

A FRAMEWORK FOR A REVIEW OF THE INTERNATIONAL FINANCIAL INSTITUTIONS¹

BACKGROUND PAPER

The international community has long discussed the need for reform of the International Financial Institutions (IFIs). The challenge for the international community is to move these discussions forward to agree on principles for reform and a realistic plan for its achievement.

The IMF Managing Director's Medium-Term Strategy is a welcome first step. However, we must be more ambitious and comprehensive in reviewing the IFIs than what may be possible in an internal review. Fundamental issues such as quotas, governance, and the interaction between the IMF and the World Bank, need to be addressed. The G-20 can play an important role in setting a framework for review and building the political momentum for reform.

The purpose of this paper is to set out a concrete plan for addressing strategic reform issues in a feasible manner, with a focus on the appropriate forum and process for taking forward particular issues.

The paper begins with a taxonomy of reform issues. It then provides an outline of why reforms are necessary so as to facilitate a shared understanding of problems to be addressed. It considers how a strategic review could be structured and which forums might be most appropriate for reviewing aspects of IFI governance. Finally, the paper outlines a 'roadmap' for G-20 action.

I) INTRODUCTION

Over the past ten years there have been a number of reviews of the IFIs which have resulted in important changes to the way in which the organisations work. However, while these reforms have improved the functioning of both institutions, there remain many aspects of IFI reform which are unresolved. Several international forums are presently discussing IFI reform issues, including the IMFC, DC, G7 and G-20, and the IMF also has its own internal review underway. However, progress has been slow, reflecting the many complex and interrelated issues involved and the variety of stakeholder interests.

From its inception, the G-20 has had a mandate to review the Bretton Woods Institutions, and has consistently sought to promote dialogue on the framework of the Bretton Woods Institutional system. As such, the G-20 has a legitimate and key role in advancing IFI reform. The G-20 could do this by taking a holistic view on the strategic reform of the IFIs. While other forums are discussing specific policy issues, the G-20 should take a step back and look at broader strategic and governance reform issues. The G-20 could articulate a framework, or a 'roadmap', for reform and also monitor progress on the reviews that are already underway.

¹ For the purposes of this paper, IFIs are defined as the IMF and the World Bank, however, many of the issues arising in the paper are also relevant to other institutions.

The G-20 would not undertake reviews itself, rather it could encourage the appropriate forums (eg the IMFC/DC, IFI Executive Boards, IFI management, IFI independent evaluation offices, etc.) to undertake the reviews. In exceptional cases, such as quotas, the G-20 might go further to help build momentum for reform.

II) IFI REFORM: A TAXONOMY OF THE ISSUES

IFI reform can be divided into two interrelated but separable streams. These in turn can be organised into simpler parts.

a) Improving the **governance and management** of the institutions — **how** decisions about the IFIs are made and implemented. This includes:

- longer-term governance issues such as quotas, representation and voice; and
- short to medium-term governance issues such as the role, structure and effectiveness of the Executive Boards, internal decision-making processes and management structure and systems (eg systems for operational planning and prioritisation, managing staff, risk and resources).

b) Setting the **strategic direction** of the IFIs — **what** the IFIs do. This includes the:

- roles, future directions, mission and/or mandates of each IFI and the relationship between the IMF and World Bank; and
- broad future directions for key policy activities (eg Fund surveillance, crisis prevention instruments, etc.).

Clearly, it will be necessary to develop a consensus on the objectives of reform — that is, it makes no sense to improve governance if there is no agreement on what is to be governed, and vice versa.

As such, there is a strong case for pursuing a) and b) simultaneously, although not necessarily at the same pace. In fact, while consensus exists about a need to reform both, there may be limited progress in engaging countries against one unless there is a process in place to tackle the other. The G-20 can play a key role in building political momentum for these reforms across both streams.

The Managing Director's Medium-Term Strategy will also be an important contribution. However, it must be recognised that the Fund will necessarily be constrained in the scope and ambition of its own review, in part because it is difficult for the Fund to challenge and change the broader framework in which it is expected to operate. It falls instead to the membership to reform the frameworks that govern and guide the IFIs.

III) THE CASE FOR REFORM

In recent years there have been advances in governance and management at the IFIs. However, these improvements have been partial — and often reactive — rather than as part of a comprehensive plan. A fundamental review could allow for a clear holistic vision for the institutions. It would facilitate progress being made across those aspects of governance and management where there remain issues that impede the effectiveness of the IFIs.

A key challenge to achieving further progress is that different countries have radically different conceptions of what needs to be covered by a strategic review. Some questions posed for the review involve high level, conceptual or strategic issues about the future direction of the organisations, while others are concrete questions about ‘here and now’ issues.

At a **governance and management** level some issues are:

- representation of members, including quotas, voice and representation;
- clarity of the roles and responsibilities of the Boards of Governors, the IMFC/DC, the Executive Boards, and senior management;
- IMFC/DC effectiveness;
- Executive Board effectiveness and size and structure of the Boards; and
- Management and staff effectiveness.

At a **strategic level** issues include:

- the roles and future directions of the IFIs and the relationship between the IMF and the World Bank; and
- policy issues, such as surveillance, improving the effectiveness and traction of policy advice, forms of assistance (financial and non-financial) to members, and the adequacy of existing crisis prevention and resolution instruments.

