

General Assembly
Ad Hoc Open-ended Working Group to follow up on the issues contained in the Outcome
of the Conference on the World Financial and Economic Crisis and Its Impact on
Development

Sixth meeting on
“Reform of the international financial and economic system, including voice and
participation of developing countries in the Bretton Woods institutions”
(New York, 26 May 2010)

Informal summary by the Secretariat

Overview. The meeting was co-chaired by H.E. Mr. Lazarous Kapambwe (Zambia) and H.E. Mr. Morten Wetland (Norway). The main issues addressed at the meeting were based in particular on paragraphs 43-50 of the Outcome document. The co-chairs had offered a number of questions for discussion at the meeting: (1) the contribution of recent reform in the World Bank to a fair and equitable representation of developing countries and to enhanced transparency and responsiveness; (2) the principles that should underlie quota and voice reforms in the IMF; (3) how the Bretton Woods institutions (BWIs) and the regional development banks helped developing countries weather the crisis; and (4) whether regional approaches need further attention. The two speakers, Mr. Amar Bhattacharya, Director of the Intergovernmental Group of Twenty-Four on International Monetary Affairs and Development (G-24), and Mr. Yilmaz Akyuz, Special Economic Advisor, South Centre, gave presentations on the reform of the BWIs. It was followed by an interactive discussion among delegations.

Summary of the presentations by the panelists

Mr. Amar Bhattacharya, Director of the Intergovernmental Group of Twenty-Four on International Monetary Affairs and Development (G-24), spoke on the issue of voice and governance reform in the Bretton Woods institutions (BWIs). He began by illustrating the disproportionately low share of votes accorded to developing countries in the IMF and World Bank and argued that, despite some recent progress in rectifying this imbalance, the “cup is more empty than full”.

According to Mr. Bhattacharya, the differing roles and missions of the World Bank and IMF indicated the need to have different parameters to determine the voting composition of their membership. In the case of the World Bank, he called for the adoption of a comprehensive and dynamic formula that would both properly reflect evolving economic weight of countries and the Bank’s development mission. For a start, a suitably higher weight should be given to GDP (at purchasing power parity) when measuring the economic weight in the formula. In addition, financial contributions should be properly measured and IDA contributions should not be seen as the only element. In fact, the bulk of financial contributions came from counterpart funds from countries and from loan charges for the functioning of the International Bank for Reconstruction and Development (IBRD) and the International Finance Corporation (IFC). Finally, Mr. Bhattacharya argued that any robust formula must incorporate the importance of clients to the Bank’s development mission.

With respect to the Fund, Mr. Bhattacharya pointed out three main deficiencies in the existing quota formula. First, he argued that economic dynamism was insufficiently recognized. To elaborate, he referred to the evolving weight of emerging market developing countries in the world economy and pointed out that because of an increasingly larger share of the dynamic emerging market countries in the world GDP they needed to be better represented. Second, some advanced countries were improperly categorized as under-represented because of distortions in measures of openness and variability. In effect, according to Mr. Bhattacharya, this had represented a tax on some large countries and a subsidy to Europe in general. Third, borrowers from the Fund had borne a disproportionate share of the recent adjustment in quota shares. To elaborate, within the category of the advanced economies, the difference between the number of countries gaining and losing from the adjustment had been small. On the other hand, the main gainers among developing countries from this adjustment had been emerging market dynamic economies, while many lower-income countries and other emerging economies had lost out.

In closing, Mr. Bhattacharya also referred to the need for other governance reforms in the IMF, such as allowing for greater diversity in staff background and specializations, and, in general, argued that the heads and senior leadership of IFIs be appointed on the basis of open, transparent and merit based process.

Mr. Yilmaz Akyuz, Special Economic Advisor, South Centre, spoke on the topic of “Reform of the Bretton Woods Institutions”. His address centred around two broad issues: (1) the mandate and governance of the IMF in relation to its role in promoting international monetary and financial stability; and (2) the overlap in development finance between the multilateral development banks, IMF and UN.

Mr. Akyuz referred to the International Monetary and Financial Committee’s (IMFC) call on the IMF to review its mandate and to seek views regarding reform of surveillance, its financing role and the international system. He argued for a more focused IMF to address the sources and consequences of instability. For a start, he called for an improvement in policy surveillance of systemically important countries. He argued that effective surveillance was undermined by current superfluous and non-binding rules and obligations. In addition, Mr. Akyuz stressed the important role of the Fund in monitoring international financial markets and providing early warnings of fragilities and risks that could spiral into crises. Thirdly, consideration should be given to improving the global reserve system and enhancing the role of Special Drawing Rights (SDRs), which should also be allocated and utilized for development purposes. Finally, according to Mr. Akyuz, the Fund needed to improve its management of exchange rates, balance of payments and debt crises. In this respect, he argued that IMF interventions in balance of payments crises and lending had been pro-cyclical, more willing to support capital outflows than financing the current account, and had tended to create moral hazard and encourage unequal burden sharing between lenders and debtors.

