

# SHOULD THE GOVERNANCE OF THE IMF BE REFORMED?

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**Ariel Buira**

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# Should the Governance of the IMF Be Reformed?

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1. Increasing the voice and participation of developing countries in decision making forms part of the Monterrey Consensus. This commitment was renewed in April 2003 in the IMFC and Development Committees. The September Development Cttee. Communique calls for a road map to this end.
2. Since 1997 the IMF has given increasing attention to the issue of governance. It promotes transparency and accountability among its member countries, to ensure good use of public resources.

## **Two questions on IMF Governance**

- a) How to attain adequate participation of all members in decision making?
- b) How does the IMF governance meet its own standards of transparency and accountability?

# Basic Votes and Quotas

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The 1944 Bretton Woods Conference considered two principles to determine voting power:

1. Legal equality of states: all countries have equal vote
2. Voting solely based on contributions

Compromise reached:

250 basic votes to each member plus 1 vote for every \$100,000 (later SDR 100,000) of quota.

- But with a 37 fold increase in quotas and no increase in basic votes, the share of basic votes declined from 11.3% to 2.1% of total, despite quadrupling of IMF membership.
- Basic votes of original members fell from 11.3 to 0.5%.
- Thus quotas are virtually sole determinant of voting power, a result that reduces the participation of small countries.

## Qualified Majorities and Vetoes

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At the BW Conference, special majorities were to be required in 2 cases  
Initial Articles of Agreement, special majorities (of 70% or 85%) required  
for decisions on 9 subjects

First Amendment: special majorities for decisions on 18 subjects

Second Amendment: special majorities for decision on 53 subjects

- Decisions on 18 subjects require 85% of the vote; with 17.2% US has veto
- Decisions on 21 subjects require 70% of the vote; the G-5 has 39.6%;
- Votes of G-7 Directors plus those cast by the Belgian, Dutch and Swiss directors exceed 60%.
- All important decisions require qualified majorities: quota size, sale of gold, access to resources, SDRs, rates of charge, remuneration of creditor positions, exchange rate arrangements, etc.

**With weighted voting, are qualified majorities justified?**

# Quota Formulas

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**Formula**, originally designed to meet a political objective:

US, largest quota, about 1/3 of total

British Empire quota, about 1/2 of US

Soviet Union quota, smaller than UK

China a quota smaller than Soviet Union

**The "Ad hoc" Formula:** 2% of National Income\*, 5% of gold and dollar reserves, 10% of average imports, 10% of maximum variation in exports, and the last 3 to be increased by ratio of average exports/national income\*

- Formula still in use, with variations in weights given to these variables combined with 4 others, giving different weights to same variables.
- **Discretion** is used in selection of formula to be applied in each case, determination of quotas lacks **transparency**.
- Quotas are not representative of importance of economies (Table 1).

\*Later GDP

# Table 1

<b>IMF Quotas and Gross Domestic Products for Selected Countries</b>				
<b>Country</b>	<b>Quota as of December 31, 2002</b>		<b>Share of world aggregate GDP in purchasing power parity, 2002</b>	<b>GDP, 2002</b> Billions of US dollars converted at market exchange rates
	Billions of Special Drawing Rights	As a proportion of total quotas		
Canada	6,369	2.99	2.01	728
China, People's Rep. of	6,369	2.99	12.67	1,237
Russian Federation	5,945	2.79	2.68	346
Netherlands	5,162	2.43	0.88	449
Belgium	4,607	2.16	0.59	247
Switzerland	3,458	1.63	0.45	268
Brazil	3,036	1.43	2.63	448
Mexico	2,586	1.22	1.90	642
Denmark	1,643	0.77	0.33	172
Korea, Republic of	1,634	0.77	1.78	462

Source: IMF World Economic Outlook Database.

## Table 2

### Is Africa Under-represented?

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<b>Small European Countries:</b>			
<b>Country</b>	<b>GDP in US Dollars (2000)</b>	<b>GDP in PPP (Share of World in 2000)</b>	<b>Quota in SDR's (2000)</b>
<b>Austria</b>	191.2	0.47	1,872.3
<b>Belgium</b>	228.6	0.61	4,605.2
<b>Denmark</b>	1.73	0.34	1,642.8
<b>Finland</b>	120.97	0.29	1,263.8
<b>Norway</b>	166.5	0.30	1,671.7
<b>Sweden</b>	239.8	0.50	2,395.5
<b>Switzerland</b>	240.1	0.47	3,458.5
<b>Total</b>	<b>1,188.9</b>	<b>2.98</b>	<b>16,909.8</b>
<b>African Countries:</b>			
<b>Algeria</b>	54.2	0.35	1,254.7
<b>Egypt</b>	98.7	0.52	943.7
<b>Ethiopia</b>	6.4	0.08	133.7
<b>Morocco</b>	33.3	0.24	588.2
<b>Nigeria</b>	41.9	0.27	1,753.2
<b>South Africa</b>	128.1	0.78	1,868.5
<b>Sudan</b>	11.4	0.14	169.7
<b>Total</b>	<b>374</b>	<b>2.38</b>	<b>6,711.7</b>

