement/PCI which, when combined, gives rise to an impermissible spread.

[66] See "Review of the Fund's Policy on Multiple Currency Practices—Proposals for Reform" in SM/22/129 of June 6, 2022, paragraph 42, last bullet. Under Art. VIII, section 3, a member should still request approval to remain in compliance with its obligations.

done at the time of the approval of an arrangement/PCI or at the time of a program review by modifying the standard PC through the relevant changes to the TMU which includes the definitions of PCs and other program-related conditions. It is expected that such exclusions would be rare.[67] An exclusion of specific MCPs from the PC could be considered, for example, when staff is of the view that the official action which would segment the market and create a multiplicity of exchange rates is necessary but the MCP, if it were to emerge, cannot be approved. Such exclusion may be for the entire duration of the program, or for a shorter period, as appropriate depending on the circumstances.

55. Where a member introduces or modifies an MCP during an arrangement, a program review can be completed only if the Board grants the waiver of non-observance. Generally, a waiver of nonobservance will be granted only if the Fund is satisfied that, notwithstanding the non-observance of the PC, the program will be successfully implemented—i.e., that it will achieve its goals—either because of the minor or temporary nature of the nonobservance or because of corrective actions taken by the authorities.[68] In the case of the non-observance of the standard PC on non-introduction and non-modification of the MCP, the following considerations apply in assessing the grounds for the waiver:

- ***Minor non-observance:***

The introduction of an MCP is a breach of an obligation under Article VIII Section 3 and thus cannot be considered "minor". As a result, this ground for a waiver of non-observance will not be available in case of introduction of the new MCP. A modification of an MCP is also not considered minor, as the modification is treated as an introduction of a new MCPs.

- ***Temporary non-observance:***

For staff to recommend a waiver based on this ground, the MCP (or its modification) which gave rise to the non-observance of the standard PC must be removed by the time of the completion of the review.[69]

- ***Corrective action:***

While the Fund may lend to a member with unapproved MCPs, the member that introduces or modifies an MCP that results in the non-observance of the standard PC is generally advised to seek

[67] In the past, such exclusions from the scope of the standard PC were used for MCPs arising from the multiple-price foreign exchange auction system, developed in line with Fund staff advice, to accommodate the temporary necessity of the auctions for countries' exchange system considering the level of development of the FX market. See, for example, paragraph 37 of the TMU for the request for an EFF arrangement by the Pakistan (IMF Country Report No. 2019/212). Under the new MCP policy, single and multi-priced auctions that conform to best practices would not give rise to MCPs.

[68] See the Guidelines on Conditionality for further details. For the PCI, no waivers are required. See footnote 63.

[69] The meaning of "temporary" in the context of the waiver of non-observance of the standard PC differs from "temporary" as a ground for approval of MCPs under Article AVIII which normally requires "a clear timetable for removal of the MCPs".

temporary approval of such MCP under Article VIII, Section 3.[70] Once such approval is granted, the Board would also normally grant a waiver of nonobservance of the PC. The member's request for approval under Article VIII is normally considered the "corrective action" for purposes of the waiver of nonobservance.[71]

56. Where the MCP (or its modification) cannot be approved by the Board under Article VIII, a waiver of non-observance of the PC for the introduction or modification of an MCP could only be granted if the MCP has been removed.[72] The member can remove the MCP as described in paragraph 39.

57. In addition to the standard PCs on MCPs and exchange restrictions, all Fund arrangements (except for FCL, SLL, and RSF arrangements) and non-financial monitoring instruments (PCI) also include a standard continuous performance criterion (PC) (for arrangements), continuous assessment criterion , or continuous quantitative target (QT) (for PCIs) that prohibits members from concluding bilateral payment agreements (BPAs) that are inconsistent with Article VIII. As discussed in paragraph 77 and Annex III, BPAs may give rise to exchange restrictions and/or MCPs. If a member, during the period of a Fund arrangement (PCI) enters into a BPA that includes such provisions, a waiver of nonobservance would be required for the upcoming review to be completed. Staff should remind the authorities of countries with Fund-supported programs that BPAs can include provisions inconsistent with Article VIII and encourage them to discuss with staff any plans to enter into a BPA during the Fund-supported program.

MCPs and Emergency Financing (RCF/RFI)

58. As RCFs and RFIs constitute outright disbursements/purchases without ex-post conditionality, these instruments do not include the standard continuous PC on the non-introduction and non-modification of MCPs. However, the ex-ante policy undertakings for RFIs and RCFs encompass the typical commitment not "to introduce or intensify exchange and trade restrictions and other measures or policies, such as MCPs, that could compound the members' BOP difficulties".[73] Such commitments are included in the authorities' LOI requesting financing under the

[70] Fund is legally not precluded from lending to the member with unapproved exchange restrictions or MCPs. See "Legal Aspects of Article VIII and Article XIV" in SM/59/73 of November 18, 1959 and "Legal Effects of Approval or Nonapproval of Exchange Restrictions by the Fund" in EBS/88/13 of January 28, 1988.

[71] While an approval of the MCP by the Fund under Article VIII is different from a waiver for the non-observance of the standard PC (and they are subject to different criteria), as explained above, there will usually be an overlap when a country has an arrangement/ and requires a waiver of nonobservance of the standard PC/AC based on corrective actions. The decision on approval under Article VIII will be taken first, before the decision on completing the review/granting the waiver of nonobservance of the PC/AC.

[72] If an MCP is also an exchange restriction, the same approach applies if the criteria for approval of exchange restrictions are not met.

[73] See in relation to RCFs, paragraph 1 (d)(1) of Section II of the Instrument to Establish the Poverty Reduction and Growth Trust ("*A member requesting assistance under the RCF shall describe in a letter the general policies it plans to pursue to address its balance of payment difficulties, how its policies advance its poverty reduction and growth objectives, and its intention not to introduce measures or policies that would compound its balance of payments*

(continued)

RFI or RCF. Staff should ensure the consistent inclusion of the relevant language in LOIs. Any Article VIII measures introduced contrary to these commitments will be discussed in the next Article IV and/or UFR staff report. Prior actions with respect to MCPs can be established where appropriate under the relevant policy.[74] The Fund can, as a condition for the RFI/RCF disbursement/purchase, require a member to implement a prior action on the elimination or calibration of the measure which gives rise to an MCP or exchange restriction subject to the Board approval under Article VIII.[75]

RELATIONSHIP BETWEEN THE MCP POLICY AND OTHER RELEVANT FUND POLICIES

59. Article VIII, Section 3 is linked to several other provisions in the Articles. These include Article VIII, Section 2(a) on exchange restrictions, Article IV on exchange rate policies and surveillance, Article XIV on transitional provisions for members who join the Fund with MCPs or exchange restrictions in place, and Article VI on capital transfers. This section elaborates on these links.

A. MCPs and Article XIV

60. The transitional arrangements under Article XIV allow members to maintain MCPs or exchange restrictions in place at the time at which they join the Fund. (See paragraph 31).

B. MCP Policy and the Fund's Policy on Exchange Restrictions

61. MCPs and exchange restrictions are distinct legal concepts covered under Article VIII, Section 3 and Article VIII, Sections 2(a), respectively. Article VIII, Section 2(a) prohibits members from imposing restrictions on the making of payments or transfers for current international

difficulties.") as well as paragraphs 180 and 224 of the 2023 LIC Handbook in relation to the RCF ("*The member would need to outline, in a LOI, the policies it plans to pursue, and set out any additional understandings to provide assurance that it will not introduce measures or policies that would compound its balance of payments difficulties.*"; "*Continuous measures could include commitments related to non-introduction of certain exchange restrictions and multiple currency practices*"). In relation to RFIs, see paragraph 4 of Executive Board Decision No. 15015-(11/112), adopted on November 21, 2011 ("*A member requesting assistance under this Decision shall describe in a letter the general policies it plans to pursue to address its balance of payments difficulties, including its intention not to introduce or intensify exchange and trade restrictions and other measures or policies that would compound these difficulties*").

[74] Under paragraph 11 (a) of the Guidance on Conditionality "*A member may be expected to adopt measures prior to the Fund's approval of an arrangement, completion of a review, or the granting of a waiver with respect to a performance criterion when it is critical for the successful implementation of the program that such actions be taken to underpin the upfront implementation of important measures. In reaching understandings on prior actions, the Fund will also take into account the strain that excessive reliance upon such actions can place on members implementation capacity*".

[75] See paragraph 222 of the 2023 LIC Handbook in relation to the RCF ("*Prior actions could be specified if necessary, but this would be expected only in exceptional circumstances, specifically when it is critical for addressing the urgent balance of payments need effectively that a measure be taken prior to the financial assistance provided under the RCF.*").

transactions, unless approved by the Fund or authorized under the transitional arrangements under Article XIV. The MCP policy is broader than the policy on exchange restrictions: an MCP can arise from any purchase or sale of FX that relates to either the making (i.e., outflow) or receipt (i.e., inflow) of payments, solely on for capital transactions, while the policy on exchange restrictions covers only outgoing payments and transfers for current international transactions. Therefore, MCPs that apply to transactions other than those defined as current under Article XXX(d), including incoming payments and transfer (e.g., differentiated rates for surrender of FX from exports), do not give rise to exchange restrictions. Sometimes exchange measures imposed by members may give rise to both MCPs and exchange restrictions (e.g., exchange taxes, mandatory import deposit requirements). As MCPs typically involve circumstances where some market participants are given access to FX at a more (or less) favorable exchange rate than others, the additional cost arising from the MCP and borne by the market participants subject to the less favorable rate may be considered by the Fund to be a limitation on their access to FX for current payments and, therefore, an "exchange restriction". Further, where an additional cost is imposed by official action (i.e., an exchange tax), such measure may be both an MCP and an exchange restriction.[76]

62. While MCPs arising from exchange taxes and other mandatory costs that apply to outgoing payments and transfers for current international transactions have generally been considered to also constitute exchange restrictions, the review of the MCP policy adjusted this treatment. Historically, the MCP policy has allowed members to impose minor taxes (i.e., less than 2 percent under the old MCP policy) on exchange transactions without giving rise to an MCP, recognizing the limited impact of such taxes on international trade in goods and services. The treatment of exchange taxes and other mandatory costs under the new MCP policy was adjusted with the aim to maintain continuity with the old policy, while allowing for the application of the new methodology.[77] Due to the absence of a de minimis rule for exchange restrictions, taxes and other mandatory costs below 2 percent were considered as giving rise to exchange restrictions.[78] To reflect these considerations and to achieve better coherence between the two policies, the new MCP policy provides that exchange taxes and other mandatory costs or subsidies that are subject to the MCP policy and do not give rise to MCPs would also not give rise to exchange restrictions.[79] In practice this would have the implications discussed in paragraph 10 and Annex I. The assessment as to

[76] See also "Review of the Fund's Policy on Multiple Currency Practices— Initial Considerations" in SM/18/208 of August 15, 2018, pages 10-11, paragraph 11, and "Review of the Fund's Policy on Multiple Currency Practices—Initial Considerations—Historical Development and Legal Framework of the MCP—Background Paper I" in SM/18/208, Supplement 1, of August 15, 2018, page 11, paragraph 25.

[77] On the treatment of exchange taxes and other mandatory costs under the MCP policy, see paragraph 10 and Annex I.

[78] See "Review of the Fund's Policy on Multiple Currency Practices— Initial Considerations" in SM/18/208 of August 15, 2018, paragraphs 7, 23, Box 4 and "Review of the Fund's Policy on Multiple Currency Practices—Proposals for Reform" in SM/22/129 of June 6, 2022, paragraphs 20-21.

[79] 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.

whether other types of official action that may give rise to MCPs also constitute exchange restrictions will continue to be made on a case-by-case basis.

63. Both MCPs and exchange restrictions can be temporarily approved by the Fund but the approval criteria under the two policies differ. While MCPs can be approved if maintained for both BOP and non-BOP reasons, exchange restrictions can only be approved if they are maintained for BOP reasons.[80] To avoid the situation where a measure which is both an MCP and an exchange restriction can be approved under the MCP policy but not under the policy on exchange restrictions, MCPs maintained for non-BOP reasons can only be approved to the extent that the same measure does not also constitute an exchange restriction.[81]

64. MCPs may also constitute discriminatory currency arrangements (DCAs), the imposition of which is also prohibited under Article VIII, Section 3. MCPs and DCAs are distinct legal concepts, however, the same measure may be an MCP and a DCA. While the Fund has not adopted a definition of DCAs, they are generally understood as arrangements by a member to discriminate, through its exchange system, to the benefit, or to the detriment, of another member or other members. DCA may or may not involve discrimination through exchange rates.[82] While an MCP may also be a DCA, in practice, the Fund does not identify measures as DCAs.[83]

C. MCP Policy and the IMF Institutional View on Liberalization and Management of Capital Flows

65. Official action that gives rise to an MCP may at the same time be a capital flow management measure (CFM) if it is "designed to limit capital flows".[84] The definition of a "current transaction" under Article XXX(d) of the IMF's Articles of Agreement captures some transactions that, from the economic perspective, are capital in nature and are registered in the capital and financial accounts of the balance of payments, namely: (i) payments of moderate

[80] See Section IV.B.

[81] MCPs that are also exchange restrictions and are introduced solely for reasons of national or international security, the streamlined approval procedure set for the in Decision No. 144-(52/51), adopted on August 14, 1952 would apply.

[82] Examples of DCAs include a restriction by the discriminating member against the use by another member or its residents of their holdings of the currency of the discriminating member (e.g., a freeze by a member of its currency holdings by another member), bilateral payment arrangements, a restriction on some or all payments and transfers, in whatever currency, by residents of the discriminating member to the member or its residents discriminated against, or measures to grant favorable treatment to some members, which therefore discriminate other members, such as the treatment by each participant in a monetary zone of other participants that is more favorable than the treatment of nonparticipants.

[83] See "Legal Aspects of Multiple Currency Practices Under Second Amendment" in SM/79/127 of May 15, 1979, p. 24-24. Members are entitled to apply capital controls even if they are discriminatory under Executive Board Decision No. 541-(56/39), adopted on July 25, 1956.

