

Reform of IMF Quotas and Voice: Responding to Changes in the Global Economy

By IMF Staff

The IMF is working on wide-ranging reforms to make sure it meets the needs of its member countries. One of the most important elements is governance reform, which involves adjusting quota shares to better reflect the relative weight of member countries in the world economy and enhancing the voice and participation of low-income members within the institution. This reform is critical for the continued effectiveness of the Fund.

As the world economy evolves, so does the distribution of economic weight across countries. The distribution of IMF quotas is intended to reflect the relative weight and role of its members in the global economy. But relative quota shares among members have changed only gradually and have not kept up with changing economic realities. Thus, there is a need to rebalance quotas to reflect the many changes that have occurred, especially the increased weight of major emerging countries in the world economy.

At the same time, there is a need to enhance the voice of low-income countries (LICs) in the IMF. While the weight of these countries in the global economy is small, the Fund plays an important advisory and financing role for these countries. The voting power of LICs has eroded over time, in part because other countries' relative economic weight has increased, and in part because the effect on total voting power of "basic votes"—an equal allocation of votes based on the principle of equality of states that was made when the IMF was founded—has declined in recent decades with successive rounds of quota increases.

The Fund is meeting the challenge of governance reform, recognizing that the complexity of the process requires a careful and deliberate approach.

A Big Step Forward

At the time of the IMF Annual Meetings in Singapore in September 2006, the membership endorsed a program to modernize and reform quotas and voice. Members agreed to a package of reforms to be completed over a two-year timeframe. It comprises the following elements:

- An initial ad hoc increase in quotas for the most underrepresented members: China, Korea, Mexico, and Turkey;
- A new quota formula to guide the assessment of the adequacy of members' quotas in the IMF;
- A second round of ad hoc quota increases based on the new formula;
- An increase in the basic votes that each member possesses to ensure adequate voice for LICs, as well as protection of the share of the basic votes in total voting power going forward; and
- Allocating additional resources for the two Executive Directors representing African members, as they stand for a fairly large number of countries.

The membership recognizes that governance reforms are essential to the continued effectiveness and credibility of the institution. A key part of the Fund's approach is to recognize that governance reforms need to be respectful of the interests of the entire membership and, therefore, require broad consultation in order to reach consensus.

A First Round of Increases

The first element in the package of reforms was ad hoc quota increases for four dynamic economies that were most clearly underrepresented—China, Korea, Mexico, and Turkey. The aggregate increase in quotas agreed for these members is SDR 3.81 billion (about US\$5.66

billion), or 1.8 percent of the pre-increase quotas, bringing the total current quotas to SDR 216.75 billion (about US\$321.92 billion).

Current Distribution of IMF Quota Shares (percent of total)		
Country/Region	Actual Quota Share¹	Nominal Quotas¹
United States	17.1	37,149
European Union	32.4	70,404
Asia	11.5	25,010
China	3.7	8,090
India	1.9	4,158
Korea	1.3	2,927
Middle East and Turkey	7.6	16,426
Turkey	0.5	1,191
Latin America	7.6	16,501
Mexico	1.5	3,153
Brazil	1.4	3,036
Africa	5.3	11,498
Canada	2.9	6,369
Russian Federation	2.7	5,945
Switzerland	1.6	3,459
Australia	1.5	3,236
All other countries	9.8	21,317

¹Consented quotas as of May 21, 2007.

Amending the Quota Formulas

The Board of Governors' Resolution in September 2006 asked the Executive Board to reach agreement on a new quota formula that better reflects the weight and role of members in the global economy. Under such a formula, higher quota shares would be expected for dynamic economies, especially emerging-market countries, whose weight and role in the global economy has been increasing.

The IMF's Articles of Agreement do not indicate how quotas should be determined. The Executive Board has neither formally adopted nor endorsed any particular method for determining quotas or quota increases. However, the Fund has developed formulas that help determine the initial quotas of new members and serve as a guide in determining increases in quotas for existing members, usually in the context of general quota reviews.