Among other things, Mr. Akyuz called for reforming IMF financing through measures such as bailing-in creditors and investors via statutory mechanisms like temporary debt standstills, exchange restrictions and debt restructuring. He also pointed to the need for greater

focus on current account financing, a separation of drawing rights from governance shares and a regular and predictable SDR allocation.

In the area of governance, Mr. Akyuz argued that present voting rights in the IMF were not reflective of the relative importance of countries in the global economy. There was a need to change the formula and no single country should enjoy veto power over key policy decisions.

On the issue of development finance, Mr. Akyuz emphasized that financing by the BWIs depended heavily on aid and that dependence of the institutions on a few donors subverted their governance and undermined autonomy of the secretariat. He argued that aid should be taken out of the BWIs and should be pooled and allocated through a development fund under the UN. He also argued that consideration should be given to linking SDR creation to aid (and to climate finance) and the necessary SDRs should be allocated to a UN development fund.

Summary of the discussion

The representative of Yemen (on behalf of the **G77 and China**) emphasized the need to reform the international financial system and architecture, including issues related to mandate, representation, scope, governance, responsibility, responsiveness and development orientation of the international financial institutions (IFIs).

The speaker stressed the need for far-reaching and expeditious reform of the BWIs, particularly their governance structures, based on full and fair representation of developing countries and ensuring their full voice and participation. As a first step, the reforms should achieve at least parity of voting power for developing countries as a group in the decision making process within the BWIs.

With respect to the reform of the IMF, the speaker argued that two critical actions must be pursued. First, fundamental reforms in the IMF governance structure needed to be implemented. Second, the IMF must provide more comprehensive, evenhanded and flexible financial responses to the needs of member countries, without imposing pro-cyclical conditionalities, respecting their need for policy space and helping them overcome the crisis. Quota shares were deemed by the speaker to be the defining governance problem at the Fund. Recent changes in voting power had been insufficient compared to changes that had occurred in the global economy. He called for quota realignments in both IMF and World Bank to result in an equitable power distribution between developed and developing countries without diluting the quotas and shares of individual developing countries. He also underlined the need to promote SDRs for development purposes.

On the issue of reforms related to the World Bank and regional development banks, the speaker called for the expeditious completion of a much more ambitious reform of the World Bank's governance structure and of an accelerated road map for further reforms on voice, participation and enhanced voting power of developing countries based on an approach that was truly reflective of its development mandate and with the involvement of all shareholders in an equitable, transparent, consultative and inclusive process. Emphasis was also given to the importance of strengthening the role of all regional development banks in the search for solutions

to overcome the financial and economic crisis, as well as in the provision of medium- and long-term responses to the development needs of developing countries. In this regard, the speaker also stressed the importance of other regional, inter-regional and sub-regional initiatives and arrangements aimed at promoting development, cooperation and solidarity among their members.

The representative of the **European Union** reiterated EU support for an enhancement of voice and participation of developing countries in global institutions and global governance, including that of emerging powers, while protecting the representation for the poorest countries. He underscored what he saw as the main challenge: to strike the correct balance between legitimacy through representation and effectiveness.

In World Bank reform, he stated EU support for the shift in voting power to developing and transition countries in both IBRD and IFC. He saw this as a one-time change which did not set a precedent for future reviews. EU also supported decisions on operational reforms at the World Bank and was eager to see their effective implementation. He emphasized that the EU remained committed to further progress at the World Bank Group toward equitable voting power which would require arriving at a new voting formula by 2015, which would reflect economic weight and IDA contributions of member countries, and ensuring that selection of the President was merit-based.

The speaker reiterated that the review of IMF governance should be comprehensive and address all elements agreed in Istanbul and should be done at the October 2010 BWI meetings. IMF quotas should reflect the weight of member countries in the world economy and their capacity to support the work of IMF. The financial size of IMF should be determined by long-term needs of member countries for IMF financing. He stressed that the current quota review should achieve a shift of about 5 per cent of quota shares from over- to under-represented developing countries, while treating under-represented developed countries equally, based solely on the existing quota formula. The EU saw no merit in reopening the quota formula because of the risk of derailing the schedule of the quota and governance review. Nevertheless, voting shares of low-income countries should be protected, through ad hoc allocations where necessary. The EU saw the need for concurrent consideration of reform to strengthen the IMFC and debate on its competencies and authority as an integral part of governance reform. The speaker also proposed consideration of lowering the threshold for qualified majorities in IMF. The EU saw the importance of reform to enhance the effectiveness of the Executive Board while supporting its current size and noting the need to respect the fundamental right of constituency formation. It also supported an open, transparent and merit-based selection process of BWI leaders and senior officials, while maintaining a balanced diversity of staff with regard to gender, geography and education.