## Table 3 Is Asia Under-represented?

<b>Small European Countries:</b>			
<b>Country</b>	<b>GDP in US Dollars (2000)</b>	<b>GDP in PPP (Share of World in 2000)</b>	<b>Quota in SDR's (2000)</b>
<b>Austria</b>	191.2	0.47	1,872.3
<b>Belgium</b>	228.6	0.61	4,605.2
<b>Denmark</b>	1.73	0.34	1,642.8
<b>Finland</b>	120.97	0.29	1,263.8
<b>Norway</b>	166.5	0.30	1,671.7
<b>Sweden</b>	239.8	0.50	2,395.5
<b>Switzerland</b>	240.1	0.47	3,458.5
<b>Total</b>	<b>1,188.9</b>	<b>2.98</b>	<b>16,909.8</b>
<b>Asian Countries:</b>			
<b>China*</b>	1,080	11.5	4,687.2
<b>India</b>	463.2	4.58	4,158.2
<b>Indonesia</b>	150.2	1.55	2,079.3
<b>Korea</b>	461.5	1.70	1,633.6
<b>Pakistan</b>	61.1	0.55	1,033.7
<b>Philippines</b>	163.9	0.67	879.9
<b>Thailand</b>	122.6	0.95	1,081.9
<b>Total</b>	<b>2,502.5</b>	<b>21.5</b>	<b>15,553.8</b>

\*Following the accession of Hong Kong, China's GDP was 1,237 billion US Dollars converted at market exchange rates; its share of World GDP rose to 12.67, and its quota was increased to SDR 6,369.



## Table 4

### Is Latin America Under-represented?

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Country	GDP in US Dollars (2000)	GDP in PPP (Share of World in 2000)	Quota (2000)	Country	GDP in US Dollars (2000)	GDP in PPP (Share of World in 2000)	Quota (2000)
<b>Austria</b>	191.2	0.47	1,872.3	<b>Argentina</b>	284.2	0.88	2,117.1
<b>Belgium</b>	228.6	0.61	4,605.2	<b>Brasil</b>	599.8	2.68	3,036.1
<b>Denmark</b>	173.0	0.34	1,642.8	<b>Chile</b>	75.0	0.48	856.1
<b>Netherlands</b>	371.9	0.91	5,162.4	<b>Colombia</b>	78.0	0.65	774.0
<b>Norway</b>	166.5	0.30	1,671.7	<b>Mexico</b>	581.4	1.97	2,585.8
<b>Sweden</b>	239.8	0.50	2,395.5	<b>Peru</b>	52.9	0.28	638.4
<b>Switzerland</b>	240.1	0.47	3,458.5	<b>Venezuela</b>	121.3	0.47	2,659.1
<b>Total</b>	<b>1,611.1</b>	<b>3.60</b>	<b>20,808.4</b>	<b>Total</b>	<b>1,756.6</b>	<b>7.41</b>	<b>12,666.6</b>

*GDP measured in PPP is more stable than measured in market exchange rates; i.e. \$/E  
 GDP converted at market exchange rates is biased against developing countries because  
 Prices & wages in tradeable sector > prices and wages in the non-tradeable sector. Moreover,  
 the value of goods sold domestically, at below US prices, is underestimated. i.e. the price of a cup of  
 coffee in Guatemala may be 1/8 of the price of same cup in New York.*

## The Size of the IMF- Are Fund resources adequate?

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- IMF purposes include: To give confidence to members by making Fund resources available to them ...“providing them with the opportunity **to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity**” i.e. without recession.
- IMF resources declined to **under 1% of world GNI**

**Table 5. Total IMF Quotas as a Proportion of World Imports**  
(Percent)

Year	1944	1950	1965	1970	1978	1990	2000	2004
Percent	58	17	15	14	9	6	4	3 est.

Source: IMF Report to the Executive Board of the Quota Formula Review Group, IFS and WEO.