Quota formulas have evolved over time, and, currently, there are five quota formulas. The oldest, the Bretton Woods formula, originally contained five variables: national income, official reserves, imports, export variability, and the ratio of exports to national income. A multi-formula approach was introduced in the 1960s, when the Bretton Woods formula was supplemented with four other formulas, with national income replaced by gross domestic product and trade variables expanded to include services and transfers. Current account transactions and variability were given larger weights. The quota formulas were last modified in 1982–83 by reducing the weight of the variability variable and reintroducing reserves as a variable, while retaining the basic structure of the formulas.

The Multifaceted Role of Quotas

Currently, a member's quota plays a key role in defining four aspects of that member's relationship with the IMF:

- (1) The amount of financial resources that a member contributes to the IMF;
- (2) The member's voting power in institutional decision making (along with basic votes);
- (3) The level of access of the member to IMF financing; and
- (4) The members' share of general Special Drawing Rights (SDR) allocations.

The September 2006 Governors' Resolution specified that consideration should be given to a significantly higher weight for GDP in the new formula and that other variables, in particular openness of members' economies, should also play an important role. Defining a new quota formula to replace the existing formulas remains challenging, with important political, conceptual and technical complexities.

The issue of which variables to use and the weight they would carry is central in the negotiations among the member countries—with consideration given to include GDP, openness, variability, and reserves. There are also questions about how each variable should be defined to reflect the evolution in the global economy, and how the formula itself should be constructed. In addition, the new formula should be simple and transparent, consistent with the roles of quotas, and appropriately capture the relative positions of members in the global economy. It also needs to be broadly acceptable to the membership as a whole, while safeguarding and enhancing the Fund's effectiveness.

The objective is to complete work on a new quota no later than the 2008 Annual Meetings.

Quota Reviews

Members' quotas are reviewed periodically at intervals of not more than five years. A general review of quotas allows the Fund to assess the adequacy of quotas in terms of its own ability to help meet the financing needs of members. A general review also allows for increases in members' quotas to reflect changes in their relative positions in the world economy. Ad hoc quota increases outside general reviews have been rare in recent decades.

Of the thirteen general reviews that have been conducted thus far, six have concluded that no increase in quotas was needed. The last quota increase under a general review—the Eleventh—took effect in January 1999. The 45 percent overall increase reflected changes in the size of the world economy, the increased risk of financial crisis, and the rapid liberalization of trade and capital flows.

The Thirteenth General Review, completed in January 2008, assessed that the aggregate size of total quotas was sufficient to meet the Fund's liquidity requirements, and therefore was no need for an increase. This review was unrelated to the ongoing quota and voice reforms agreed upon by the membership in September 2006.

The Second Round of Ad Hoc Quota Increases

Ad hoc quota increases address the relative position of individual members. While not reducing actual quotas, they do reduce other members' actual quota shares. In the past, ad hoc increases have been limited in both number and scale, and have tended to take place in the context of a general quota increase, that is, in a situation in which all members benefit from an increase in their actual quotas. Ad hoc adjustments are, however, possible outside of a general quota review if a high degree of consensus is obtained, as was the case of that achieved in September 2006 in Singapore.

The Existing Five Quota Formulas

Bretton Woods: $Q1 = (0.01Y + 0.025R + 0.05P + 0.2276VC) (1 + C/Y)$;

Scheme III: $Q2 = (0.0065Y + 0.0205125R + 0.078P + 0.4052VC) (1 + C/Y)$;

Scheme IV: $Q3 = (0.0045Y + 0.03896768R + 0.07P + 0.76976VC) (1 + C/Y)$;

Scheme M4: $Q4 = 0.005Y + 0.042280464R + 0.044 (P + C) + 0.8352VC$;

Scheme M7: $Q5 = 0.0045Y + 0.05281008R + 0.039 (P + C) + 1.0432VC$; where:

Q1, Q2, Q3, Q4, and Q5 = Calculated quotas for each formula;

Y = GDP at current market prices for a recent year;

R = twelve-month average of gold, foreign exchange reserves, SDR holdings and reserve positions in the IMF, for a recent year;

P = annual average of current payments (goods, services, income, and private transfers) for a recent five-year period;

C = annual average of current receipts (goods, services, income, and private transfers) for a recent five-year period; and

VC = variability of current receipts, defined as one standard deviation from the centered five-year moving average, for a recent 13-year period.