The speaker highlighted the role of the BWIs in helping developing and transition countries most impacted by the financial crisis. He welcomed the adaptation and streamlining of IMF lending facilities for low-income countries, the increase of the grant element in lending to these countries and the elimination of interest charges until the end of 2011. He called on other countries, particularly major emerging countries, to follow the example of EU's pledge of SDR4.4 billion for new loan resources. He welcomed the decision to increase the resources of

the World Bank and the regional development banks which would support them in discharging their mandate. He underscored the need to ensure that the multilateral development banks (MDBs) had sufficient resources for their concessional arms and referred specifically to the hope for expeditious progress of IDA 16 replenishment talks based on fair burden-sharing.

The representative of **Switzerland** affirmed support for governance reform of the World Bank system but underscored that the outcome fell short of fair treatment of shareholders and fair burden-sharing which could have a negative impact on donors' willingness to provide resources. Implementation was the key to the results of operational reforms which addressed oversight, accountability, transparency and ownership rights and required a realistic timeline and prioritization. He saw the reform in quota subscriptions at the IMF as sufficient to meet members' needs in normal times. Borrowing facilities such as the New Arrangements to Borrow (NAB) could meet resource needs in exceptional times. He supported selective increases in quotas to enhance the voice of under-represented member countries. He posed a question to Mr. Battacharya on how G20 discussion of issues affected governance and decision-making in the IMF.

The representative of the **Russian Federation** underscored that the second stage of voice reform of the BWIs needed to perfect the quota formula. Reform of the World Bank was needed to achieve optimal efficiency in assistance for development. This process required realistic goals and effective implementation. He raised questions about the focus of reform efforts and what should be their priority. He also asked whether it was appropriate to consider the issue of using SDRs for financing development.

The representative of **Venezuela** underscored that a new global architecture, complemented by new regional arrangements, was needed for global employment and income growth. The international community needed to create a system based on the UN to counter credit monopoly by international financial centres and conditionalities. He called for a review of the statutes governing the founding of the BWIs, especially those regarding their independence from the UN system and their accountability to member states. He highlighted changes that should be made to the governance of the BWIs: (1) democratization of the governance structures; (2) a democratic, fair and equitable process of selection of the heads of the BWIs; (3) greater participation and transparency in the discussions in the Executive Boards; (4) voting reform should increase voice of the South; and (5) BWIs should be subordinate to UN decision-making bodies.

The representative of **Mexico** welcomed reforms underway at the BWIs and stressed that a great deal remained to be done to reflect the weightings of member countries in the global economy. He also underscored the critical role of regional development banks in development. He emphasized that all IFIs should have the necessary resources to respond to member country needs. He reiterated that the selection of the heads of IFIs should be merit-based. He posed a question to Mr. Battacharya on how the dynamics of these institutions would change if reforms were made in the selection process of their respective heads. He asked Mr. Akuz about the long-term change in the role of IFIs in global imbalances given the changes in their scope of work in recent weeks with regard to the sovereign debt crisis in some European countries.

In his reply, **Mr. Bhattacharya** noted that the issues of IMF mandate and governance were closely related. He also stressed that improved governance was not only about voice, but also about responsible engagement of all stakeholders. The panelist reiterated the need to discuss what weaknesses in the quota formula ought to be addressed. In this regard, he stressed that the dominant element should be GDP. He also noted that it could be difficult to move simultaneously on many fronts in the governance reform. Consequently, a piecemeal approach could be more realistic. As for the MDBs, the panelist was of the view that development banks had not done very much. In this regard, he noted that over the last ten years the MDB net lending had been close to zero. He also argued that it would not be right to wait until 2015 for the last stage of the World Bank governance reform.

The representative of **Australia** welcomed the ongoing governance reform at the BWIs as an important first step. He stressed that there should be additional measures to improve accountability, transparency and effectiveness of these institutions.

The representative of the **IMF** posed several questions to the panelists: how, given that the IMF was a voluntary organization, to improve the traction of the IMF surveillance; and how to resolve the problem of pro-cyclical conditionality, i.e. cutting spending irrespective of the phase of the economic cycle, when there was no alternative in terms of additional resource mobilization.

In his reply, **Mr. Akyuz** stressed that before taking any measures the international community should first agree on the problems facing the world. He noted that the IMF should not be involved in development. Its objective was financial stability and not adjustment. As for the use of SDRs for development purposes, if there was agreement on that, the IMF should allocate SDRs to development institutions. This would also concern financing related to climate change. The panelist asserted the need to discuss what binding rules at the IMF were required. His view was that binding obligations could be with respect to exchange rate management including currency intervention, capital controls, target zones or currency bands. According to the panelist, it was not appropriate to cut budget deficit if they were not the result of policy mistakes. For instance, external shock should not lead to belt tightening. Also, fiscal adjustment should come from growth and adjustment by cutting the budget deficit during recession would be a recipe for a disaster.