IV) ROADMAP FOR REFORM

For the G-20 to have an impact it first needs to consider “higher, further, faster” issues. That is:

- Higher — how ambitious should be the strategic review? Should it include fundamental issues such as quota reform and the role and mission of the IFIs?
- Further — how far forward should we look? A 2-3 year timeframe, as has been proposed by the IMF for its own internal review, or a longer timeframe?
- Faster — how fast do we want to move? Is this to be one all encompassing review, or are we looking for a roadmap that takes us – sequentially or simultaneously – through issues?

Being ambitious, looking beyond an operational planning horizon (ie beyond three years), and adopting a roadmap for progress seems preferable to one large review. **In considering these issues we also need to be mindful of where the competency for conducting the reviews will lie.** The appropriate forum to oversee reform will vary depending on the particular issue.

The G-20 is not necessarily the appropriate forum for deliberation on many of the issues set out in Section III. But, it can add value by providing momentum to other forums to conduct reviews while also undertaking its own reviews in a few key issues where external prosecution is needed to break an existing impasse.

For example, one issue not being adequately addressed elsewhere could be the principles that might underlie quota reform. While ultimately this is an issue for the Board of Governors of the IMF, the G-20 is a useful forum for discussion as it is external to the IFIs and has a range of representation from developed and emerging economies. If the G-20 were able to achieve progress on issues such as this, it would facilitate their consideration in other forums.

Similarly, the G-20 could encourage the IMFC and DC and Executive Boards to undertake reviews of other aspects of IFI governance as appropriate.

There are four proposed elements to the roadmap which are outlined below.

1. Quotas and representation of members

- Successful resolution of this is beyond the scope of Management and the Executive Boards. While formally it is a matter for the IMF/World Bank Governors, consideration in an external forum, such as the G-20, may be useful in building the momentum for reform and in reaching a consensus on a way forward.
- While last year has seen a growing consensus around the need to reform quotas, at the 2005 Annual Meetings, the IMFC simply sought progress on this issue, with a report back at the 2006 Spring meetings. Yet failure to address this issue in a timely way may damage the legitimacy of the IFIs.
- As such, there is value in the G-20 considering principles (not formulae) for quota reform which reflect changing economic weights. The G-20 Ministers and Governors could agree to the principles at their meeting in November 2006.

The G-20 could develop principles for quota reform which reflect changing economic weights. The principles would be an important input into the review of quotas.

2. Governance accountabilities and operational effectiveness

- This encompasses the roles and responsibilities of the Executive Boards, IMFC/DC and Management; the operational effectiveness of the IMFC/DC and the Executive Boards and the IFIs' management structure and systems.
- This is within the scope of the IMFC/DC and the Executive Boards (although it may require some external assistance).
- IMFC/DC Deputies could consider possible terms of reference for this review at their meeting in March/April 2006.
 - : Agreement on appropriate terms of reference will be very important — a review that is too wide, or is undertaken by an inappropriate reviewing body could result in poor or ineffective recommendations.
- The IMFC/DC could consider the possible review at its meeting in April 2006.

The IMFC/DC could consider the scale of a review of governance and operational effectiveness. For example, the review could consider the size of the Boards and constituency arrangements.

There would be several elements to the review:

- the roles and responsibilities of the Executive Boards, IMFC/DC and Management;
- the operational effectiveness of the IMFC/DC;
- the operational effectiveness of the Executive Boards; and
- the responsibilities and accountabilities of management positions.

The review could be undertaken by a subcommittee of the IMFC/DC or by Deputies. The review could also seek the advice of independent experts, such as the independent evaluation offices of the IMF and the World Bank. For example, the responsibilities and accountabilities of management positions could be reviewed by a panel of experts in organisational governance and management.

3. Roles and responsibilities of the IFIs

- At its broadest, a review could examine the entire international financial architecture and the appropriateness of the current institutional arrangements, including the IFIs, as well as a full review of their Articles of Agreement. However, this could be unduly time and resource intensive given that there is no groundswell of support for radical change. Rather, we suggest taking the broad purposes of the IMF and the World Bank as given, and focusing on the delineation of responsibilities and cooperation between the IMF and the World Bank. This would allow effort to be concentrated on how the institutions can best work to promote economic growth, international financial stability and poverty reduction.
- Accordingly, a review could assist by considering how the IFIs work together to achieve their stated purposes. The aim would be for a clearer role for both institutions, especially in low income countries.
- While Management, the Executive Boards and the Boards of Governors have roles, external involvement may be beneficial and may assist in consideration of how the roles of the two institutions relate to each other.
- As with the governance review, IMFC/DC Deputies could consider the details of this review at their meeting in March/April 2006.
- The IMFC/DC could consider commissioning this review at its meeting in April 2006.

The IMFC/DC could commission experts, including the independent evaluation offices of the IMF and the World Bank, to review the delineation of responsibilities between the IMF and World Bank to reduce overlap.

4. Future directions for key policy activities (eg Fund surveillance)

- Specific policies have been the focus of much of the discussion on IFI reform to date. However there is less discussion of whether the current mix of activities is right (for example, is the level of resources allocated to lending programs versus technical assistance appropriate?).
- Reviewing key policy activities is within the scope of Management and the Executive Boards (although at times external involvement may be beneficial).

The Executive Boards and the IMFC/DC are the most appropriate forums for consideration of the broad strategic directions of key policy activities (eg Fund surveillance). Improving the operations of the Executive Boards should assist with consideration of these key policy issues.

At times there may also be merit in the IMFC/DC and/or the G-20 discussing particular policy issues.