# The Decline in the Size of the IMF

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- No industrial country has resorted to IMF support over last 25 years
- Countries in control have chosen to limit the size of the IMF (quota increases require 85% majority)

## Consequences:

- Increased conditionality. The severity of an adjustment process tends to be a function of amount of financing available.
- Limited financing makes for sharply contractionary programs. Consequently, the rate of success of Fund programs has fallen sharply. i.e. less than half were completed successfully in 1973-97, but only ¼ of programs successful in 1993-97 . Mussa & Savastano 2000

**Table 6. Quotas and Voting Power of Selected Industrial Countries in 2000**

	GNI <sup>1</sup> (PPP)	GNI <sup>1</sup> (billion \$) at market exchange rates	IMF Quotas (million SDRs)	Votes	% of Total
European Union	<u>8,864</u>	<u>8,459.4</u>	<u>64,339.5</u>	<u>647,145</u>	29.8
of which:					
France	1,438	1,438.3	10,738.5	107,635	
Germany	2,047	2,063.7	13,008.2	130,332	
Italy	1,354	1,163.2	7,055.5	70,805	
United Kingdom	1,407	1,459.5	10,738.5	107,635	
Other members	2,618	2,334.7	22,798.8	230,738	
United States	<u>9,601</u>	<u>9,601.5</u>	<u>37,149.3</u>	<u>371,743</u>	17.2
<i>Memorandum Items</i>					
World	44,459	31,315	212,666	2,172,350	
All Industrial Countries	24,793	24,994	130,567	1,347,885	62.0
Developing Countries and Transition Economies	19,666	6,321	82,099	824,465	38.0

<sup>1/</sup> In 2000

Source: World Bank, *World Development Indicators*, 2002. *IMF Survey Supplement*, September 2002.

# Elements in Reforming the Governance of the IMF

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## I. Restructure the Executive Board:

- Eliminate the over-representation of the EU that has 8/9 Directors and 73% % more vote than the US with a smaller GDP.
- If EU quotas are adjusted for intra-Euro trade they fall by 40%\*
- Increase representation of developing countries

## II. Revise quota formulas

- Quotas should be closely related to size of economies (Table 1)
- Use PPP in measuring GDP to avoid:
  - distortions arising from exchange rate fluctuations
  - bias against developing countries

## III. Restore “basic votes” to their original role

## Does the IMF meet its own standards of governance?

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**Transparency** – requires all decisions be the result of open discussion with full participation of members.

- Appointments of MD and Senior Staff lack transparency
- The determination of quotas lacks transparency

**Accountability** – requires that decision-makers face up to the consequences of their decisions.

- To whom is the IMF accountable for programs that fail due to faults in design?
  - Who is accountable for under-financing of programs?
  - Developing country EDs have limited vote; they represent petitioners that may have to ask for assistance.

**Legitimacy** – requires adequate checks and balances, i.e. that all members participate fully in decision-making, that the interest of most members, developing countries and transition economies be given full consideration.

## CURRENT AND ADJUSTED CALCULATED QUOTAS FOR EU-12 (Euro zone)

	Current Calculated Quota (in millions SDR)	Share (in percent)	Adjusted Calculated Quota (excluding intra-trade in good and services) (in millions SDR)	Share (in percent)
<b>EU-12</b>	<b>234,860</b>	<b>28.3</b>	<b>120,926</b>	<b>16.9</b>
Austria	9,572	1.2	4,177	0.5
Belgium	17,709	2.1	6,649	0.8
Finland	4,955	0.6	2,592	0.3
France	38,652	4.7	21,593	2.6
Germany	62,854	7.6	34,872	4.2
Greece	3,087	0.4	2,031	0.2
Ireland	9,323	1.1	6,494	0.8
Italy	30,286	3.6	17,407	2.1
Luxembourg	12,903	1.6	3,580	0.4
Netherlands	24,562	3.0	10,990	1.3
Portugal	4,433	0.5	1,844	0.2
Spain	16,522	2.0	8,697	1.0

# Global Economic transformation must be reflected in Governance

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- The GDP of the developing countries is similar to that of the G7, in terms of PPP
- Developing countries' international reserves greatly exceed those of the G7
- In the face of major transformations in the global economy, the IMF needs a more representative decision-making process to increase its resources and enhance its legitimacy



# Does governance reform matter?

A representative Governance would help:

- the global adjustment process
- a fuller utilization of global resources
- higher rates of growth and employment
- reduce costs of financial crisis
- facilitate counter cyclical policies
- responding to commodity shocks
- other benefits dealing with negative capital flows, global liquidity, etc.