[84] Such cases are expected to be rare, as the IV provides that CFMs should generally not be designed in a way that gives rise to exchange restrictions and MCPs on current transactions. See "Review of the Fund's Policy on Multiple Currency Practices—Proposals for Reform" in SM/22/129 of June 6, 2022, paragraph 32.

amounts for amortization of loans or for depreciation of direct investments; (ii) normal short-term banking and credit facilities; and (iii) moderate remittances for family living expenses. As a result, measures that impact these types of transactions may be classified simultaneously as MCPs and CFMs (and exchange restrictions). In addition, some measures that affect solely capital transactions (as per Article XXX(d)) may be an MCP as well as a CFM. Finally, a measure that is broad enough so as to affect both capital transactions and transactions defined as "current" under the Articles may be classified as an MCP and a CFM with respect to the underlying capital transactions and an MCP (and an exchange restriction) with respect to payments and transfers for current transactions. In advising members on CFMs, staff should be mindful that CFMs should generally be designed in such a way as not to give rise to exchange restrictions or MCPs for current transactions.[85] Measures that are both MCPs and CFMs will always be mentioned and discussed as MCPs in relevant staff reports in line with the discussion in section VIII and will be identified in the report as being a CFM if the criteria for coverage of CFMs in surveillance are met.

66. MCPs including those that are also CFMs are subject to Board approval, except for MCPs applicable solely to capital transactions (see paragraph 65). The Article VIII approval criteria differ from the criteria to assess the appropriateness of CFMs under the IV. To avoid potentially inconsistent policy advice that may result from the application of the two frameworks to a measure which is at the same time an MCP and a CFM, such measures will be treated as set out in paragraph 67.

67. Measures that are MCPs and also CFMs due to the Articles' definition of current transactions and are subject to Fund approval under Article VIII will be assessed only under the MCP policy. Such measures will not be assessed under the IV for appropriateness.

68. A measure may be broad enough so as to affect both capital transactions and transactions defined as "current" under the Articles. Such measures may be classified as a CFM (and an MCP) with respect to capital transactions and as an MCP (and an exchange restriction as the case may be) with respect to payments and transfers for current transactions. A measure, which is an MCP and which affects both current (as defined in the Articles) and capital transactions and thus is also a CFM, will be assessed only under the MCP approval policy.[86] The appropriateness of such measure will not be assessed under the IV. An example of such measure may be an exchange tax that gives rise to an MCP and applies to both current and capital transactions.

69. MCPs that are also CFMs and are applicable solely to capital transactions (as per Article XXX(d)) will be assessed only under the IV.[87] As such, staff should identify MCPs applicable to capital transactions in Article IV (or UFR) reports, but no finding of a breach of obligation under Article VIII, Section 3, will be made and such MCPs are not subject to Fund

[85] See SM/22/129, paragraph 32.

[86] See SM/22/129, footnote 50.

[87] "Capital transactions" in this Section VII.C are transactions that are registered in the capital and financial accounts of the balance of payments, except for those defined as "current" under Article XXX(d)) of the Fund's Articles of Agreement.

approval.[88] An illustrative list of official actions that apply solely to capital transactions and may give rise to an MCP is included in Box 5.

Box 5. Illustrative Examples of Official Actions That May Give Rise to MCPs Applicable Solely to Capital Transactions

- A tax on FX purchase for acquiring securities abroad by residents.
- The requirement to use a specific exchange rate for FX purchases by residents to acquire real estate abroad.
- Cash margin requirement or URR on inflows resulting from external borrowings by residents.
- The requirement to use a subsidized forward exchange rate in FX swaps concluded between banks and the central bank to assure banks' future acquisition of FX in connection with their repayment of the principal amount of long-term non-residents' deposits.

70. An official action that may give rise to an MCP and is also a CFM should be discussed as an MCP in the relevant staff report only if an impermissible spread arises. In the absence of impermissible spread the CFM should be discussed in the staff report to the extent the measure meets the criteria for coverage in the surveillance for CFM. For the coverage of the official action in the staff report see paragraph 79.

D. Member's Obligations to Provide Data to the Fund

71. MCP assessments are data driven. Information and data required for MCP assessments include information about official action and, once official action is identified, exchange rate and other, e.g., tax, interest rate data to assess whether an impermissible spread arises. While with market exchange rates, the policy relies primarily on exchange rate data compiled by the primary and secondary exchange rate data providers, information may also need to be provided by a member country, for example, when data is not available from the mentioned data providers or in respect of transactions data or information that are not publicly available.

72. The MCP policy does not introduce any new data provision requirements but relies on the Fund's existing data provision frameworks. Some data and information necessary for MCP assessment are provided by members voluntarily, while provision of other data and information are mandatory. For instance, Article VIII, Section 5 requires each member to provide information on: (i) "buying and selling rates for foreign currencies," [89] (ii) information on "exchange controls, i.e., a comprehensive statement of exchange controls in effect at the time of assuming membership in the

[88] 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.

[89] Under Rule H-6 of the IMF By-Laws, Rules and Regulations, "*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.*" In practice, such arrangements include a reporting of monthly and quarterly exchange rate data to the Fund. However, monitoring of exchange rates under the MCP policy will need to rely on daily data.

Fund and details of subsequent changes as they occur", and (iii) for existing official clearing arrangements, "details of amounts awaiting clearance in respect of commercial and financial transactions, and of the length of time during which such arrears have been outstanding.[90] Therefore, as part of this existing obligation, members must provide information on exchange rates arising in their territory from official action, such as: (i) unpublished exchange rates used in transactions by the authorities that segment the market;[91] (ii) exchange rates in legal parallel markets; (iii) taxes, fees, other costs and subsidies related to exchange transactions; and (iv) exchange rates set forth in official payment arrangements. Country teams should have understandings with the authorities on the provision of exchange rate data, including market exchange rates if not available from third party providers or other public sources, and other data relevant for MCP assessments. Also, it is members' obligation to inform the Fund, on a continuous basis[92] about the details of any changes to 'exchange controls", including the introduction of new measures, or changes to the existing ones including related to existing MCPs (and exchange restrictions). Failure to provide mandatory data/information, or the provision of inaccurate data/information could lead to a breach of obligation, unless non-provision or inaccurate provisions is due to the member's lack of capacity.[93,94] If a member has an arrangement or a non-financial monitoring instrument with the Fund, the Fund may require additional information to that required under Article VIII, Section 5.[95] Any deficiencies concerning data required for an MCP assessment may be noted as part of data adequacy assessments in Article IV reports as is the case with all data issues. They can also be mentioned in other reports, e.g., on program reviews.

73. Beyond information that is required under the Articles or in Fund-supported programs, members have generally also provided all other information necessary for staff to conduct an MCP assessment and would be expected to continue to do so. This includes, for example, agreements such as BPAs. For agreements between central banks, staff should continue to request copies of all such agreements in order to assess whether they include features found in official payments arrangements and official clearing arrangements that may give rise to MCPs and/or exchange restrictions. Staff often prepare a questionnaire for the authorities specifying information necessary for an MCP assessment.

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[90] Article VIII, Section 5 (x), (xi), (xii) of the Fund's Articles of Agreement.

[91] This would include, for instance, price data from exchange auctions that do not comply with best practices, exchange rates used in transactions with government.

[92] Unless more specific understandings have been reached with IMF country teams.

[93] See Executive Board Decision No. 13183-(04/10), adopted on January 30, 2004, as amended, on Strengthening the Effectiveness of Article VIII, Section 5.

[94] See Executive Board Decision No. 7842-(84/165), adopted on November 16, 1984,as amended, in respect of misreporting in the GRA. Appendix I of the Instrument to Establish the Poverty Reduction and Growth Facility and Exogenous Shocks Facility Trust annexed to Executive Board Decision No. 8759-(87/176), adopted on December 18, 1987, as amended, deals with misreporting under PRGT arrangements.

[95] Data required for program monitoring is normally specified in a Technical Memorandum of Understanding. However, additional information or data may be required if needed for the MCP assessment.

74. The Fund's framework for the treatment of confidential information applies to data provided for MCP assessments. The Fund has a robust framework in place for treatment of confidential information, which applies to non-public data provided for purposes of MCP assessments.[96] In providing data to the Fund a member can designate particular non-public data as "confidential," in which case the relevant provisions of the confidentiality framework will apply. However, a member cannot request staff, and staff cannot agree, to refrain from sharing with the Executive Board data required to be provided under the Articles.

COVERAGE OF MCPS IN STAFF REPORTS

75. Staff reports should provide a comprehensive discussion of MCPs.[97] This discussion of the coverage of MCPs in staff reports supersedes guidance laid out in the "Guidance Note for Surveillance under Article IV Consultations". The new MCP policy aims for increased transparency and accountability through consistent and comprehensive discussion of MCPs in staff reports. As MCPs are exchange rate policies and may lead to a breach of obligations under the Articles they are always discussed in Article IV consultation reports. Staff reports are expected to discuss the official actions that gave a rise to an MCP, reasons underlying the practice, the MCPs' actual or expected economic impact, and advice provided to the authorities, as well as the authorities' plans regarding the measure. Coverage in staff reports—including the depth and prominence—depends on several factors as discussed below. The Informational Annex to the Article IV staff report should always include information on the new and existing MCP(s), including MCPs applying solely to capital transactions. [98] MCPs which are also CFMs should be identified and discussed in the staff reports also considering specifics outlined in Section VII.C.

A. MCP Findings

76. New MCP findings and modifications of the existing MCPs should receive prominent coverage in the staff report. The main text of the staff report should discuss: (i) staff's assessment that an MCP has arisen or that modification to the existing MCP has been made; (ii) describe the underlying official action and observed impermissible spread or changes to them in case of MCP modifications, including noting the most recent date when impermissible spread was observed; (iii) reasons underlying the introduction or modification of the MCP ; and (iv) the actual or expected economic effect. The views of the authorities should also be noted (see paragraph 82). In addition, staff's initial finding of a new, or a modification to an existing MCP should be included in the Staff Appraisal section of the report. The Staff Appraisal section should also clearly state whether approval has been requested and, if so, whether the approval criteria are met. The staff report

[96] See Annex IX of the "Updated Guidance Note on the Fund's Transparency Policy".

[97] Outside of the Article IV consultation/UFR reports, reports on Article VIII acceptance and reports requesting temporary approval of Article VIII measures (that is, ad hoc staff reports and decisions) are occasionally sent to the Executive Board for consideration.

[98] Unlike Article IV consultation reports, UFR reports typically do not include an Informational Annex. However, the country team may decide to include it.

should also discuss the authorities' plans regarding the measure and staff's policy advice on removal. Where staff does not recommend, or the authorities do not request, approval of the MCP, staff should urge its removal in the Staff Appraisal section.[99] The Informational Annex should elaborate on all existing MCP findings and modifications to existing MCPs, describing the official action that gives rise to the MCP (or modified it), the date when an impermissible spread first arose, and also the most recent date when the impermissible spread was observed. In program countries, a waiver of nonobservance of a continuous performance criterion on non-introduction and non-modification of an MCP would need to be requested by the authorities where relevant (see paragraph 50). Accordingly, the staff report on the program review will discuss, in the main text and in the Staff Appraisal section, staff's recommendation for a waiver and whether the criteria for granting a waiver are met (see Box 6 for examples of coverage in staff reports in the past).

Box 6. Examples of Past Coverage of MCPs in Staff Reports

Argentina. In the period between 1st and 2nd reviews of the 2022–24 EFF, the authorities introduced new measures (preferential exchange rates for soybean exports and non-resident tourists) that gave rise to new MCPs. The staff report discusses MCP-related issues throughout the report, including an elaboration on the measure. It cautioned that despite a potential for some FX cash flow relief, FX restrictions and incentives are not a substitute for addressing underlying macroeconomic imbalances. Staff recommended to gradually unwind MCPs as conditions permit and the impact of tighter macroeconomic policies materializes. It found a breach of a continuous performance criterion (all in the main text and the Staff Appraisal). The Staff Appraisal included a recommendation to the Executive Board to grant a temporary approval of the MCPs on the basis that they are temporary, expected to be gradually lifted over the program period, and do not give rise to an unfair competitive advantage over other members or discriminate among members. Also, as this was a program review, it recommended waivers of nonobservance of the performance criteria based on temporary nature as one measure (the preferential rate for soybean exports) was expected to expire ahead of the Board meeting and planned corrective action, i.e., request for approval of the MCPs. Further discussion on the measures adopted by the authorities and their assessment in the context of Article VIII are provided in Annex II of the above staff report.

Burundi. As of mid-2022, the authorities continued to maintain an MCP which was discussed in the Informational Annex of the 2022 Article IV staff report. Recalibration of exchange rate policy was advised to ensure external sustainability. Advantages, downsides, and risks of two proposed approaches to exchange rate unification—an instant unification and a gradual adjustment within a target period—were examined and summarized in the Text Table 10. The measures' assessment was discussed in the main text of the report and noted in the Informational Annex.

Nigeria. At the time of the 2022 Article IV staff report, the authorities maintained four MCPs, one of which—repatriation rebate scheme for non-oil exporters—was introduced in the period since the previous staff report. The main text of the report provides a description of MCPs and advised that "Moving towards a unified and market-clearing exchange rate has become more urgent than ever to restore confidence, build up buffers, address persistent FX shortages, and bring down high parallel market premiums, which are contributing to elevated inflation". The selected issue paper, that accompanied the 2021 Article IV staff report, examined the impact of the MCPs on exchange rate pass-through to inflation. The external sector

[99] In rare circumstances, staff may find it inappropriate to recommend removal of an unapproved MCP in the near term (for example, when authorities are engaging in FX market reforms and plan to remove an MCP but in this context removal may take time). In those rare cases, it would be sufficient to note the MCP without necessarily advising its near-term removal.

Box 6. Examples of Past Coverage of MCPs in Staff Reports (concluded)

assessment (Annex III to the above staff report) elaborated on MCPs and stressed that "the complex exchange rate regime, multiple exchange rates, and widening parallel market premium leave Nigeria vulnerable to external shocks".

77. In subsequent years after an MCP finding, where the MCP has not been removed since the previous staff report, the staff report should continue to discuss the MCP. The Article IV staff report should note that the country continues to maintain the MCP and include a discussion of the official action that gave rise to an MCP, the impermissible spread with the most recent date and continue to provide policy advice, as discussed above (see paragraph 76).[100,101] The staff report (Article IV and UFR) may provide an update on the authorities' plans to remove it. If the authorities seek an extension of the temporary Board approval of an MCP, the staff report (Article IV and UFR) should provide an assessment of whether criteria for approval continue to be met, and the Staff Appraisal should include staff's recommendation regarding approval. The Informational Annex should elaborate on the MCP, describing the official action, the date when an impermissible spread first arose and the most recent observed date.

