

# INTERNATIONAL MONETARY FUND

## Executive Board Report to the IMFC on Reform of Fund Governance

October 3, 2009

1. **Background.** This paper responds to the request in the last IMFC communiqué for the Executive Board to report on governance reform. Preliminary Board discussions have yielded agreement in some areas, but the topic is complex, and it should be stressed that more work is needed to refine proposals and garner broad consensus (see <http://www.imf.org/external/np/sec/pn/2009/pn0998.htm>). In drafting this report, a range of external inputs have also been considered, including from the Trevor Manuel Group, the Independent Evaluation Office, academics/think tanks, and civil society.
2. **Motivation.** The current crisis has shown that the Fund's decision-making structures can deliver the kind of innovative and rapid responses the membership needs and expects. Even so, there is an undercurrent of doubt about the future, reflecting the perception that much of the recent responsiveness has been driven by outside forces (e.g., the G-20) and that, once the crisis fades, old dissatisfactions with vote, voice and process will resurface to undermine the political backing that has been key to the Fund's renewal. Hence, the IMFC's interest in reforms to underpin the institution's legitimacy and effectiveness is important and timely. This report focuses on five areas: fair quota share; high-level engagement; effective decision-making and representation at the Executive Board; open selection of management (and, more broadly, staff diversity); and updating of the Fund's mandate.

### I. FAIR QUOTA SHARE

3. **A defining issue.** The task of realigning quota shares with current global realities remains politically vexing and incomplete. With even the April 2008 quota and voice reform yet to be ratified by many members, it is clear that the goal of concluding the next quota review by January 2011 is highly ambitious. Fortunately, there is new momentum for a shift in quota share to dynamic emerging market and developing countries of at least 5 percent from over-represented to under-represented countries using the current IMF quota formula as the basis to work from. Setting a target for the overall quota increase, which—aside from raising the Fund's permanent resources—also facilitates rebalancing shares, can move the process forward.
4. **Quotas, other reforms, and sequencing.** The effectiveness of many reforms hinges on a satisfactory realignment of quota shares. For instance, reforms relating to representation at the IMFC, Board composition, voting power, and voting majorities (and blocking minorities) depend on the quota outcome. As such, these may need to be decided on as a package. That said, the reform process need not be hostage to the quota issue, central as it is. It should be possible to move in other areas, enhancing engagement in the IMFC (some measures—e.g., better meeting formats and communiqué processes—could be piloted at the

Istanbul meetings), strengthening the work of the Board, putting in place a truly open management selection process, and looking into an update of the Fund's mandate.

## II. HIGH-LEVEL ENGAGEMENT

5. ***Participation.*** Engagement by ministers and governors is essential to the effective discharge of the institution's responsibilities. But, despite efforts, the formalistic style and bureaucratic tenor of IMFC meetings has been an impediment to serious discussion of issues of interest to senior officials, thus displacing the debate to smaller, outside groupings. The crisis has marked a change, and the vesting of important new tasks for the Fund (e.g., early warnings, elaboration of exit strategies) and added resources make continued engagement all the more important. This effort may at times require the explicit backing of world leaders.

6. ***IMFC reform versus Council.*** The specific modalities of enhanced ministerial engagement involve difficult tradeoffs. Transforming the IMFC into a Council with formal decision-making powers, as envisaged in the Articles of Agreement and espoused by the Manuel Report, would certainly focus ministerial attention and institutionalize engagement. But many consider that it would also weaken the consensus-based guidance underlying IMFC communiqués and transfer some decisions from a resident Board, where members have built the capacity to influence decisions, to a more distant entity, with negative implications for oversight of management and staff. As such, what to advise ministers on this issue has been controversial at the Board, with a few counseling activation, a number of others open to further deliberation (especially once quota reform progresses), and a somewhat larger group considering the proposal to be counter-productive.

7. ***IMFC reform.*** Ministerial engagement in the IMFC process can be enhanced through a number of initiatives, each small in its own right, but adding up to a transformation. Box 1 outlines proposals that would move from formalistic meeting formats to more fluid and interactive ones, adopt a more inclusive leadership model, improve the communiqué drafting process, and incorporate mechanisms for greater Board accountability.

## III. EXECUTIVE BOARD EFFECTIVENESS AND REPRESENTATION

8. ***Strong Board.*** Since the Fund's inception, the Executive Board has always played a central role in the institution's decision-making process. A strong Executive Board is vital to the effective functioning of the institution, bringing the views and interests of members and lending political voice and support to the technical work of management and staff. The distribution of responsibilities is broadly satisfactory, but the Board's effectiveness could be enhanced by modernizing work practices, including through better use of Board committees and lapse of time procedures, and a stronger role in setting the institution's strategic agenda. The peer review exercised by the Board is essential to Fund surveillance, but there is scope to streamline processes for considering Article IV reports.

