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on

Reforming the Governance of the IMF

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Although the IMF is an international organization, its members do not have equal voting power. At the Bretton Woods Conference in 1944, a compromise solution was adopted between two approaches for determining voting power, one related solely to members' contributions, or quotas, and another based solely on the legal principle of equality of states. The compromise assigned voting rights on a combination of the two: it gave each member country one vote for every $100,000 of quota (later for every SDR 100,000) plus 250 basic votes. Basic votes, and the voice in decision-making they gave smaller countries were also considered to be necessary in view of the regulatory functions of the Fund in certain areas. Because the number of basic votes has note been changed with successive quota increases, the ratio of basic votes to total votes has declined from 11.3 percent in 1945 to 2.1 percent today.

With the increase in quotas, the proportion represented by basic votes in the total falls, which raises the relative voting power of larger countries. With the accession of new members the total number of basic votes rises, but not necessarily their share. Nevertheless, the importance of the basic votes of any given member in the total continues to diminish. With the nearly 37-fold increase in quotas since then, the share of basic votes in the total has declined to 2.1 percent despite a four-fold growth in membership. This has substantially shifted the balance of power in favor of large countries, away from the compromise agreement contained in the Articles of Agreement that was designed to protect the participation of small countries.

The original quota formula responded to no economic logic and was designed to attain a political objective: the United States (US) should have the largest quota, the United Kingdom (and its then colonies) about half the US quota, the Soviet Union an amount just under that of the United Kingdom, and China somewhat less. The major concern was that the US military allies (i.e. President Roosevelt's *big four*) should have the largest quotas, with a ranking on which the president and the secretary of the treasury had agreed.

Given this historical fact, it is remarkable that—with only some adjustments in the weights and definition of the main variables of the quota formula—the IMF continues to use the original formula for determining members' quotas today. The original formula is now combined with four other formulas, which give different weights to the same variables, and an element of discretion is used in selecting the formula to be applied in each case. (At times, the average of the various calculations is used to set a country's

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quota.) It is therefore not surprising that current quotas are far from representative of the actual size of economies, of their ability to contribute to the IMF, or of their importance to the world economy.

This can be easily illustrated by the fact that such large countries as Brazil, Mexico and the Republic of Korea, with real gross national incomes (GNIs) and populations much larger than those of Belgium, the Netherlands and Switzerland, have quotas that are only a fraction of the latter countries' quotas—and fewer votes. Another case is that of Canada, which in real and nominal terms is much smaller than China's economy, yet Canada's quota in the Fund is equal to that of China. Note also that measured in real terms, the Canadian economy is smaller than that of the Russian Federation, Brazil and Mexico, but Canada's quota is much larger than any of these countries' quotas. Thus, for many developing countries, their share in decision-making is not commensurate with the systemic importance of their economies. (See Table 1.)

TABLE 1
IMF Quotas and Gross National Incomes (GNIs) for Selected Countries

Country	Quota effective December 31, 2002 (Billions of Special Drawing Rights)	Purchasing power parity GNI, 2000 (Billions of US dollars)	GNI, 2000 (Billions of US dollars converted at market exchange rates)
Canada	6,369	836	650
China, People's Rep. of	6,369	4,951	1,063
Russian Federation	5,945	1,165	241
Netherlands	5,162	412	398
Belgium	4,607	282	252
Switzerland	3,458	219	274
Brazil	3,036	1,243	610
Mexico	2,586	861	497
Denmark	1,643	145	172
Korea, Republic of	1,634	818	421

Source: IMF (2002); World Bank (2002)

It would be difficult to argue that, for instance, the quota of China, the second largest economy in the world measured in terms of purchasing power parity, should be identical to that of Canada. Or that Belgium's quota, and therefore influence on governance, should be 52 percent larger that that of Brazil, and 74 percent larger that that of Mexico. Or that Denmark should have the same weight in international monetary and financial decision-making as the Republic of Korea. Moreover, many of the major differences that arise mainly between the quotas of developed and developing countries are not simply the result of history. For instance, in the calculation of quotas for Switzerland, a recent member of the Fund, the quota was determined in line with that of other industrial countries with a similar economic structure and levels of development. As a result, distribution of quotas is skewed.

Quotas are important not just because they confer decision-making power but also because they determine access to financing. But for some exceptional cases, a member can borrow only up to a total of 300 percent of its quotas under regular Fund facilities. Thus the small quotas of developing countries limit both their share of voting power and their access to IMF resources.

The consequences of the imbalance of power have been further aggravated by the fact that since the late 1970s, no industrial power has resorted to Fund support. This development has changed the nature of the Fund. Formerly, when the Fund was a credit cooperative and all members drew resources from it form time to time, they all had an interest in these resources being available on reasonable terms and conditions. Over the years, however, the Fund has turned into an institution consisting of two distinct groups of countries: industrial country creditors and developing country debtors. The fact that for some twenty five years the Fund has lent only to developing countries has come to mean that the creditor countries try to lend as little as possible and therefore favor a hardening of conditionality, while prospective borrowers, generally wish to have ample access to financing and tend to be defensive of their country's short-term interests. Thus, the objectivity and impartiality of the Executive Board of the Fund (assumed by the Articles of Agreement) has been eroded to a significant extent.

Recently, the idea of applying certain principles of corporate governance to protect minority rights in international financial institutions has elicited growing interest. These principles would seek to ensure a minimum degree of transparency and voice, or participation, in certain decisions. Such principles would also seek to ensure that members seeking financial support receive a certain protection against excessive demands in the Fund.

Because political and economic changes have not been appropriately reflected in the decision-making structure of the Fund, this structure has become dysfunctional, and the governance of the Fund and the legitimacy of the Fund's policies have been increasingly questioned. Too often, the member countries see programs more as inevitable impositions, aimed at serving the economic and political interests of other parties, rather than as a result of an exercise in monetary cooperation, in which their full participation gives them a sense of ownership. It is hardly coincidental that while the need for support of a significant group of developing countries has risen, the size of the Bank and the IMF has shrunk relative to world trade—and even more so in relation to international capital movements.

The smooth functioning of the Fund would seem to require a balance between the different interest groups. Therefore, a point of departure for the necessary negotiation leading to the re-apportionment of quotas and the revision of basic votes could be an agreement that the groupings of industrial and developing countries, or of potential debtor and creditor countries should each have about half of the total vote of the Board. A further stage could be the revision of quota formulas, particularly the weight to be given to national income or output (measured in purchasing power parity) and other variables. But since it would be difficult to come to an agreement on quota formulas without reference to what would happen to the determination of the share of basic votes in the total, this might have to be a simultaneous exercise.

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