78. The coverage of official actions that could give rise to an MCP but where there is no MCP finding can vary depending on the economic impact of those measures. Staff reports can discuss the official action and its economic impact, including for example, that the measure segments the FX market and/or can be distortionary. Staff can also advise to remove or change the official action. The Policy Note should discuss that staff are monitoring the relevant exchange rates for impermissible spreads related to specific official actions (see paragraph 47). However, the staff report should not refer to the official action as "likely to give rise to an MCP" or other similar language, nor should staff explicitly discuss that they are monitoring specific transactions.

79. Newly identified MCPs that apply only to capital transactions should also be reported as MCPs in the main text of the staff report, Staff Appraisal and in the Informational Annex.[102] In subsequent years, such MCPs and any modifications to them (including those that are also CFMs) should be discussed in the Informational Annex (and, where relevant, in the staff report, see Section VII.C).

[100] This approach aligns treatment of approved and unapproved MCPs and is in line with the discussion of approaches to encourage member countries to eliminate MCPs in the context the 2018 Board paper by more transparent reporting in respect of unapproved MCPs. See Press Release No. 19/203.

[101] If there is no change since the last staff report in which the MCP was covered, this can be done by cross-referencing the earlier staff report(s).

[102] As noted in the Acting Chair's Summing Up on the Review of the Fund's Policy on Multiple Currency Practices—Proposals for Reform in SU/22/104 of July 8, 2022, Directors agreed that MCPs that apply solely to capital transactions are not subject to Fund approval under Article VIII, Section 3 but would continue to be identified as MCPs in Article IV reports and will be assessed only under the IV.

B. Requests and Recommendation for Approval

80. If the member requested temporary approval of an MCP, the staff report will confirm this and include staff's assessment on whether criteria for temporary approval are met. The Staff Appraisal should note that the authorities have requested temporary approval of the MCP; and it should also discuss whether staff supports the request, whether the MCP is for BOP or non-BOP reasons, and whether the MCP meets the relevant criteria for approval. In case of a request for approval of an MCP for non-BOP reasons, a description of the credible strategy for eliminating the MCP should be included in the main text of the staff report, along with an indication of when or under what conditions the MCP will be eliminated.

C. Removal of MCPs

81. Where an MCP previously identified in a staff report has been removed, removal should be discussed in the next staff report (or the next Article IV staff report, at the latest) and this information should be included in the Informational Annex. The main text of the staff report should note that the member has removed the MCP and discuss when and how it was removed (e.g., the date of removal of the official action, the date when credible measures were taken, or if it has been 12 months since the last observation of an impermissible spread). When the authorities take credible measures to remove the MCP, these should be described in the staff report. The Informational Annex should also include information on the MCP removal and its date.

D. Authorities' Views

82. Authorities' views in staff reports. 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 staff report even when the authorities accept the staff's finding, but especially when there is disagreement.[103]

E. Countries on a 24-Month Article IV Consultation Cycle

83. Coverage of MCPs in staff reports for countries on a 24-month consultation usually follows rules described above. However, a situation may arise when an official action gives rise to an impermissible spread, but a 12-month observation period ends, the official action is removed, or other credible measures are taken before the next Article IV staff report's consideration by the Board. In this case, where appropriate, the staff report may include a discussion of an official action, impermissible spread, their economic impact, the authorities' actions and dates of the MCP emergence and elimination.

[103] Inclusion of the authorities' views on MCP findings in UFR staff report is also encouraged.

F. Annual Reporting to the Board

84. Staff will prepare an annual report to the Board on existing MCPs and their approval status across the membership. The reporting will commence once the new MCP policy becomes effective. The annual report will provide a list of all existing MCPs and MCPs removed over the previous calendar year as reported in the latest IMF staff reports.[104] The list will contain a brief description of the MCPs, their approval status, and, for approved measures, whether they are for BOP or non-BOP reasons and, where applicable, the date of the MCP removal. MCPs that apply solely to capital transactions and that are noted as such in staff reports will also be included. The annual reports will be circulated to the Board for information and are not expected to be disseminated externally. For external audiences, the Annual Report on Exchange Arrangements and Exchange Restrictions (AREAER) includes information on MCPs as discussed in the latest IMF staff reports issued as of December 31 of the AREAER reporting year.

[104] As envisaged in paragraph 11 in the 2022 MCP paper.

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Annex I. Taxes, Other Mandatory Costs, and Subsidies

1. Taxes, other mandatory costs, or subsidies imposed on, or closely related to an exchange transaction, are considered official action and may therefore give rise to MCPs. Such taxes and other mandatory costs (e.g., fees, surcharges) increase the cost of exchange transactions and may also segment the market (e.g., if the tax/cost applies only to certain types of exchange transactions).[1,2] In contrast, a mandatory subsidy decreases the cost of exchange transactions and may segment the market as well. If a tax or other mandatory cost or subsidy is imposed on, or closely related to an exchange transaction, it is considered part of the effective exchange rate for that transaction and, if the resulting effective exchange rate exceeds the permissible spreads under the methodology, it would give rise to an MCP.

2. As a first step in assessing taxes, other mandatory costs or subsidies under the MCP policy, staff should determine whether these taxes, costs or subsidies are "so closely related to an exchange transaction" as to constitute part of the effective exchange rate. An exchange tax (i.e., a tax imposed on an exchange transaction such as a stamp tax on purchase or sale of FX) is an example of a tax that is considered so closely related to the exchange transaction as to become a part of the effective exchange rate for the exchange transaction. Sometimes, a tax is imposed on an international transfer rather than on the sale or purchase of FX (e.g., transfer taxes, withholding taxes).[3] In these cases, the assessment of whether the tax should be considered as part of the effective exchange rate would require a comprehensive analysis based on country specific facts, e.g., whether it applies only to transfers abroad, or to all transfers, etc.[4] (See section II.B.) Taxes which are levied on the exchange of currencies are considered as exchange taxes even if they are collected separately from the exchange transaction or at a different time than the exchange transaction. 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.

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[1] Exchange taxes have been under the purview of the MCP policy since its inception. The Fund has long recognized that exchange taxes fall within the Fund's jurisdiction under Article VIII, Sections 2(a) and 3. See the Statement to Members transmitting Fund's Decisions on Multiple Currency Practices, in Appendix to Executive Board Decision No. 237-2, adopted December 18, 1947, and "Legal Aspects of Multiple Currency Practices under Second Amendment" in SM/79/127, of May 15, 1979. See also "Review of the Fund's Policy on Multiple Currency Practices—Initial Considerations—Historical Development and Legal Framework of the MCP—Background Paper I" in SM/18/208, Supplement 1, of August 15, 2018.

[2] The treatment of exchange taxes under the MCP policy will generally apply to other mandatory costs and subsidies closely related to exchange transactions and introduced by official action.

[3] Transfers subject to tax may be for current or capital transactions. For the treatment of MCPs applicable solely to capital transactions, see Sections IV.B and VII.C.

[4] A transfer tax (i.e., a tax which applies only to funds remitted abroad) can be considered as closely related to the exchange transactions and as such be part of the effective exchange rate if the transfer requires the exchange of one currency to another. For example, if local currency must be converted into foreign currency before transferring the funds abroad, the transfer tax can be considered as part of the effective exchange rate. However, if the transfer can be done in local currency as well, and the transfer tax applies on such transfers the tax would not be considered as closely related to the exchange transaction.

3. For the calculation of the effective exchange rate the entire amount of tax(es) levied on the transaction must be included. However, if the tax is reimbursed fully or partially later, the effective exchange rate would be calculated considering the time value of the tax, i.e., similarly as the cash margin requirements and the part of the tax paid which has not been reimbursed. In case the amount of tax reimbursed and the time period during which the reimbursement is made varies according to the other tax liability of the person subject to tax and the date of the transaction during the tax year, the average amount (share) of tax and period until compensation needs to be considered for the calculation of the effective exchange rate. In the absence of such information, the nominal tax rate and the longest period until reimbursement (e.g., one year) will be included.

4. If staff determines that a tax, other mandatory cost or subsidy constitutes part of the effective exchange rate for the underlying exchange transaction, it will apply the methodology to assess whether the resulting effective exchange rate remains within the permissible spreads. The new MCP policy seeks to broadly provide continuity for the treatment of exchange taxes, other costs and subsidies imposed by official action. Their treatment will differ depending on whether the tax is imposed on market determined exchange rates or on exchange transactions where the exchange rate is determined by other official action. The methodology will apply as follows:

- **Exchange taxes, other costs or subsidies imposed by official action on exchange transactions where the exchange rate is market determined.** Such taxes, other costs or subsidies are considered 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).[5] This implies that exchange taxes that alone or in the aggregate with other mandatory costs and subsidies, do not exceed 2 percent would not be considered MCPs. Conversely, it would also imply that for those member countries with a H/L permanently wider than 2 percent, exchange taxes (or other mandatory costs or subsidies) may not give rise to an MCP even though they exceed 2 percent alone or in the aggregate. 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.[6]

- **Exchange taxes, other mandatory costs or subsidies are imposed on an exchange transaction with an exchange rate arising from other official action (e.g., a rate determined by the authorities).** Such taxes, other costs or subsidies imposed on the exchange transaction by official action will be considered part of the effective exchange rate that will be compared to the permissible spread under the new methodology. As a result, in such cases, the

[5] See the description of the new methodology for identifying MCPs, including the tolerance margin in Section II.B.

[6] Not considering 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, would provide a degree of certainty to the treatment of exchange taxes that is important for fiscal policy making. 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.

mandatory cost, including an exchange tax, or subsidy however small amount could give rise to an MCP. Conversely, an exchange tax (and/or other mandatory costs or subsidy) would not necessarily result in an MCP if the effective exchange rate remains within the H/L of the day. In other words, any tax can give rise to an MCP and need to be monitored.[7]

- ***Taxes, other mandatory cost or subsidy imposed on transfers:*** taxes imposed on transfers rather than on the exchange transaction as such, if considered to be so closely related to the exchange transaction as to constitute part of its effective exchange rate, will be assessed as specified in the previous two bullets, depending on whether the exchange rate for the underlying exchange transaction (i.e., purchase or sale of FX necessary to make the transfer) is determined by official action.

5. As explained in Section VII.B of this note, exchange measures that give rise to MCPs may also give rise to exchange restrictions under Article VIII, Section 2(a).[8] The new policy seeks to better align the treatment of exchange taxes and other mandatory costs under the MCP policy and the Fund's policy on exchange restrictions. Unlike under the previous policy, under the new policy exchange taxes and other mandatory costs that are subject to the MCP policy but do not give rise to MCPs would also not give rise to exchange restrictions.[9] This approach acknowledges that the Fund historically has considered minor taxes (i.e., taxes up to two percent) to be non-objectionable,[10] under the MCP policy while, due to the absence of a *de minimis* rule for exchange restrictions, exchange taxes and other taxes (e.g., taxes targeting the making of payments and transfers for current international transactions) below 2 percent were found to be exchange restrictions.

6. Taxes and other mandatory costs that are not considered as part of the effective exchange rate and thus cannot give rise to an MCP, would continue to be considered to give rise to exchange restrictions regardless of the size of the tax/cost.

[7] For example, a tax of less than 2 percent in itself or in aggregate with other mandatory costs and taxes may give rise to an MCP if the effective exchange rate that includes the tax would be outside of the permissible margins. Conversely, even a larger tax exceeding 2 percent may not give rise to an MCP if the effective exchange rate remains within the permissible margins which can happen if the H/L is wider than the tolerance buffer.

[8] See "Review of the Fund's Policy on Multiple Currency Practices—Initial Considerations—Historical Development and Legal Framework of the MCP—Background Paper I" in SM/18/208, Supplement 1, of August 15, 2018, paragraphs 23-25 and Section VII.B of this Guidance Note.

[9] See "Review of the Fund's Policy on Multiple Currency Practices— Initial Considerations" in SM/18/208 of August 15, 2018, paragraphs 7 and 23, as well as Box 4. 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.

[10] According to the Board paper on the "Operational Aspects of Multiple Currency Practices under the Second Amendment" in SM/79/161 of June 13, 1979, it was felt that a two percent spread would accommodate minor taxes on exchange transactions "*without jeopardizing an orderly system of exchange rates*".

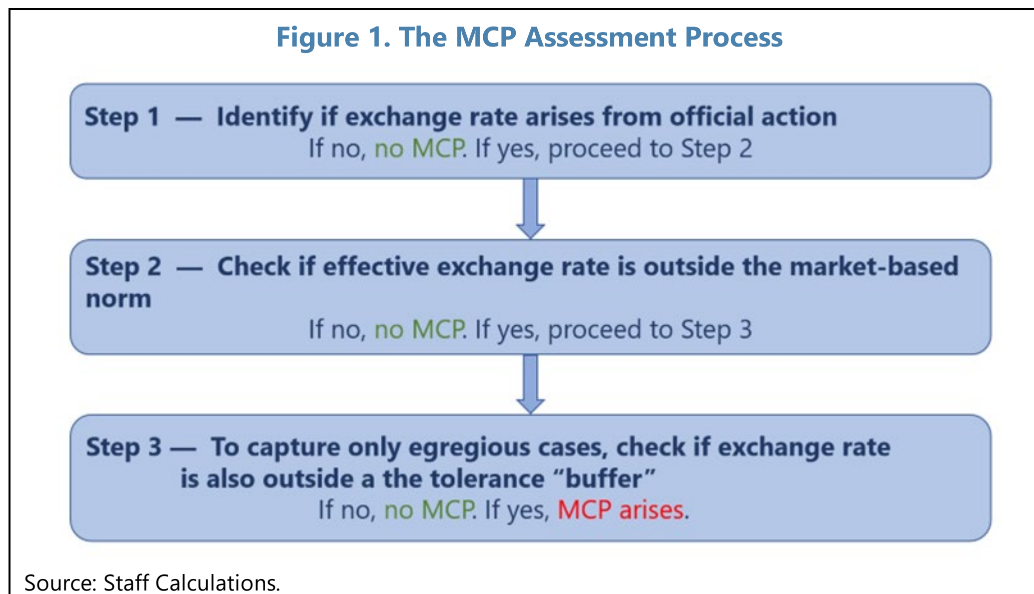
Annex II. Technical Aspects of Monitoring Spreads

A. The New Methodology: A Three-Step Assessment Process

1. The framework for assessing the existence of an MCP under the new policy is based on three distinct stages, for both spot and non-spot FX transactions (Figure 1).