### **Box 1. Proposals for Enhanced Engagement at the IMFC**

**Strategic priorities.** The IMFC can give greater specificity to the Fund’s work objectives.

**IMFC interaction.** Despite some progress in recent years, there is scope to increase the quality of engagement among ministers and governors. The focus should be on a few systemic or controversial issues, with lead speakers, a Q&A session, and time-limited interventions; comprehensive set speeches should be eliminated. The following may help:

- **Plenary size.** This has become an impediment to interaction, with over 40 people at the table and 350 participants in the room:
  - Instead of harsh limits on representation per chair, it is better to combine a shorter plenary with more restricted sessions (invited participants).
  - The number of Fund staff in the room and non-IMFC members at the table (ILO, OECD, UNCTAD, etc.) should be cut drastically.
- **Informality.** The informal setting of the restricted breakfast meetings has worked well, and the time allocated to it could be extended.
- **Leadership.** Consideration could be given to a troika model—of past, current, and future heads—to foster ownership, broaden participation, and avoid dominance.
  - To encourage rotation, terms might be of 1-2 years, and Spring meeting venues could include troika capitals.
  - Precise modalities of rotation, regional balance, venues etc. are best worked out by the IMFC or their deputies.

**Deputies’ meetings.** The usefulness of these meetings has declined. The deputies should be asked to propose an overhaul (e.g., serving more as agenda setters than as testers of IMFC dry-runs), and to consider holding these meetings only in compelling circumstances.

**Communiqué drafting.** A better process can reduce the bureaucracy around IMFC meetings, allowing ministers to move beyond issues of nuance to debating urgent and strategic policies.

- The communiqué should be concise, forward looking, strategic, and prepared ahead of the meeting (with early drafts circulated for electronic comment prior to the formal drafting session); only unresolved issues need be brought to the IMFC.
- The addition of new items to the communiqué at the last minute should be avoided.

**Board accountability, not accounting.** The IMFC could ask the Board to report on the use of its delegated authority to achieve priorities. Rather than comprehensive accounting, the Board could report on progress and problems in one or two specific areas at each meeting.

9. **Size and composition.** Most Directors view a reduction in the size of the Board from 24 to 20 chairs as unlikely to lead to efficiency gains in excess of representational costs, although some stressed the importance of increasing the relative presence on the Board of emerging market and developing country members. The Manuel Report also suggests to move to a system of all elected Executive Directors, removing the provision in the Articles for the largest five quota holders to appoint Executive Directors. Such a step has advantages (e.g., facilitating consolidation of chairs) but requires more careful consideration than has been possible so far.

10. **Consensus, majorities, thresholds.** Consensus-based decision making has long been the norm at the Fund. Although consensus is formed “in the shadow” of voting rules, which is partly why quota reform is so important, a robust process of give and take has evolved to develop proposals that command broad—not merely requisite—majorities. Thus, the two proposals put forward in the Manuel Report, for all their merit, must be considered carefully:

- Lowering the 85 percent threshold for special majorities to 70–75 percent eliminates the US veto and appears to level the playing field. But it also reduces the voice of all minority groupings by making it more difficult to form blocking minorities.
- Extending double-majority voting to key decisions can broaden support on critical issues, but gridlock in decision making is a risk.

Both of these changes involve amendments to the Fund’s Articles—and, hence, require a level of support that so far has not been forthcoming.

#### IV. MANAGEMENT SELECTION AND STAFF DIVERSITY

11. **Management selection.** The selection of the Managing Director, and of the Deputy Managing Directors, should be open, transparent and, most importantly, without regard to nationality. A 2001 draft report on the selection process of the World Bank’s President and Fund’s Managing Director recommended principles and procedures for search, which were merely “endorsed” by the Executive Board and “noted” by the IMFC in April 2001. A firm political commitment to it would help, including a clear IMFC statement against informal understandings on nationalities among major shareholders.

12. **Staff diversity.** Staff diversity in all its dimensions—nationality, gender, education, and experience—should be enhanced, in line with the Articles’ injunction to pay due regard to geographic diversity subject to securing the highest standards of technical competence. Progress is being made to increase regional and academic diversity and work experience through the Fund’s hiring policies, and these efforts will need to be redoubled.

#### V. MANDATE

13. **Post-crisis role.** The issues exposed by the current crisis suggests the need for a careful review of the Fund’s mission statement. The emphasis of the Fund’s formal surveillance mandate to promote a stable system of exchange rates is too narrow a reflection of what the Fund actually does and the new directions in which it is moving. A discussion is needed on arrangements to require and enable the Fund to go deeply into all issues that bear on global stability and to do so in a more multilateral way. The reality is that surveillance is limited in various ways and there are important data gaps facing both country authorities and Fund staff. A reconsideration of the Fund’s work need not necessarily entail a formal change in the Articles of Agreement at this stage; a declaration from the IMFC, and associated policy modifications by the Board, may well suffice.