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Center on Law and Globalization Conference Addresses IMF Governance Reform:

Experts find that a muscular IMF must solve governance issues

CHICAGO, IL- APRIL 29, 2009 – Last weekend's meetings of the G-7, G-20, and IMF/World Bank all pointed to two key issues on the global agenda. The IMF needs much deeper pockets to cope with the global financial crisis. More money at the IMF's disposal will intensify discussions on who makes decisions at the Fund.

President Obama's news conference at the Summit of Americas pointed to a massive projected expansion in IMF resources for troubled economies. Estimates range from an increase of $250 billion to $500 billion of new moneys beyond the $250 billion currently available. These moneys are intended to rescue countries whose foreign reserves are depleted, to provide credit lines for more stable countries like Mexico that might need some liquidity in reserve, and to give a cushion to the poorest countries where the global financial crisis will hit vulnerable populations most severely.

It is not surprising that Mr. Obama linked this great expansion of IMF powers to major changes in the way it is governed.

The IMF confronts Governance Critics

At a recent meeting convened by the Center on Law and Globalization, a joint enterprise of the American Bar Foundation and University of Illinois College of Law, senior IMF legal officials discussed with academic experts on the Fund and IFIs constructive ways the IMF can get beyond criticisms.

Sean Hagan, General Counsel of the IMF and a member of the Center's International Advisory Board, acknowledged that "we face enormous challenges, but the crisis is catalyzing reform within the IMF." Said Hagan, "among other things, the crisis brings greater urgency to governance reform." Two years ago, says Hagan, the Managing Director decided "to take a proactive role—the need for Governance reform had become so acute that it was perceived as undermining the legitimacy of the IMF."

In April 2008 the IMF began changing voting quotas by increasing the voting power of 54 IMF members, including many developing economies. The IMF shifted from an exclusive reliance on GDP to calculate a country's economic power to one where purchasing power parity was also taken into account. The important winners were China, Turkey, Mexico, Turkey and Brazil.

Although important steps have been taken to shift voting power to emerging markets, it is generally regarded as too modest.

A Reform Committee recommends major changes

To press forward, the IMF created a governance review panel of distinguished persons, chaired by South Africa's Finance Minister, Trevor Manuel. The panel's report, released immediately before the G-20 meeting in London, points to far-reaching changes.

- Create an IMF Council: Ken Dam of the Manuel Committee told the conference that a much more powerful IMF needs influential policy-makers to make its key decisions. The Report proposes a new Council of national finance ministers should act as its governing board and set strategic policy. Council members would be more likely to exercise their domestic political strength to ensure constructive IMF influence at home. At the same time, they can form a strong political base for IMF authority worldwide.
- Remove U.S. veto power: The Manuel Committee recommends a shift to 70% majorities for major decisions, said a committee member, so that "the U.S. will no longer be able to throw its weight around to other countries."
- Give other countries veto power: Proposed changes to voting through the use of double majorities "will help low income countries band together to veto activities they don't like." Said Mr. Dam, "this will provide a balance between the veto capabilities of high and low income countries."
- Elect the Managing Director: It can "no longer be tolerated," says Ken Dam, that the Director must always be a European. There must be an open selection process.
- Broaden Staff expertise: IMF has recruited staff with expertise in money and fiscal policy. Now new competencies over wider areas of financial instruments and markets are needed

- Shield Staff from Political Pressures: The Executive Board, sitting three times a week in Washington for three hours a day, has got heavily involved in operations. The Executive Board should provide oversight of IMF operations without micro-managing. This would also insulate staff from the fact or appearance of political pressures.

<u>The Proposals Face Hurdles</u>

Terence Halliday, Co-Director of the Center on Law and Globalization, says that “experts on the IMF expect that some of these proposals will face major hurdles.”

The U.S. Treasury and U.S. Congress would need to agree that the U.S. give up its veto power, a step that could face difficulties in Congress where this could be viewed as a surrender of sovereignty to the IMF rather than a step to a more legitimate international organization.

Other countries might be reluctant to give the IMF the force of hard law in the international order. And many European nations could get cold feet at the idea of consolidating the several European seats on the Executive Board to a single seat on the proposed ministerial Council or Executive Board. The fact that representation in the proposed Council and in the current Executive Board now is held by nations, not a supra-national body, also creates some technical difficulties for E.U. representation.

The shift in the role of the current Executive Board from its close involvement in operations to an accountability role of management oversight is a major institutional change that will require flexibility and adaptations by current and aspirant Board members.

Despite the difficulties, the Manuel Committee speaks with much authority. It responds to changes from developing nations. Within the E.U. some welcome the idea of an E.U. bloc which would be larger than the U.S. A commentator on the IMF, law professor Daniel Bradlow, states in a recent blog that “the world needs the IMF.” But it has to be an IMF without the coordination, functional and legitimacy problems it currently has.

The Spring 2009 meeting of IMF and World Bank may not have the drama in the streets of G-7 meetings. But the politicking that continues among the G-7, G-20 and IMF leaders will determine how far the proposed governance reforms will make credible the high aspirations the President anticipates for this much empowered player in the world economy.

The Center on Law and Globalization is a Partnership of the American Bar Foundation and the University of Illinois College of Law. The Center brings together the top legal officials of international organizations, key journalists, and academic experts to understand behavioral and legal dimensions of critical global issues, to stimulate well-informed global policy choices, and to advance empirical research on globalization and law.

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