- First, staff should ascertain whether an exchange rate has arisen from official action as defined in the MCP policy. If the measure is identified as official action, staff would proceed to the next step.
- Second, staff should compare the effective exchange rate arising from the official action (hereafter 'R') with the market-based norm, that is whether R is within range of the highest (H) and lowest (L) wholesale exchange rates of the trading day. If it is, there is no MCP. If R is beyond the H/L range, staff would proceed to the next step.
- The last step consists of examining if R exceeds the tolerance margin of +/- 2 percent of the mid H/L of the day, which is set to avoid capturing insignificant deviations from the market norm. If R is within the tolerance margin, there is no MCP. If R is outside of the tolerance margin, an MCP would arise.

Figure 1. The MCP Assessment Process



Source: Staff Calculations.

B. Market-Based Norm and Tolerance Margin

2. The permissible spread is determined by a country-specific market-based norm and the tolerance margin, building upon the exchange rate determined on the country's wholesale FX market. The methodology sets market-based boundaries for the effective exchange rate arising from official action, determined by the highest (H) and lowest (L) exchange rates in the member's wholesale FX market on a given day. The daily H and L on a wholesale FX market will be

primarily collected from benchmark data providers (LSEG Eikon, Bloomberg) and would generally be considered representative of the FX market. In rare cases when such data is not available from these data providers or appear to be manifestly irregular or inaccurate, exchange rate data from other sources can be used. Such alternative data sources include the following: (i) publicly available independent data source, (ii) publicly available data from the authorities, or (ii) other data from the authorities. In all these cases staff would determine whether the data are representative of the market. Only exchange rate data representative of the FX market will be used for assessments under the MCP policy. For non-spot transactions the assessment can be concluded even in the absence of representative market data if the theoretical price of the non-spot transaction can be calculated.

3. **Staff is expected to determine whether the alternative data are representative of the FX market.** In each case of using alternate data-source other than the primary and secondary data-providers, staff need to assess whether the exchange rate data have been computed in compliance with the IOSCO principles for the computation of financial benchmarks (see Box 1). As part of this assessment, staff may consider the underlying data contributors, dataset and the methodology used to derive the exchange rates being used.

4. **In cases where alternative data is used, and there is more than one wholesale FX market, the exchange rates determined on the largest market are considered representative of the market exchange rates.** The largest market is usually determined by FX turnover but other factors such as the number of active participants etc. could also inform staff's judgment. The data needed to identify the principal market can be obtained either from the benchmark data providers or from reliable independent sources or from the authorities. Private or semi-private entities that own and/or operate FX trading platforms can be alternative sources of information on the volume of transactions that are conducted on the platforms.

5. **If representative wholesale FX market data does not exist, exchange rate data from other segments that are representative of the FX market can be used to determine the permissible margin.** Depending on the specific conditions in the country, the wholesale FX market, the bank-client FX market or the exchange bureaus–client market or the combination of these may provide representative exchange rates that can be used for the MCP assessment.

Box 1. IOSCO Key Principles for Financial Benchmarks

Replicability: This refers to the market participants' ability to adopt a trading strategy that could provide them a tradable price/exchange rate as close as possible to the reference rate.

Transparency: Reference rates should be produced based on clear rules, including transparent fallback procedures for periods of market stress. Governing rules should be well-known, computational methodology should be publicly documented and supported by continuous monitoring.

Reliability: The reliability of the FX reference rate – the extent to which their governance and administration adequately safeguard against manipulation and error. The process to change the computation method should be explained in the computation guideline and any changes in the computation method should allow consultation with market participants.

Box 1. IOSCO Key Principles for Financial Benchmarks (concluded)

Availability: The reference rate should be available at sufficient frequency to all market participants to allow the pricing of contracts on an ongoing basis, through most convenient means of publication.

Accountability: The reference rates should be readily available to facilitate verification. Oversight of the computation agent should be in place to audit the benchmark regularly; this will address possible challenges from market participants. The benchmark administrator should keep a record of all inputs in the computation of the benchmark for at least 12 months.

6. **In the rare case in which there is no local FX market, the closest exchange rate equivalent to a "market" rate should be used to determine the tolerance margin.** A typical illustration would be a fixed exchange rate regime with a buying rate and a selling rate and no FX market outside the central bank. This would be the case for example when in a pegged exchange rate regime, all FX inflows are subject to surrender to the authorities and thus there are no interdealer transactions; the CB sells FX to intermediaries. In these cases, the wholesale reference rate is the mid-rate between the rate at which the authorities capture FX revenues through the surrender requirement (buying rate) and the rate at which they redistribute them (selling rate). In such circumstances, no MCP would arise as long as the rates arising from official action remain in the +/- 2 percent tolerance margin from the mid of the official buying and selling rates.

7. **In countries with no separate legal tender exchange rate data from the FX market of the country whose legal tender has been adopted should be used to determine the permissible margins.** When retrieving data, staff should be conscious about the possible time zone differences between the two countries and use the exchange rate data which overlaps with the opening hours of the local FX market.[1]

8. **One single deviation from the permissible margin is sufficient for an MCP to arise.** Once an official action is identified, the monitoring of the exchange rate arising from the official action must therefore be conducted on a continuous basis to assess any deviation from the permissible margin (see paragraph 43 of the Guidance Note). The monitoring of the exchange rate should be daily in the period between the end of the mission and the Board consideration/meeting.

C. Monitoring Exchange Rates and Reporting Deviations from Permissible Spreads

9. **Country teams—and country authorities—are responsible for monitoring the effective exchange rate arising from official action as well as the H and L market exchange rates to ascertain whether a breach of the permissible spread has occurred.** Exchange rates arising from existing and new official actions require systematic continuous monitoring by the country team.

[1] The overlap time zone with any of the major trading centers like London, NY, Frankfurt, Tokyo, Singapore can be used when a major currency is adopted as a legal tender. Moreover, all these major trading centers trade major currencies twenty-four hours globally.

Data on the exchange rate arising from official action can be gathered from public sources (e.g., HAVER), members, for instance from the website of the central bank, or by requesting the data directly from the authorities. If the member has in place measures that constitute official actions under the MCP policy and could thus give rise to an MCP, staff should have understandings with the authorities on the reporting of the exchange rates data relevant for MCP assessments.[2]

10. The monitoring starts with downloading the market H and L data from the benchmark data providers (see Annex V ol) and the exchange rate arising from the official action into a pre-designed forthcoming monitoring tool for automated testing against the market norm and the tolerance margin. The monitoring tool already includes the MCP methodology in the "Test" worksheet, so that the quantitative assessment can be performed automatically. The test should be run on a continued basis (see paragraph 9 of this annex) to detect an MCP in a timely manner except in those cases where the monitoring needs to happen in predetermined dates for example for settlements between central banks under BPAs.

11. The forthcoming monitoring tool will flag any instance of breach that gives rise to an MCP Once the breach has been confirmed, the country team should promptly inform relevant functional departments staff and the authorities. (See Section V).

D. Selected Hypothetical Examples of Exchange Rates Subject to Monitoring

Lagged Official Exchange Rates[3]

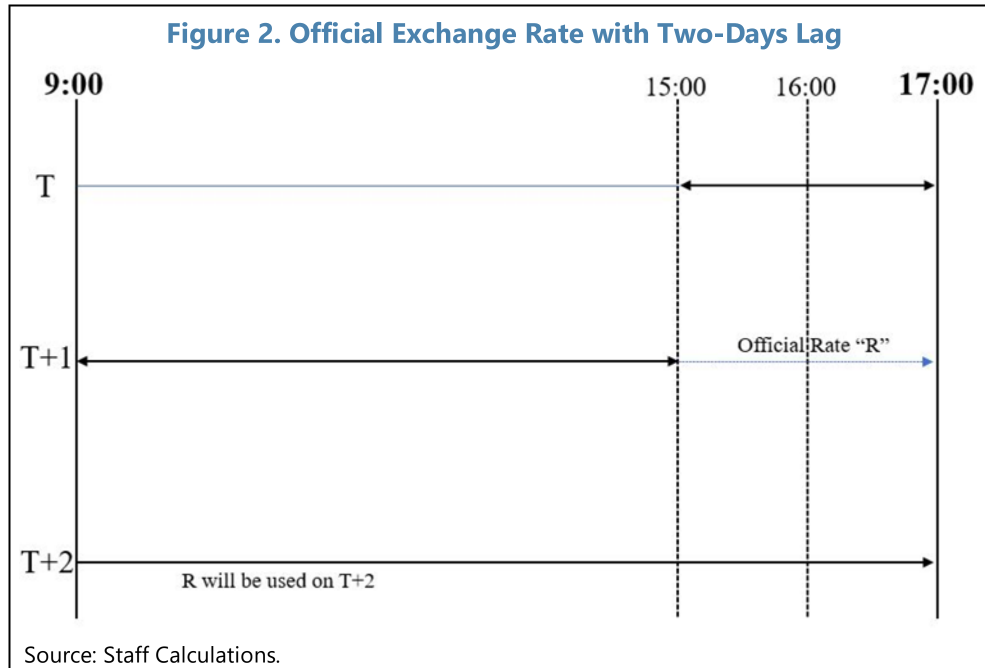
12. Country A's central bank uses the official exchange rate for government transactions (official action). The central bank announces the official exchange rate (R/USD) at 16:00 every trading day (see Figure 2). The official exchange rate is determined as the weighted average interbank market exchange rates from 15:00 on the previous trading day (T) to 15:00 on the current trading day (T+1). The government trades with the central bank the next day (T+2) using this official rate calculated on the current day (T+1). Te official exchange rate cannot be considered as meeting the criteria for the one-day lagged exchange rate which would not give rise to an MCP. It does not meet the criterion to include only transactions that occurred the day (T+1) immediately preceding the day when the official exchange rate is used (T+2) as it includes transactions from 2 different days (the transactions between 15:00 and 17:00 on T and the transactions until 15:00 on T+1), and it includes transactions from 2 days before. Furthermore, it does not meet the criterion that it should include all transactions in the wholesale market of the previous day as it excludes transactions

[2] Alternative data sources for FX market exchange rates 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) data from the authorities. See also Section VII.D.

[3] The same treatment applies to any other reference rate computed and published by authorities that is required to be used for actual exchange transactions.

occurred after 15:00 on T. Thus, the exchange rate would need to be monitored, since in this example this is used for government transactions.

Figure 2. Official Exchange Rate with Two-Days Lag



Source: Staff Calculations.

13. To verify if the lagged official exchange rate is within the permissible margins staff should obtain the necessary data to apply the methodology. In this case, we assume that the interbank market rate is the representative market exchange rate and that the interbank market data (R/USD) is available on LSEG Eikon. The corresponding H/L can then be downloaded from the same source. Staff should insert the currency first, and then set the start date and the end date of the observation period in the Excel file. The official exchange rate data (starting from the date of the official action or the last 12 months) should be obtained, for example, from the central bank's website, and manually entered into the Excel file. By including the official exchange rate and the H/L data into the forthcoming monitoring tool for automated testing against the market norm and the tolerance margin, the trading days with MCP findings will be flagged. Although the official action does not meet the criteria for one day lagged exchange rate to be outside of the MCP policy, no impermissible spreads are found in the assessment period of May 2–23, 2022 (Figure 3). However, the official exchange rates are outside the daily H/L on several days, and they are also outside the +/-2 percent tolerance margin in 9 cases in the period of November 26, 2021–February 8, 2022, thus resulting in an MCP (see Figure 4 below).

Figure 3. Official Exchange Rate with Two-Days Lag: No Cases of an Impermissible Spreads Identified in the Assessment Period

	A	B	C	D	E	F	G	H	I	J	K	L	M
1	Insert currency, start date, end date in Column B from the selected data source. Insert the market high and low in columns C and D respectively & official rate data in column D. The current marke												
2	Currency	XYZ=											
3	Market rate (Source)												
4	Start Date	31-Jul-21											
5	End Date	03-Aug-22	Note: MCP assessment to be done latest till t-1 date.										
6	Date	High (H_t)	Low (L_t)	R (official rate)		$M_{H/L}$	$M_{H/L}$ +2%	$M_{H/L}$ -2%		MCP test	Total findings	Days since last MCP	Date Last MCP
7	8/3/22	36.24	36.00	36.16		36.12	36.84	35.40		no MCP	0	0	#N/A
8	8/2/22	36.22	35.98	36.14		36.10	36.82	35.37		no MCP			
9	8/1/22	36.19	35.96	36.11		36.08	36.80	35.35		no MCP			
10	7/31/22	36.17	35.93	36.09		36.05	36.77	35.33		no MCP			
11	7/30/22	36.15	35.91	36.07		36.03	36.75	35.31		no MCP			
12	7/29/22	36.13	35.89	36.05		36.01	36.73	35.29		no MCP			
13	7/28/22	36.11	35.87	36.03		35.99	36.71	35.27		no MCP			
14	7/27/22	36.09	35.85	36.01		35.97	36.69	35.25		no MCP			
15	7/26/22	36.06	35.83	35.98		35.95	36.66	35.23		no MCP			
16	7/25/22	36.04	35.81	35.96		35.92	36.64	35.21		no MCP			
17	7/24/22	36.02	35.78	35.94		35.90	36.62	35.18		no MCP			
18	7/23/22	36.00	35.76	35.92		35.88	36.60	35.16		no MCP			
19	7/22/22	35.98	35.74	35.90		35.86	36.58	35.14		no MCP			
20	7/21/22	35.96	35.72	35.88		35.84	36.55	35.12		no MCP			
21	7/20/22	35.93	35.70	35.85		35.82	36.53	35.10		no MCP			
22	7/19/22	35.91	35.68	35.83		35.79	36.51	35.08		no MCP			
23	7/18/22	35.89	35.66	35.81		35.77	36.49	35.06		no MCP			
24	7/17/22	35.87	35.63	35.79		35.75	36.47	35.04		no MCP			
25	7/16/22	35.85	35.61	35.77		35.73	36.45	35.02		no MCP			
26	7/15/22	35.83	35.59	35.75		35.71	36.42	34.99		no MCP			
27	7/14/22	35.81	35.57	35.73		35.69	36.40	34.97		no MCP			
28	7/13/22	35.78	35.55	35.70		35.67	36.38	34.95		no MCP			
29	7/12/22	35.76	35.53	35.68		35.64	36.36	34.93		no MCP			
30	7/11/22	35.74	35.51	35.66		35.62	36.34	34.91		no MCP			
31	7/10/22	35.72	35.48	35.64		35.60	36.31	34.89		no MCP			
32	7/9/22	35.70	35.46	35.62		35.58	36.29	34.87		no MCP			
33	7/8/22	35.68	35.44	35.60		35.56	36.27	34.85		no MCP			
34	7/7/22	35.66	35.42	35.58		35.54	36.25	34.83		no MCP			
35	7/6/22	35.63	35.40	35.55		35.52	36.23	34.81		no MCP			
36	7/5/22	35.61	35.38	35.53		35.50	36.21	34.79		no MCP			
37	7/4/22	35.59	35.36	35.51		35.47	36.18	34.76		no MCP			
38	7/3/22	35.57	35.34	35.49		35.45	36.16	34.74		no MCP			
39	7/2/22	35.55	35.31	35.47		35.43	36.14	34.72		no MCP			
40	7/1/22	35.53	35.29	35.45		35.41	36.12	34.70		no MCP			

Source: Staff Calculations.