For each of the four non-Bretton Woods formulas, quota calculations are multiplied by an adjustment factor so that the sum of the calculations across members equals that derived from the Bretton Woods formula. The calculated quota of a member is the higher of the Bretton Woods calculation and the average of the lowest two of the remaining four calculations (after adjustment).

Upon agreement on a new quota formula, the Executive Board is to recommend to the Board of Governors a second round of ad hoc quota increases for members that are underrepresented under the new formula and have requested that their quotas be increased. The purpose of the second round of ad hoc increases is to achieve a further rebalancing of quota shares for a broader range of members. In order to avoid the erosion in voting share of LICs, these ad hoc increases would not be effective until the amendment to the Articles of Agreement regarding basic votes becomes effective. Agreement on a second round of ad hoc increases will require the agreement of members exercising 85 percent of the total voting power. After that, legislative approval in member countries will also be required to make these changes effective.

Amendment of Basic Votes

Enhancing the voice of LICs is a central element of the reform package. A key mechanism for achieving this goal is through an increase in basic votes. Basic votes reflect the principle of equality of states and give the smallest members of the Fund (many of which are LICs), a greater voice in the Fund's deliberations. Increasing basic votes will require an amendment to the Articles of Agreement, which is a relatively rare occurrence and will itself be a delicate, three-stage process.

- The Executive Board, by a majority of votes cast, must propose a draft text of the amendment for approval by the Board of Governors.
- Next, the Board of Governors must approve the amendment—again by a majority of votes cast.
- Finally, three-fifths of the membership, having eighty-five percent of the total voting power, must accept the amendment.

Therefore, amending the Articles of Agreement will require broad support from members, and in many countries legislative approval will be needed before a member may

communicate acceptance of the amendment. Amendments become effective once the required majority of members have each communicated their acceptances and the Fund formally notifies all members of this fact.

The Governors agreed that basic votes should, at a minimum, be doubled for each member and that the increases be at least sufficient to preserve the existing voting power of LICs as a group. The amendment would also add a provision to the Articles of Agreement that the share of basic votes in total voting power should remain constant in the event of any future change in total voting power. The precise size of the increase in basic votes will be determined in a parallel manner to the determination of the size of the second round of ad hoc quota increases.

Additional Resources for Executive Directors Representing a Large Number of Countries

The large number of countries represented by the two African chairs and the heavy workload that flows from the important advisory and financing role that the Fund is playing in these countries call for further steps to strengthen the operations of these offices. In this context, Governors asked the Board to increase the staffing resources for Executive Directors elected by a large number of members and consider the merits of amending the Articles of Agreement to enable Executive Directors elected by a large number of members to appoint more than one Alternate Executive Director in order to facilitate the work of their offices.

Why Increase the Number of Basic Votes?

Currently, each IMF member has 250 "basic votes" plus one vote for each SDR 100,000 of its assigned quota. The effect of an increase in basic votes is to increase the voting power of those members whose voting power is below the average voting power for Fund membership as a whole, and thereby to allow the smallest members to have an increased measure of influence in the Fund's decision-making process. Successive general increases in quotas have reduced the share of basic votes to the present 2 percent from 11 percent when the Fund was established. The declining role of basic votes is perceived by some as weakening the voice of small developing countries in the decision-making process within the Fund.

The Road Ahead

The Fund has a global membership and global responsibilities. It is the most important and sometimes the only forum for collective action on complex economic problems. The Fund has gained legitimacy in part through its record of effectiveness. Nevertheless, if it is to retain its legitimacy and maintain its effectiveness, Fund members must be confident that they have a fair share in its decision making and that their voice is appropriately heard.

The membership has called for completion of these reforms by no later than by the 2008 Annual Meetings. This timeframe is ambitious in light of the complexity of the reforms, but recognizes the importance of reinforcing the effectiveness of the Fund.