Figure 4. Official Exchange Rate with Two-Days Lag: An Example of 9 Cases of an Impermissible Spreads Identified in the Assessment Period

	A	B	C	D	E	F	G	H	I	J	K	L	M
1	Insert currency, start date, end date in Column B from the selected data source. Insert the market high and low in columns C and D respectively & official rate data in column D. The current market												
2	Currency	XYZ=											
3	Market rate (Source)												
4	Start Date	31-Jul-21											
5	End Date	03-Aug-22	Note: MCP assessment to be done latest till t-1 date.										
6	Date	High (H_t)	Low (L_t)	R (official rate)		$M_{H/L}$	$M_{H/L}$ +2%	$M_{H/L}$ -2%		MCP test	Total findings	Days since last MCP	Date Last MCP
7	8/3/22	38.23	36.59	36.16		37.41	38.16	36.66		MCP finding	9	0	03-Aug-22
8	8/2/22	37.96	36.23	36.14		37.10	37.84	36.35		MCP finding			
9	8/1/22	36.19	35.96	36.11		36.08	36.80	35.35		no MCP			
10	7/31/22	36.17	35.93	36.09		36.05	36.77	35.33		no MCP			
11	7/30/22	36.15	35.91	36.07		36.03	36.75	35.31		no MCP			
12	7/29/22	36.13	35.89	36.05		36.01	36.73	35.29		no MCP			
13	7/28/22	36.11	35.87	36.03		35.99	36.71	35.27		no MCP			
14	7/27/22	36.09	35.85	36.01		35.97	36.69	35.25		no MCP			
15	7/26/22	36.06	35.83	35.98		35.95	36.66	35.23		no MCP			
16	7/25/22	36.04	35.81	35.96		35.92	36.64	35.21		no MCP			
17	7/24/22	37.72	36.01	35.94		36.87	37.60	36.13		MCP finding			
18	7/23/22	36.00	35.76	35.92		35.88	36.60	35.16		no MCP			
19	7/22/22	35.98	35.74	35.90		35.86	36.58	35.14		no MCP			
20	7/21/22	35.96	35.72	35.88		35.84	36.55	35.12		no MCP			
21	7/20/22	35.93	35.70	35.85		35.82	36.53	35.10		no MCP			
22	7/19/22	36.89	36.24	35.83		36.57	37.30	35.83		MCP finding			
23	7/18/22	35.89	35.66	35.81		35.77	36.49	35.06		no MCP			
24	7/17/22	35.87	35.63	35.79		35.75	36.47	35.04		no MCP			
25	7/16/22	35.85	35.61	35.77		35.73	36.45	35.02		no MCP			
26	7/15/22	35.83	35.59	35.75		35.71	36.42	34.99		no MCP			
27	7/14/22	35.81	35.57	35.73		35.69	36.40	34.97		no MCP			
28	7/13/22	36.96	36.33	35.70		36.65	37.38	35.91		MCP finding			
29	7/12/22	36.88	36.22	35.68		36.55	37.28	35.82		MCP finding			
30	7/11/22	35.74	35.51	35.66		35.62	36.34	34.91		no MCP			
31	7/10/22	35.72	35.48	35.64		35.60	36.31	34.89		no MCP			
32	7/9/22	35.70	35.46	35.62		35.58	36.29	34.87		no MCP			
33	7/8/22	35.68	35.44	35.60		35.56	36.27	34.85		no MCP			
34	7/7/22	36.82	36.01	35.58		36.42	37.14	35.69		MCP finding			
35	7/6/22	36.78	35.99	35.55		36.39	37.11	35.66		MCP finding			
36	7/5/22	36.71	35.82	35.53		36.27	36.99	35.54		MCP finding			
37	7/4/22	35.59	35.36	35.51		35.47	36.18	34.76		no MCP			
38	7/3/22	35.57	35.34	35.49		35.45	36.16	34.74		no MCP			
39	7/2/22	35.55	35.31	35.47		35.43	36.14	34.72		no MCP			
40	7/1/22	35.53	35.29	35.45		35.41	36.12	34.70		no MCP			

Source: Staff Calculations.

FX Auctions

14. Multiple-price FX Auctions. The Central Bank (CB) of Country A buys FX from intermediaries (all commercial banks) through daily multiple-price auctions to manage its FX reserves. To select the winning bids, the CB arranges the bids from the cheapest (the most appreciated rate) to the most expensive. The CB retains the discretion to purchase more or less than the announced amount depending on market conditions. In the event the CB decides to accept bids, it determines a cut-off point according to the following criteria: accepted bids shall be priced at rates that do not deviate by more than 1 percent (i) from each other and (ii) from the interbank mid rates at the time of the auction. In this case, the auction does not meet the criteria for best practice[4] as it fails to meet the allotment criterion on best price principle and include a reference price to reject some bids. As a result the auction is considered as segmenting the FX market and thus the exchange rates arising from it need monitoring.

Figure 5. FX Auction: An Example of Several Cases of Impermissible Spreads Identified in the Assessment Period

High (H_t)	Low (L_t)	R (WAR)	$M_{H/L}$	$M_{H/L}$ +2%	$M_{H/L}$ -2%	MCP test
123.87	117.03	117.15	120.45	122.86	118.04	no MCP
122.99	117.39	117.08	120.19	122.59	117.78	MCP finding
123.02	117.32	117.01	120.17	122.57	117.76	MCP finding
123.04	117.25	116.94	120.15	122.55	117.74	MCP finding
123.07	117.18	116.87	120.12	122.53	117.72	MCP finding
123.09	117.11	116.80	120.10	122.51	117.70	MCP finding
123.12	117.05	116.73	120.08	122.48	117.68	MCP finding
123.15	116.98	116.66	120.06	122.46	117.66	MCP finding
123.17	116.91	116.59	120.04	122.44	117.64	MCP finding
123.20	116.84	116.52	120.02	122.42	117.62	MCP finding
123.22	116.77	116.45	120.00	122.40	117.60	MCP finding
123.25	116.71	116.38	119.98	122.38	117.58	MCP finding
123.27	116.64	116.31	119.96	122.36	117.56	MCP finding
123.30	116.57	116.24	119.94	122.33	117.54	MCP finding
123.33	116.50	116.17	119.91	122.31	117.52	MCP finding
123.35	116.44	116.10	119.89	122.29	117.50	MCP finding
123.38	116.37	116.03	119.87	122.27	117.48	MCP finding
123.40	116.30	115.96	119.85	122.25	117.46	MCP finding
123.43	116.23	115.89	119.83	122.23	117.44	MCP finding
123.46	116.17	115.82	119.81	122.21	117.41	MCP finding
123.48	116.10	115.75	119.79	122.19	117.39	MCP finding
123.51	116.03	115.68	119.77	122.16	117.37	MCP finding
123.53	115.96	115.61	119.75	122.14	117.35	MCP finding
123.56	115.90	115.54	119.73	122.12	117.33	MCP finding
123.59	115.83	115.47	119.71	122.10	117.31	MCP finding
123.61	115.76	115.40	119.69	122.08	117.29	MCP finding
123.64	115.69	115.33	119.67	122.06	117.27	MCP finding
123.66	115.63	115.27	119.65	122.04	117.25	MCP finding
123.69	115.56	115.20	119.63	122.02	117.23	MCP finding
123.72	115.49	115.13	119.60	122.00	117.21	MCP finding
123.74	115.43	115.06	119.58	121.98	117.19	MCP finding
123.77	115.36	114.99	119.56	121.95	117.17	MCP finding
123.79	115.29	114.92	119.54	121.93	117.15	MCP finding
123.82	115.23	114.85	119.52	121.91	117.13	MCP finding

Source: Staff Calculations.

15. An MCP would arise if the auction exchange rate exceeds the permissible margins. In this case we assume that the interbank market rate is the representative exchange rate. As a result, the spot wholesale market rate is the reference used for the H/L and the mid of the H/L, to which

[4] See paragraph 8 of the Guidance Note for a discussion of the criteria for FX auctions that are not considered official action under the MCP policy.

the tolerance margin is applied. The weighted average rate (WAR) of successful bids constitutes the rate arising from official action (R). The estimated data are collected over the sample as described in paragraph 43. After including the data into the monitoring tool, many impermissible spreads can be observed in this period, which gives rise to an MCP (Figure 5).

Exchange Taxes

16. Exchange taxes on the market exchange rate. Before applying the MCP methodology to exchange taxes, it needs to be determined if the tax is related closely enough to the exchange of currencies to be considered part of the effective exchange rate by increasing the cost of the exchange transaction. If taxes closely related to exchange transactions and are levied on the market exchange rates (including either the wholesale market exchange rate or the bank-client exchange rate), the tax is deemed to be levied on the mid of the daily H/L and thus the effective exchange rate which is compared with the H/L of the same day and the 2 percent tolerance buffer would be R=Mid H/L*(1+Tax). Staff need to consider different scenarios to decide if the monitoring of the effective exchange rate is needed.

(i) If the tax does not exceed 2 percent (and there are no other mandatory costs imposed by the authorities on the underlying exchange transaction), it would not result in an MCP as the effective exchange rate would remain within the tolerance buffer of +/- 2 percent measured on the Mid of the H/L of the wholesale market exchange rate.

(ii) If the tax is more than 2 percent, staff needs to monitor on a continuous basis if the effective exchange rate resulting from the tax gives rise to an MCP. Since in this case the existence of an MCP depends on whether the effective exchange rate is within the daily H/L of the market exchange rate, the same tax may or may not give rise to an MCP. For example, if the tax is 3 percent and the H/L is consistently wider than the +/-2 percent band so much that although the effective exchange rate exceeds the +/- 2 percent tolerance buffer but it remains within the daily H/L, no MCP would be found. However, if during the observation period, the H/L becomes narrower even for one day and thus the effective exchange rate exceeds the H/L, a tax of 3 percent levied on market exchange rates would give rise to an MCP.

17. Exchange taxes on exchange rates arising from official action (e.g., official exchange rate). In country A, exchange transactions for payments of certain luxury goods are subject to a specific official exchange rate of x S for 1 USD ("S" is the local currency). There is also a 1.5 percent stamp duty on FX transactions for imports. Since the stamp duty is set by an official action and payable on the exchange transactions, it will be considered part of the effective exchange rate, which gives the effective exchange rate R = x * (1+0.015). According to the methodology, this effective exchange rate will be compared to the H/L of the wholesale FX market and the tolerance buffer of 2 percent of the mid H/L of the same day. Depending on the official exchange rate and the permissible margins, the effective exchange rate may exceed the permissible margins and thus the tax of 1.5 percent (i.e., less than 2 percent) can give rise to an MCP. In a hypothetical case shown as below (see Figures 6 and 7), the effective exchange rate R is occasionally outside of the tolerance margin, therefore, it gives rise to MCPs.

Figure 6. Exchange Tax on Exchange Rate Arising from Official Action: An Example of 6 Cases of an Impermissible Spreads Identified in the Assessment Period

Market rate (Source)											
Start Date	31-Jul-21										
End Date	03-Aug-22	Note: MCP assessment to be done latest till t-1 date.									
Date	High (H_t)	Low (L_t)	R (official rate)	R (effective rate)	$M_{H/L}$	$M_{H/L}$ +2%	$M_{H/L}$ -2%	MCP test	Total findings	Days since last MCP	Date Last MCP
8/3/22	92.90	87.77	91.23	90.83	90.34	92.14	88.53	no MCP	6	1	02-Aug-22
8/2/22	92.24	88.04	91.34	92.36	90.14	91.94	88.34	MCP finding			
8/1/22	92.26	87.99	91.45	91.06	90.13	91.93	88.32	no MCP			
7/31/22	92.28	87.94	91.57	91.17	90.11	91.91	88.31	no MCP			
7/30/22	92.30	87.89	91.68	91.28	90.09	91.90	88.29	no MCP			
7/29/22	92.32	87.83	91.79	91.39	90.08	91.88	88.28	no MCP			
7/28/22	92.34	87.78	91.91	92.56	90.06	91.86	88.26	MCP finding			
7/27/22	92.36	87.73	92.02	91.62	90.05	91.85	88.25	no MCP			
7/26/22	92.38	87.68	92.13	91.73	90.03	91.83	88.23	no MCP			
7/25/22	92.40	87.63	92.24	91.85	90.01	91.81	88.21	no MCP			
7/24/22	92.42	87.58	92.36	91.96	90.00	91.80	88.20	no MCP			
7/23/22	92.44	87.53	92.04	92.07	89.98	91.78	88.18	no MCP			
7/22/22	92.46	87.48	91.72	92.19	89.97	91.77	88.17	no MCP			
7/21/22	92.48	87.43	91.40	92.30	89.95	91.75	88.15	no MCP			
7/20/22	92.49	87.38	91.09	92.41	89.94	91.73	88.14	no MCP			
7/19/22	92.51	87.33	90.77	92.53	89.92	91.72	88.12	MCP finding			
7/18/22	92.53	87.28	90.46	92.49	89.90	91.70	88.11	no MCP			
7/17/22	92.55	87.23	90.15	91.86	89.89	91.69	88.09	no MCP			
7/16/22	92.57	87.17	89.83	91.24	89.87	91.67	88.08	no MCP			
7/15/22	92.59	87.12	89.52	90.62	89.86	91.66	88.06	no MCP			
7/14/22	92.61	87.07	89.21	90.00	89.84	91.64	88.05	no MCP			
7/13/22	92.63	87.02	88.91	89.39	89.83	91.62	88.03	no MCP			
7/12/22	92.65	86.97	88.60	88.79	89.81	91.61	88.02	no MCP			
7/11/22	92.67	86.92	88.29	88.18	89.80	91.59	88.00	no MCP			
7/10/22	92.69	86.87	87.99	87.59	89.78	91.58	87.99	no MCP			
7/9/22	92.71	86.82	87.68	86.99	89.77	91.56	87.97	no MCP			
7/8/22	92.73	86.77	87.38	86.40	89.75	91.54	87.95	MCP finding			
7/7/22	92.75	86.72	87.08	85.82	89.73	91.53	87.94	MCP finding			
7/6/22	92.77	86.67	86.78	87.82	89.72	91.51	87.92	no MCP			
7/5/22	92.79	86.62	86.88	87.23	89.70	91.50	87.91	no MCP			
7/4/22	92.81	86.57	86.99	86.64	89.69	91.48	87.89	no MCP			
7/3/22	92.83	86.52	87.10	86.05	89.67	91.47	87.88	MCP finding			
7/2/22	92.85	86.47	87.21	89.88	89.66	91.45	87.86	no MCP			
7/1/22	92.86	86.42	87.31	89.27	89.64	91.43	87.85	no MCP			

Source: Staff Calculations.

Figure 7. Exchange Tax on Exchange Rate Arising from Official Action: An Example of 6 Cases of Impermissible Spreads Identified in the Assessment Period

Source: Staff Calculations.

Cash Margin Deposit Requirement

18. Unremunerated cash margin deposit requirement is imposed by the authorities for certain imports. In country A, the local currency is 'S' and the authorities introduce a requirement that each letter of credit (LC) opened for payment of imports of certain goods, should be covered by an unremunerated 100 percent cash margin deposit (official action). The cash margin is usually deposited in local currency for the duration of LCs which typically varies within a 3–6 months-term. The margin deposits may be used to make the relevant import payments under the LC after conversion to FX. The additional cost of the cash margin arises from the unremunerated nature of the requirement (see paragraph 10 of the Guidance Note), at the time when, according to statistical data from the central bank website, the annual interest rate on customers' fixed deposits for 3 months is 15 percent and for 6 months is 25 percent.

19. The additional cost arising from the cash margin requirement is considered so closely related to the exchange transaction that it should be considered as part of the effective exchange rate. Thus, the effective exchange rate that includes the additional cost of the cash margin deposit requirement needs to be calculated to determine if the official action gives rise to an MCP. The calculation of the effective exchange rate depends on whether it is applied on the market exchange rate or the exchange rates arising from official action.

- **Cash margin requirement is applied to the exchange rates arising from official action (e.g., official exchange rate).** For a 100 percent cash margin requirement (G=1) of 6 months (T=0.5) with no remuneration (i_g = 0), where market annual interest rates for the duration of the cash margin requirement is 25 percent (i_k = 0.25)[5] and the official exchange rate required by the authorities to be used for import payments (DC) is 200 S for 1 USD, the additional cost of the transaction is 200*(0.25-0)*1*0.5=25 S, resulting in an effective exchange rate of (200+25)=225 S. This effective exchange rate has to be compared with the daily H/L of given day on the wholesale FX market and the tolerance margin (+/-2 percent of mid H/L) to determine if the effective exchange rate gives rise to an MCP.

- **Cash margin requirement is applied to the market exchange rates.** If a cash margin applies on market exchange rates, the cash margin is deemed to be levied on the mid of the daily H/L of the day and thus the effective exchange rate is compared with the daily H/L of given day on the wholesale FX market and the tolerance buffer. Assuming that the mid of the daily H/L of the day is 200 S for 1 USD and G, T, i_g, i_k are the same, the calculation of the effective exchange rate is the same as in the previous bullet.

Subsidies

20. Like exchange taxes, exchange subsidies arising from an official action can give rise to MCPs. A subsidy provided on or closely related to an exchange transaction would be considered as

[5] If the interest rates change during lifetime of the cash margin requirement, the updated interest rates should be factored in the calculation of the effective exchange rate.

part of the effective exchange rate. For the assessment of subsidies under the MCP policy, first the effective exchange rate of the transaction has to be calculated. The effective exchange rate for the purchase of FX for import payments is calculated by subtracting the subsidy from the nominal exchange rate. In the case of the export of certain goods, the subsidized effective exchange rate used for the sale of such FX export proceeds will be calculated by adding the amount of subsidy to the nominal exchange rate used for the sale of export proceeds. If the subsidy is levied on the market exchange rates, like in case of exchange taxes, the subsidy is deemed to be levied on the mid of the daily H/L and thus the effective exchange rate is compared with the H/L of the same day and the +/-2% tolerance margin. If the subsidy is levied on an exchange rate arising from official action, like in case of exchange taxes, it will be considered part of the effective exchange rate and thus the effective exchange rate would need to be compared on a daily basis with the permissible margins (the daily H/L of the wholesale market and the +/-2% tolerance margin).

- **Incentive Schemes (exchange rate subsidies).** To encourage worker remittances into the country, the authorities of country A decide to pay exchange rate subsidy of X units of local currency for each dollar in addition to the official exchange rates used by banks for purchases of FX from inward remittances. For the MCP assessment, the effective exchange rate on a particular day (R_t) is computed by adding the incentive X to the nominal official exchange rate of that day applicable for the transaction and compared with the H_t/L_t and the +/- 2 percent tolerance margin around the mid H_t/L_t. If R_t is outside of the permissible margins an MCP would arise.

- **Subsidy for imports of essential goods.** Country A decided to implement an exchange rate subsidy by compensating importers with X units of local currency for each dollar purchased at the market exchange rate to pay for such imports. For the MCP assessment, the effective exchange rate on a particular day (R_t) is computed by subtracting the subsidy from the mid of the daily H_t/L_t of that day and thus the effective exchange rate compared with H_t/L_t and the +/-2 percent tolerance margin around the mid H_t/L_t. If R_t is outside of the permissible margins an MCP would arise.

Non-Spot Transactions

21. **FX forwards**. Here we use the example of a 1-year FX forward to illustrate how the non-spot transactions are assessed. Assuming the official action (e.g., the FX forward between the central bank and a commercial bank) and thus the observation period runs from Feb 9, 2021, to Feb 8, 2022, the representative tenor forward rate (in this case 1-year) of the currency pair of the wholesale forward market should be used to compare with the forward rate affected by the official action. Figure 8 indicates 44 MCP findings during all the transaction days (just shows one case on Jan 18, 2022) and Figure 9 depicting the rates outside the margin, shows that these forward exchange rates are not within either the H/L of the prevailing market forward rates for the same maturity or the additional tolerance margin, thus giving rise to an MCP. (see Box 2 for further elaboration)

Figure 8. FX Forwards: An Example of an Impermissible Spreads Identified in the Assessment Period

Date	High	Low	R (official rate)	$M_{H/L}$	$M_{H/L}$ +2%	$M_{H/L}$ -2%	Test	Total findings	Days since last MCP	Date Last MCP
8/3/22	158.34	151.63	154.42	154.99	158.09	151.89	no MCP	1	33	02-Jul-22
8/2/22	159.24	152.50	152.75	155.87	158.99	152.75	no MCP			
8/1/22	160.14	153.36	153.62	156.75	159.89	153.62	no MCP			
7/31/22	161.05	154.23	154.49	157.64	160.80	154.49	no MCP			
7/30/22	161.97	155.11	155.37	158.54	161.71	155.37	no MCP			
7/29/22	162.89	155.99	156.25	159.44	162.63	156.25	no MCP			
7/28/22	163.81	156.88	157.14	160.34	163.55	157.14	no MCP			
7/27/22	164.74	157.77	158.03	161.25	164.48	158.03	no MCP			
7/26/22	165.68	158.66	158.93	162.17	165.41	158.93	no MCP			
7/25/22	166.62	159.56	159.83	163.09	166.35	159.83	no MCP			
7/24/22	167.57	160.47	160.74	164.02	167.30	160.74	no MCP			
7/23/22	168.52	161.38	161.65	164.95	168.25	161.65	no MCP			
7/22/22	169.47	162.30	162.57	165.89	169.20	162.57	no MCP			
7/21/22	170.44	163.22	163.49	166.83	170.16	163.49	no MCP			
7/20/22	171.40	164.15	164.42	167.78	171.13	164.42	no MCP			
7/19/22	172.38	165.08	165.35	168.73	172.10	165.35	no MCP			
7/18/22	173.36	166.02	166.29	169.69	173.08	166.29	no MCP			
7/17/22	174.34	166.96	167.24	170.65	174.06	167.24	no MCP			
7/16/22	175.33	167.91	168.19	171.62	175.05	168.19	no MCP			
7/15/22	176.33	168.86	169.14	172.59	176.05	169.14	no MCP			
7/14/22	177.33	169.82	170.10	173.57	177.05	170.10	no MCP			
7/13/22	178.34	170.78	171.07	174.56	178.05	171.07	no MCP			
7/12/22	179.35	171.75	172.04	175.55	179.06	172.04	no MCP			
7/11/22	180.37	172.73	173.02	176.55	180.08	173.02	no MCP			
7/10/22	181.39	173.71	174.00	177.55	181.10	174.00	no MCP			
7/9/22	182.42	174.70	174.99	178.56	182.13	174.99	no MCP			
7/8/22	183.46	175.69	175.98	179.57	183.16	175.98	no MCP			
7/7/22	184.50	176.69	176.98	180.59	184.20	176.98	no MCP			
7/6/22	185.55	177.69	177.99	181.62	185.25	177.99	no MCP			
7/5/22	186.60	178.70	179.00	182.65	186.30	179.00	no MCP			
7/4/22	187.66	179.71	180.01	183.69	187.36	180.01	no MCP			
7/3/22	188.73	180.73	181.04	184.73	188.42	181.04	no MCP			
7/2/22	189.80	181.76	180.13	185.78	189.49	182.06	MCP finding			
7/1/22	190.88	182.79	183.10	186.83	190.57	183.10	no MCP			
6/30/22	191.96	183.83	184.14	187.89	191.65	184.14	no MCP			

Source: Staff Calculations.

Figure 9. FX Forwards: Examples of Impermissible Spreads Identified in the Assessment Period

Source: Staff Calculations.

Box 2. Non-Spot Transactions

Official actions can affect exchange rates of transactions with maturities longer than spot. Consistent with the methodology for spot transactions, such rates would be considered under the policy if the authorities use them in transactions or require that market participants use them, and if the official action creates market segmentation. Official actions can impact FX derivatives, including forwards, swaps, NDFs and options.

Forwards: The market norm for forward exchange rates arising from official action would be the daily H/L of the forward wholesale market. The market norm and the tolerance margin would be applied to the assessment of the exchange rate as in the case of spot transactions. An MCP would arise if the forward rate arising from official action (R_1) exceeds the H_t/L_t of the wholesale forward market rates for the same maturity and the tolerance margin, i.e., +/- 2 percent of the mid of the H_t/L_t. When interdealer rates are not available, the theoretical forward rate for the same maturity has to be calculated based on the interest rate differential in the relevant local and foreign markets.[1] An MCP would arise if the exchange rate resulting from official action (R_t) were to exceed+/- 2 percent tolerance margin of the theoretical price.

Swaps: Exchange rates of FX swaps arising from official action need to be assessed under the methodology. Hence, the spot rate would be assessed as any other spot rate. The spot exchange rates of the swap arising from the official action (R_t) should remain within the permissible margin of spot wholesale transactions, i.e., wholesale market H_t/L_t and the tolerance margin of +/-2 percent of the mid of the H_t/L_t. The forward rate arising from official action should be compared with the market forward rates for forwards with the same maturity. When wholesale market interdealer rates for forwards of the same maturity are not available, the theoretical price of the forward for the same maturity should be calculated as described above. The forward rate of the FX swap arising from official action (R_1) should remain (i) within the daily H_t/L_t of similar wholesale market forward rates and the tolerance margin (i.e., +/- 2 percent of the mid of the H_t/L_t.) or (ii) in the tolerance margin +/- 2 percent of the calculated theoretical price, to avoid an MCP.

The primary source of information for exchange rates for non-spot transactions is LSEG Eikon. The primary data source provides H/L forward rates quoted by interbank market participants for 76 currencies, where forward markets exist. Three can be sourced from Bloomberg as secondary source. Those forward exchange rates can be monitored continuously. In cases where wholesale forward market exchange rates from the benchmark providers are not available, or the exchange rate data appear manifestly irregular or inaccurate, data from alternative data sources can be used. If representative data from alternative sources is not available, theoretical prices must be used. The theoretical forward rate is computed as described above.

Options

Options to buy or sell FX arising from official action are assessed under the MCP policy only if exercised. For the assessment of the options, the effective exchange rate needs to be calculated. The effective exchange rate is the sum of the strike rate and the option premium. This effective exchange rate is compared with the daily H_t/L_t of wholesale market option exchange rates with similar terms (pull/put, currency, amount, maturity, type etc.) and the +/- 2 percent tolerance margin around the mid H_t/L_t. If such representative market data is not available, the theoretical price of such an option has to be calculated (see below). The effective exchange rate of an option so calculated needs to remain within the +/-2% tolerance margin of the theoretical price, to avoid an MCP.

In practice, the assessment of options would have to rely mainly on theoretical prices. Option markets are often not deep and standardized enough to provide relevant price benchmarks. However, both LSEG Eikon and Bloomberg provide the possibility to calculate theoretical option prices for a wide range of contracts, including “exotics.” The default setting is based on the data available to the benchmark administrator and their assumption regarding expected volatility. Staff would assess whether the default parameters used by the theoretical price calculator of Bloomberg are the most representative for the country. Staff may use alternative data sourced from local markets to change the parameters of the

Box 2. Non-Spot Transactions (concluded)

calculation, in particular implied volatility and the local currency interest rate, to obtain option prices. Alternative implied volatility should be based on prices formed in the domestic market that reflect expected exchange rate volatility. Alternative local interest rates should be based on actual cost of funding for the relevant maturities. In the absence of such information, the assessment would be based on the theoretical option price derived from the default setting of the calculator, depending on the type of option.[2]

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[1] The forthcoming monitoring tool will enable users to calculate theoretical forward prices by inputting the H_t and L_t wholesale spot market rate and the respective domestic and foreign interest rate. Staff may use alternative data from the domestic market if considered more representative of the funding rate than that used by the benchmark providers for a given maturity.

[2] Due to evolving trends in FX market sophistication, assessment of non-spot transactions may become more frequent under the MCP policy. There might be circumstances in which market related information on prices may be difficult to obtain or assessing non-spot exchange rates may be complex. Thus, further refinement of the methodology and guidance may be needed after more experience with assessing non-spot transactions is gained.

22. Non-Deliverable Forwards (NDFs). Under the MCP policy, official NDFs will be assessed if they are sufficiently closely related to a foreign exchange transaction. In addition, the MCP assessment would only consider NDFs if they are part of a scheme administered by central banks or other official entitles under which: (a) *NDFs are made available to a subset of intermediaries or end-users or are earmarked for specific transactions*, therefore segmenting the market, and (b) *NDFs are closely related to acquiring or selling foreign exchange*. All other NDFs are excluded from the policy. The benefit or the cost from the NDF will be considered part of the effective exchange rate of the exchange transaction. The exchange transaction can be any spot or non-spot transaction to which the NDF is closely related, and the effective exchange rate of the transaction will be assessed according to the relevant methodology. For the assessment the effective exchange rate of the transaction has to be determined. The effective exchange rate includes the benefit/cost arising from the NDF which is the difference between the market NDF rate and the rate at which the NDF is provided or required to be concluded by the authorities (official NDF). To determine the difference the official NDF rate would need to be compared with the H/L of the market NDF rates of the date for the same maturity. If market NDF rates are not available theoretical NDF rates can be calculated. The spread by which the official NDF exceeds the H/L of the market NDF rates or the difference between the theoretical NDF rate and the official NDF rate are the benefit that should be added to the nominal exchange rate of the exchange transaction to which the NDF is closely related. Please reference Annex V for further information on NDFs data retrieval.

Guarantee Rate Guarantee Schemes

23. Exchange Rate Guarantee Schemes. The authorities can put in place an exchange rate guarantee scheme to cover exchange rate risks for specific market participants (e.g., exporters). Depending on the features of the scheme, unless the scheme is self-financed, the compensation for exchange losses is considered to be part of the effective exchange rate (see also Annex IV). This is the case when the benefit of the coverage of exchange risk flows directly from exchange losses, and thus from the exchange transaction in which these losses are realized. For example, a country introduces an exchange rate guarantee scheme and provides 1.00 unit of domestic currency as

exchange rate support per U.S. dollar—i.e., if an exporter sells its FX at a market rate below a certain threshold per U.S. dollar (say X), the effective exchange rate (R) will be (X+1.00) per U.S. dollar. Alternatively, a country may set a fixed exchange rate under the export guarantee scheme allowing exporters to sell FX to the CB or the operator of the guarantee scheme at a fixed exchange rate. (R). The exporters' benefit is the difference between the lower market exchange rate and the fixed exchange rate provided by the authorities minus the premium, if any paid by the exporter for benefitting from the scheme.

Annex III. Bilateral Payment Arrangements

1. Since its creation, the Fund has promoted a multilateral system of trade and payments. One of the purposes of the Fund is to "assist in the establishment of a multilateral system of payments in respect of current transactions between members and in the elimination of foreign exchange restrictions which hamper the growth of world trade" (Article I (iv) of the Articles of Agreement). Historically, the Fund's policies on bilateralism and convertibility were extensively discussed by the Executive Board as members were transitioning from their reliance on bilateral payments arrangements prevalent in the post-war period to a multilateral system of payments for current transactions that the Fund was stablished to promote. The Fund was concerned that bilateralism could cause economic distortions and include restrictive and discriminatory features that would undermine a multilateral payment system. Accordingly, the Fund's policies on bilateralism and convertibility, set forth in several Board decisions,[1] aimed at eliminating exchange restrictions and the earliest possible establishment of a multilateral system of payments in respect of current transactions between members, affirming the link between those policies and the Fund's jurisdiction under Article VIII, Section 2(a) and 3.[2]

2. The Fund's policies on bilateralism and convertibility focus on bilateral payments arrangements (BPAs).[3] BPAs are formal or informal arrangements between two (or more) countries, under which there is established at least one account with a central or commercial bank through which payments for current international transactions between the countries may or must be passed. While BPAs may be structured differently, they typically involve certain basic features as described in Box 1 on Typical Features of BPAs. BPAs fall under a broader category of official payments and clearing arrangements and can give rise to exchange measures that are inconsistent with members' obligations under the Fund Articles.

[1] See Executive Board Decision No. 433-(55/42), adopted on June 22, 1955 ("Bilateralism and Convertibility"); Executive Board Decision No. 955-(59/45), adopted on October 23, 1959 ("Discrimination for Balance of Payments Reasons"); and Executive Board Decision No. 1034-(60/27), adopted on June 1, 1960 ("Articles VIII and XIV"). See also "Bilateralism and Convertibility" in SM/54/118 of December 13, 1954; "Bilateralism and Convertibility" in SM/55/31 of May 12, 1955 and "Articles VIII and XIV" in SM/60/34 of May 12, 1960.

[2] Executive Board Decision No. 433-(55/42), adopted on June 22, 1955, provides that "*Fund policies and attitude on bilateral arrangements which involve the use of exchange restrictions and represent limitations on a multilateral system of payments are an integral part of its policy on restrictions. This policy aims at the elimination of foreign exchange restrictions and the earliest possible establishment of a multilateral system of payments in respect of current transactions between members. The Fund's policies and procedures on such restrictions rest on Articles I, VIII and XIV of the Fund Agreement*." See also Executive Board Decision No. 955-(59/45), adopted on October 23, 1959 ("Discrimination for Balance of Payments Reasons"), Executive Board Decision No. 1034-(60/27), adopted on June 1, 1960 ("Articles VIII and XIV"),as well as page 4 of "Review of Bilateral Payments Arrangements, 1976-81" in SM/82/169 of August 17, 1982, on the evolution of the Fund's policy on bilateral payment arrangements.

[3] The terms "bilateral payment arrangement" and "bilateral payment agreement" are often used interchangeably in Fund policies, although the former encompasses any restrictive payments arrangements between the two parties, either formal or informal. Official payments and clearing arrangements that include more than two parties would be subject to similar analysis for purposes of compliance with Article VIII, Section 2(a) and 3.

Box 1. Bilateral Payment Arrangements—Typical Features

While BPAs can take different forms, they often include the following typical features:

- A system of bilateral accounts through which the settlement of the bulk of the current payments between two (or more) countries would be setup. The accounts are either denominated in the currencies of the parties themselves or in the currency of another country. For example, Country A and Country B establish an arrangement under which the central bank of each country opens an account on behalf of the other central bank denominated in US$ up to, e.g., US$ 10,000. Parties to the agreement are usually central banks of the relevant countries, although in some cases, commercial banks or other entities may assume this role.

- The arrangements usually provide for a mutual extension of credit between the parties so that residents of each country will be permitted to channel payments through the bilateral accounts notwithstanding that that country/party is in net debit position. In this manner, either party will be allowed to accumulate a net debit balance on the clearing accounts up to a designated amount. The arrangement will provide that balances on the clearing accounts may accumulate for a designated period; at the end of each such period, balances on the accounts will be "cleared" and "settled." Thus, the parties will calculate the net debit balance owed by one party to the other (i.e., "clearing") and the debtor will then be required to "settle" this amount periodically, normally by payment in "convertible" currency or in another currency acceptable to the creditor. To illustrate:

- On Day 1 of the arrangement, balances in the two accounts are set at zero. If a resident of Country A uses the accounts to pay for goods s/he has imported from Country B at a cost of US$ 1,000, the importer will pay the equivalent of the contract price in his national currency to the central bank of Country A. The central bank of Country A will then credit an equivalent amount in dollars on the account held by the central bank of Country B in the central bank of Country A, and the central bank of Country B will then pay the exporter the equivalent of the contract price in the national currency of Country B. At this point, the central bank of Country A will owe a net debit balance of US$ 1,000 to the central bank of Country B. However, this debit balance may be offset by subsequent payments or imports by Country B. If no further transactions take place, the central bank of Country A, at the end of the first three-month period, will have to settle a net debit balance of US$ 1,000. Thus, the two accounts will be "cleared" (i.e., the net debit balance will be calculated, and the accounts reduced to zero) and the central bank of Country A will pay US$ 1,000 to the central bank of Country B.

- The typical payments arrangement also defines the exchange rates applicable between the countries-parties to BPA and lists the types of current transactions in respect of which settlements are to be made through the arrangement accounts.[1]

- The arrangement will restrict transferability or conversion of balances in bilateral accounts to another country. Under most arrangements, partner banks will accumulate balances of currency which have been recently acquired as a result of current international transactions. Such balances will accumulate as residents of the partner countries make payments for current transactions through the arrangement and amounts are credited to or debited from the accounts of the partner banks. However, under many bilateral arrangements, a partner bank will not be permitted to freely convert and transfer the net credit balance which it holds against another partner bank; rather, this amount will only be available for payments between the parties.

[1] See "Review of Bilateral Payments Arrangements, 1976-81" in SM/82/169 of August 17, 1982, page 2.

3. Certain provisions of BPAs may give rise to exchange restrictions and/or MCPs subject to Article VIII, Sections 2(a) and 3 and may also involve discriminatory currency features. In particular:

- BPAs can give rise to exchange restrictions (i) at the level of residents of the countries which are parties to the BPA, and (ii) at the level of central banks or commercial banks with respect to the settlement of balanced which have accumulated between them.
  - A restriction on payments by residents may arise if a resident is subject to "undue delay" in making a payment for current international transaction due to the BPA.
  - An exchange restriction may also arise where the settlement of a net credit balance between the central or commercial banks only take place upon the expiration of a certain period specified under the arrangement if the period between such settlements is unduly long. The Fund has considered periods up to three months as not undue and thus did not find an exchange restriction in those cases.[4]
  - An exchange restriction would also arise if balances in the bilateral accounts maintained under the arrangement can be used only to make settlements between the parties and cannot be converted into another currency or be used to make payments to a third country.[5]
- If for exchange transactions the BPA provides for the use of "special" exchange rates which differ from those prevailing in the FX markets, an MCP may arise at the level of: (i) transactions of residents making use of the arrangement, or (ii) settlement of credit balances by (central) banks of countries parties to the BPA.[6] The assessment for BPAs, consists of verifying whether the exchange rate established by the agreement (R)[7] is within the permissible margin of the wholesale spot FX market in all countries participating in the BPA. R is the spot exchange rate agreed upon by two (or more) central banks for currency conversion needed, for example, for

[4] See "Review of Bilateral Payments Arrangements, 1976-81" in SM/82/169 of August 17, 1982, page 3 ("*As regards the length of period between settlements under clearing arrangements, the practice has evolved to consider periods up to three months as not undue for this purpose*.").

[5] See "Review of Bilateral Payments Arrangements, 1976-81" in SM/82/169 of August 17, 1982, page 3 ("*One feature of a bilateral payments arrangement that gives rise to a restriction on the making of payments and transfers for current international transactions is that the transferability of balances in bilateral accounts is restricted or prohibited, i.e., that balances in the bilateral accounts maintained under the agreement can be used only to make settlements between the two parties, and cannot be transferred into another currency or he used to make payments to a third country*.").

[6] The Fund has also taken the position that, where a BPA provides that the net credit balance owed by one partner bank to another is not remunerated at the "prevailing representative interest rate in the market", the difference between the rate of remuneration under the arrangement and the "market" rate must be taken into account in determining the effective rate of exchange at which the net credit balance is settled (see "Review of Bilateral Payments Arrangements, 1976-81" in SM/82/169 of August 17, 1982, page 3). See also "Developments in International Exchange and Payments Systems" in SM/92/2 of January 6, 1992, page 77 ("*bilateral payments arrangements may involve multiple currency practices subject to Article VIII, Section 3 if the credit balances in the clearing accounts are not remunerated at the prevailing representative interest rate in the market*"). However, this rule has proven difficult to apply in practice and, as a result, does not appear to have resulted in an MCP finding.

[7] Effective exchange rate where it is appropriate.

the settlement of payments on pre-defined future settlement dates. The assessment would measure R_t against the H_t/L_t of the wholesale spot FX market *in each country* on the settlement dates and the +/- 2 percent tolerance margin around the mid H_t/L_t in each country with *t* being equal to the Bilateral Payment Agreement settlement date. BPA exchange rates are not continuously monitored as the actual settlement dates are used for any assessment, when the MCP may arise at the level of settlement balances between central banks. In other cases, more frequent monitoring may be required.

4. Most Fund arrangements (and , PCIs) include a standard performance criterion under which the country should not conclude BPAs inconsistent with Article VIII; and exchange restrictions and MCPs arising from a BPA are also monitored under standard continuous PCs (see section VI).[8] Whether a change in the main features of a BPA represents an intensification of the related exchange restriction or a modification of a related MCP would have to be assessed on the basis of sufficiently detailed information.

5. BPAs that are inoperative, i.e., no new transactions are channeled through them and no balances outstanding in such arrangements, do not give rise to exchange restrictions or MCPs. Where balances are still outstanding (as between monetary authorities), Fund jurisdiction has continued to be invoked even if such balances are in the process of liquidation, on the grounds that such balances remain currently acquired and settlement is subject to undue delay. Where outstanding balances have been repaid in full or converted to loans from one government to another in the process of liquidation, such balances are considered to be no longer outstanding under the inoperative bilateral payments agreements from which they arose.

6. Bilateral Payment Agreements. Central banks may enter into agreements to settle current transactions (e.g., imports and exports) between the two or more countries on pre-defined dates at specific exchange rates. It has been the practice of the Fund to assess agreements between central banks that are structured as BPAs[9] to determine whether they are consistent with the members' obligations under Article VIII, Section 2(a) and 3 of the Articles of Agreement. For example, an official payment or clearing arrangement would generally give rise to an MCP if for exchange transactions it provides for the use of exchange rates that effectively are not the same as the rates that are used in the market.[10] Staff does not assess agreements between central banks that are not structured like BPAs (for example, swaps for liquidity support or for reserve management purposes). 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

[8] Arrangements (and PCIs) may also include a performance criterion aimed at the elimination of, or reduction in, the scope of, BPAs. See the Board Paper on "Review of Bilateral Payments Arrangements" in SM/82/169 of August 17,1982, page 5, footnote 1.

[9] For discussion of bilateral payment arrangements, see "Review of Bilateral Payments Arrangements, 1976-81" in SM/82/169 of August 17, 1982.

[10] 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 "Official Clearing and Payments Arrangements – Temporary Exemption from the Three-Month Rule" in SM/94/188 of July 14, 1994.

exchange rate deviations in excess of the permissible spread will be assessed under the methodology.

Annex IV. Exchange Rate Guarantee Schemes

Definition and Use of Exchange Rate Guarantee Schemes

1. **Exchange rate guarantee schemes (ERGSs) may take different forms and carry various names.** These are essentially mechanisms designed to cover, in whole or in part, exchange rate risks of certain market participants (e.g., some exporters or some banks), by compensating part or all of the losses incurred by these market participants on exchange transactions due to the fluctuations of exchange rates in the future.[1] Exchange rate guarantees provided by official action can be considered as a subsidy of the rate that applies to exchange transactions covered by the scheme. Only ERGS arising from an official action are covered by the MCP policy.

2. **Contingency facilities that pertain to other exchange market developments, but do not cover losses in exchange transactions, are not treated as ERGSs under the MCP policy.** For example, facilities that (i) secure a beneficiary against the non-payment in foreign currency of financial obligations ("suretyships"), or (ii) insure a beneficiary against other foreign exchange-related risks ("inconvertibility insurance"), are not considered as ERGSs.

3. **ERGSs may cover exchange rate risks arising in different contexts.** In practice, ERGSs have been used to cover exchange rate risks arising, for example, from trade, auctions, external debt operations, and deposits associated with foreign assistance for development projects.

Conditions Under Which ERGSs May Give Rise to MCPs

4. **An ERGS gives rise to an MCP if the scheme (a) is not considered to be "self-financed" and (b) an impermissible spread has arisen.**

(a) The self-financed character:

5. **ERGSs are considered to be self-financed if the premia paid by the beneficiaries of the scheme can be reasonably assumed to be sufficient to cover the exchange rate risks over time.** In such cases, the member or its fiscal agency does not have to provide additional funds (i.e., subsidies) to compensate for such risks. The non-self-financed character of the scheme would be indicative of an inherent subsidy and may result in an exchange rate that deviates unreasonably from a market rate for the operations covered by the scheme. A scheme will not be considered as self-financed if the beneficiaries of the scheme and/or third parties do not provide a financial contribution to the scheme, or if such contribution is not sufficient to cover the exchange risks, and as result, the authorities have to provide a subsidy or earmark funds to the scheme.

[1] See "Review of the Fund's Policy on Multiple Currency Practices— Initial Considerations" in SM/18/208 of August 15, 2018", paragraph 23, Box 1, and Box 5; "Review of the Fund's Policy on Multiple Currency Practices—Initial Considerations—Methodology to Assess Multiple Currency Practices—Background Paper III" in SM/18/208, Supplement 3, of August 15, 2018, paragraph 33, and Appendix I, as well as Table 1 of "Review of the Fund's Policy on Multiple Currency Practices—Proposals for Reform" in SM/22/129 of June 6, 2022.

6. The determination of the self-financed character is made *ex ante*, i.e., when the scheme is established, not when the compensations are paid to the beneficiaries. The determination as to whether or not the premia could be reasonably expected to cover the exchange risks over time is assessed at inception based on a reasonable assumption about the exchange rate path over time. However, the scheme must be reviewed periodically to ensure that it continues to be self-financed.

7. Depending on its features, the self-financed nature of an ERGS could be assessed under the methodology for non-spot transactions either as a forward or option. ERGS that are akin to forwards or options would be treated in a similar manner (i.e., compared to either available relevant market rates/prices or theoretical rates/prices).

(b) Assessing the exchange spread

8. If the scheme is not self-financed, staff will apply the methodology for spot or non-spot transactions depending on the features of the scheme to determine whether it results in an impermissible spread. When an ERGS is not self-financed the compensation for exchange losses is considered to be part of the effective exchange. In order to avoid the MCP, the effective exchange rate of the exchange transaction covered by the ERSG should be within the permissible margins which are calculated depending on whether the ERGS is akin to forwards, options or spot transactions. The assessment requires comparing the forward exchange rate with the market exchange rate for forwards of the same maturity, while the effective exchange rate of the option should be compared with the market option exchange rates with the similar terms. When wholesale market interdealer rates for forwards of the same maturity and options for the same terms are not available, the theoretical price of the forward/option should be calculated. Should the ERGS, depending on its features, be akin to a spot transaction, it should be assessed under the methodology for spot transactions. If the effective exchange rates are outside the respective permissible margins, an MCP would arise.

Removing an MCP Arising from an ERGS

9. MCPs arising from ERGSs may be difficult to remove quickly because, even if new commitments are suspended, old obligations would need to be honored until the relevant contracts expire. However, an MCP arising out of an ERGS will be considered removed if the authorities, render the scheme self-financed or, if the scheme remains under-financed, the authorities take actions to ensure that no impermissible spread emerges in the future. Also, an MCP arising from an ERGS will be considered removed when, without any action being taken by the member, no new impermissible spread has arisen over a period of 12 months after the emergence of the impermissible spread that gave rise to the MCP.

10. A member may request approval of MCPs arising from ERGSs. In practice, the Fund has generally approved MCPs arising from ERGSs, provided that no new commitments were made under the scheme.

Annex V. Retrieval of Market Exchange Rates for the Assessment of Multiple Currency Practices[1]

Timing for Data Retrieval

1. To apply the methodology for the MCP assessment, staff must ensure that the wholesale foreign exchange market in the respective country is closed before extracting the highest and lowest exchange rates. This will prevent the retrieval of market data while FX transactions, which could alter the highest and lowest rates, are still taking place. Further, the time zone on LSEG Eikon and Bloomberg should be set to match the trading day of the country for which market exchange rates are collected. This will ensure that the exchange rate affected by official action is compared to market exchange rates of the same trading day using inter-day high and low.

2. Setting the time zone of the local onshore market prevents next-day data influencing the daily high and low for market exchange rates. The daily highest and lowest market exchange rates of a given country could well be different in Eastern Standard Time (GMT -4) from the daily highest and lowest exchange rate of the country in its local time (e.g., GMT+8). Because of the 12-hour difference between the two time-zones in this example, any exchange rates retrieved post-12pm EST could alter the daily highest and lowest rates, since this is the close time of the market in local time. Any transactions occurring after 12PM EST should therefore be considered for the daily exchange rates of the following day.

3. The assessment can be conducted only for those days when the relevant FX market is open. If the foreign exchange market is closed on a given day, the comparison of the exchange rates is impossible, and thus the assessment cannot be completed and no MCP can be found.

Currency Pairs

4. If an official action results in market segmentation for multiple currency pairs, the MCP assessment is performed on the dominant currency pair first. If an MCP is found for the dominant currency, staff do not need to identify MCPs in other currency pairs to avoid multiple MCP findings arising from the same official action. In case there is no MCP finding for the dominant currency pair, staff must assess if there is an MCP in the other currency pairs resulting from the official action.

5. The information on the dominant currency pair should be determined by staff and would be based on the trading volumes in each currency pair. The dominant currency pair would be the one in which the highest volume is traded in the wholesale market and usually the one in which the authorities intervene. If the country implements an official action resulting in market segmentation for multiple currency pairs, with the dominant currency pairs being USD/local currency, while the market also trades in EUR/local currency, and CAD/local currency, staff will first

[1] The procedure described in this Annex assumes that representative wholesale FX market data is available from the primary or secondary data sources (LSEG Eikon/Bloomberg).

ascertain whether there is an MCP in the dominant currency pair (USD/local currency). If yes, then there is no need to assess the other two currency pairs. If there is no MCP finding in the dominant currency pair, staff would need to look at the second most dominant currency pair, etc.

Dual or Multiple FX Markets in a Single Jurisdiction

6. In cases of dual or multiple FX markets in a jurisdiction, the trading day is defined by the overlapping trading hours of the primary and secondary markets. Two legal FX wholesale markets in a jurisdiction may have different time zones or trading hours. In such case, the overlapping trading hours of the primary and secondary markets set the time for the collection of market data (from the primary market) and the effective exchange rate arising from official action (from the secondary market) which is the mid of the H/L of the secondary market +/- any mandatory costs and/or subsidies that should be considered as part of the effective exchange rate. If one of the two markets or both are closed on a given day, the comparison of the market and official exchange rate is not possible, and the assessment is not done on those days.

7. When collecting market data for the overlapping period in two FX wholesale markets the time zone must be properly calibrated on the interface provided by the benchmark data providers. The highest and lowest exchange rates for a limited time period corresponding to the overlapping period are available from both data providers.

Availability of FX Wholesale Market Exchange Rates

8. If wholesale FX market data are unavailable from both LSEG Eikon and Bloomberg or existing data appears to be manifestly irregular or inaccurate staff should use other data sources. As wholesale market exchange rate data is crucial for assessment, in case the data is not available through the primary or secondary sources or the data from them is manifestly irregular or inaccurate staff should rely on other reliable sources to obtain exchange rate data that are representative of the wholesale FX market. Alternative data sources staff could use include: (i) publicly available independent data sources (e.g., other third-party data providers for that market, the BIS (Bank for International Settlements) etc.); (ii) publicly available data from the authorities (e.g., exchange rate or interest rate data published on the CB's website; or (iii) data obtained directly from the authorities. For example, Emerging Market and Developing Economies with FX controls typically have transaction reporting requirements in place. In the event where there is no active interbank market, the data collected based on this requirement can be leveraged to establish a daily H/L. Staff are expected to determine whether the alternative data is representative of the FX market in each case by assessing whether they have been computed in compliance with the IOSCO principles for the computation of financial benchmarks (see Annex II Box 1).

9. Rates sourced from LSEG Eikon or Bloomberg are considered representative unless staff or the authorities have reasonable evidence to the contrary. The exchange rate data provided by benchmark providers, are validated through pre-established robustness checks on data-sourcing and validation process and are therefore considered as representative unless there is evidence that they are manifestly irregular or inaccurate and thus not representative of the FX

market. To conclude that exchange rate data from the primary and/or secondary data sources cannot be used for MCP assessment there should be reasonable evidence that rates published by LSEG Eikon and Bloomberg are manifestly irregular or inaccurate (not representative). This may be the case for example, when the segment of the market from which the data are sourced reflects only a small volume or number of transactions, irrelevant of the broader market. Other reasons could include the existence of constraints on FX trading represented by the exchange rate data (spread limitations imposed by the authorities and constraints on exchange rate movements), or if market trades are concentrated only between few banks.

10. When exchange rate data from the primary and secondary data providers cannot be used, representative exchange rates can be used from third parties that follow a robust process of data selection and auditing with respect to data sourcing, type of data and methodology for data collection and validation. Staff would confirm that the data selection and auditing process is consistent with IOSCO principles (see Annex II Box 1).

11. Representative wholesale FX market rates computed by the authorities can be used if representative exchange rates from a third party are unavailable. Underlying data (price and quantity) for the computation of the rate should be provided to staff to ascertain that the data collection, data selection and computation follow IOSCO principles.

12. In the absence of wholesale market rates that are representative of the FX market, exchange rate data on other segments of the FX market may be used.[2] Although the MCP assessment should be primarily based on wholesale FX market exchange rates, in case the available wholesale exchange rate data is not representative of the FX market in the country, staff should seek to obtain representative exchange rate data from other segments of the FX market including the intermediary-client market (e.g., bank-client or exchange bureau-client market). Such rates and transaction amounts should be representative of the broader FX market, e.g., negotiated (large) ADs-client transactions (if there are no interbank quotes or they are not used in actual transactions) or the weighted average rate of the bank-client transactions. When such data is used it should include all bank-client (or FX bureau-client) transactions except that data on transactions below a minimum transaction amount may be disregarded thus excluding the smallest transactions in the bank-client transaction distribution. In case there is more than one representative exchange rate data, the one which is more representative should be used.

13. Non-spot exchange rate data may not always be available. Two likely scenarios may arise for the assessment of official action involving non-spot transactions: one where a non-spot interdealer market exchange rate exists, and the other where such a market does not exist. In the first case, the same methodology to extract data and assess them as for spot transactions should be used. That is, the non-spot exchange rate arising from official action is compared with the permissible margin, where H and L of market exchange rates for transactions with similar terms is obtained on the relevant non-spot domestic interdealer FX market. If the non-spot official exchange

[2] Staff should ascertain that data collection, data selection, and computation follow IOSCO principles.

rate is in the permissible margin, there is no MCP but in the event of a breach, an MCP is found (see Annex II Box 2).

14. When market prices for non-spot FX transactions are not available from the benchmark providers or alternative data sources, the theoretical non-spot price needs to be calculated. The theoretical non-spot price should be calculated utilizing spot wholesale market exchange rate and interest rate data provided by LSEG Eikon and Bloomberg. Theoretical forward and NDF prices can be calculated in the forthcoming monitoring tool. Additionally, theoretical price calculators provided by LSEG Eikon and Bloomberg may be used to compute theoretical exchange rates for options.[3] The calculators include pricing models depending on the type of derivatives transaction being evaluated and is based on a standardized methodology. The valuation tools enable the amendment of some of the parameters in the calculator with other data that may be more appropriate to use (e.g., a more relevant interest rate). As in the case of spot exchange rates, staff should verify the representativeness of the data used in the calculation. Staff may use alternative data sourced from local markets to change the parameters of the calculation if such data appears to be more representative of the market conditions in the country. For forwards (and the forward leg of swaps), data sourced from local markets on the actual funding rate in that market for a given maturity can be used. In the case of options, volatility and the local currency interest rate are relevant to obtaining option prices. In the absence of implied volatility, historical volatility based on prices formed in the domestic market that reflect exchange rate volatility and local interest rates based on actual cost of funding for the relevant maturities should be used.[4] When such data is not publicly available staff may be able to source it from the authorities depending on the type of option.

15. If representative data for spot exchange rates cannot be obtained, the MCP assessment for spot transactions cannot be conducted and thus no MCP finding can be established. For non-spot transactions the assessment can be concluded even in the absence of representative market data if the theoretical price of the non-spot transaction can be calculated.

[3] LSEG Eikon provides a FX Options Calculator as FXOC, while Bloomberg provides a similar calculator as OVML.

[4] Historical volatility may not be appropriate if significant changes affecting exchange rate volatility occurred in the country.