

Testimony of

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Mr. Chairman and members of the Subcommittee, thank you very much for the opportunity to testify regarding the Administration's request for a \$100 million contribution to the IMF's Enhanced Structural Adjustment Facility (ESAF) program. Since 1987, the ESAF program has been a valuable tool for supporting economic reform and recovery in the poorest nations. It has a successful track record in many countries, though not in as many as it might. Moreover, the proposed \$100 million contribution is part of a multilateral effort already subscribed to by more than three dozen countries, so that the overall ESAF program will be able to extend loans of more than \$5 billion, to the poorest countries of the world.

For these reasons, I strongly support the proposed extension of the ESAF and the U.S. contribution. But I do not support that extension unconditionally or at this time. The U.S. contribution should be delayed until the IMF management and Executive Board create conditions to ensure the more effective utilization of replenished ESAF resources.

The IMF fails to abide by one of the most basic American beliefs about good governance: the need for openness and accountability in official institutions. The IMF is probably the most secretive international institution outside of the military and security areas. All of its operational documents, including all loan agreements, policy recommendations to member governments, and even the annual reviews of member-country economies (so-called Article IV consultations), are confidential, and are not available for public scrutiny. Moreover, this confidentiality is without expiration date. As far as I know, the IMF has not released any operational documents previously characterized as confidential since the inception of the institution, in 1946.

It is easy to be misled by IMF procedures regarding

publication of documents. The IMF supplies voluminous materials to the public, including valuable data on member-country economies. It also publishes general analyses of the economic developments in several of its member countries. This documentation does not, however, describe the IMF's detailed advice concerning economic policies, nor the terms under which IMF loans are made available, nor the detailed results of IMF programs. The IMF tends to issue studies on "successful" cases but not on unsuccessful cases where its own advice should be subjected to scrutiny.

The work of the IMF staff is, of course, subject to the approval of the Executive Board of Directors, constituted by Finance Ministry officials of a subset of member countries. It is also the case that an individual congressman can peruse IMF documents through the U.S. Executive Director's office. But this is an insufficient basis for oversight. There is no public availability of key information in the countries undertaking economic reforms, nor in the donor countries, nor in the professional communities of economists, bankers, investment analysts, political scientists, development aid specialists, and others that have extensive professional knowledge of the countries in question.

The IMF's secrecy has at least two sources. Formally, the IMF operates under the mandate of the Executive Board. Many member governments resist the publication of information concerning their own economies. Many members have no tradition or inclination to release public information about their economic policies. The IMF management and staff have pointed out that the IMF receives information on a confidential basis from member countries, and so must keep that information confidential unless the Executive Board deems that other procedures are appropriate. At the same time, the IMF staff is eager to preserve the secrecy of the institution. The secrecy lessens public scrutiny and insulates the staff from accountability. While it is true that the current secrecy reflects the decisions of many countries and not just the IMF management, there is no reason why the U.S. should simply abide by these decisions, or should be prepared to appropriate funds for the ESAF under current procedures.

In my professional judgement, IMF secrecy has had serious adverse consequences for the design and implementation of IMF programs, including ESAF programs. As economic advisor to more than one dozen governments that have had extensive dealings with the IMF, I have found the quality of IMF recommendations and program design to be uneven, and in many cases to fall below best professional practices. Even when the general direction of IMF advice is salutary, as it usually is, the specific content of that advice is often flawed, leading to program failures that could and should have been avoided.

There is no realistic possibility under current circumstances

for public scrutiny to help correct these shortcomings. According to IMF public relations, all economic success stories are partly the result of good IMF advice, and all economic failures are due to shortcomings in the reforming country, but never to the IMF recommendations. I know from personal experience, however, that many economic successes resulted from measures that were initially vehemently opposed by the IMF; and many failures came because of flaws in the design and timing of IMF programs. Nonetheless, without the written record, there is no realistic way to have a serious public debate on the key issues, nor to bring public pressure to bear to correct the flaws in IMF programs.<sup>1</sup>

I have recently had several difficult experiences as a result of this secrecy. I have recently prepared a study and critique of IMF policies in Russia, for an annual World Bank conference that will take place later this month. Despite the urgency of the issues involved, I was not allowed to quote from IMF documents in the presentation of my arguments. This is like having a debate with a phantom. Last year, at the invitation of the Kyrgyz President, I offered a written critique of IMF policies in Kyrgyzstan. The IMF subsequently applied informal pressure to key members of the Kyrgyzstan Government to stop "complicating" matters by having more than one source of macroeconomic advice.

Let me summarize the kinds of technical issues that arise in the preparation of an ESAF program. When an IMF member government is in financial distress, and appeals to the IMF for a loan, the IMF must make several important judgements, of the following sort:

- (1) In meeting the financial crisis, what should be the relative weights given to budget cutting, foreign financial flows, and debt reduction?
- (2) What should be the timing and use of the IMF's own resources as part of the overall assistance package?
- (3) What kind of exchange rate arrangements should the IMF recommend (in fact, require): a floating exchange rate, a crawling peg exchange rate, or a fixed exchange rate?

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<sup>1</sup>I will cite one example of pressing relevance. The IMF initially opposed the early introduction of the Estonia currency, and the use of a currency-board arrangement for the Estonian Central Bank. The Estonians decided to proceed anyway, and at the last moment, the IMF decided to support the effort. Later on, the IMF has basked in the acclaim of the Estonian monetary reforms, which had gone ahead despite its opposition. Currently, several other countries in the Former Soviet Union, such as Kyrgyzstan, would like to explore the feasibility of a similar currency-board arrangement, but are strongly advised by the IMF not to proceed in that way.

(4) What kind of institutional reforms should be recommended, and perhaps required, as a condition of the lending: central bank independence, budgetary reform, and so forth?

In my view, the IMF makes systematic and repeated mistakes on these delicate questions. Most importantly, the IMF puts too much weight on budget cutting, and not enough on foreign assistance and debt relief as mechanisms for addressing the acute phases of a financial crisis. The IMF often limits the availability and use of its own funds to the point of rendering the IMF loan itself little more than window dressing.<sup>2</sup> There is too much IMF reliance on floating exchange rates, and not enough use of pegged exchange rate (crawling or fixed) as a key "nominal anchor" in stabilization programs. The IMF generally pays insufficient attention to institutional reform, such as central bank independence or currency-board arrangements for smaller countries.<sup>3</sup>

The case for greater public disclosure rests on three legs. First, it would raise the chances for well-functioning IMF programs, by bringing to bear public and professional scrutiny and debate on IMF analyses. Second, it would enhance Congress's and the public's ability to oversee the use of funds appropriated for the ESAF program. Other than the U.S. Treasury itself, there is no General Accounting Office, Congressional Budget Office, or independent watchdog groups that provide independent checks on the use of the funds. Therefore, it is extremely important that the program's documents be made publicly available.

Third, and equally important, greater IMF openness would improve the political accountability and democratic functioning of the member governments that seek to draw upon IMF resources. Some of the least democratic governments in the world have been regular users of IMF funds, including ESAF funds. These governments agree to take actions that involve the most basic welfare of their citizens, and yet do not involve their own citizenry in the formulation and debate over these measures. Moreover, the IMF encourages this secrecy, even years after IMF agreements have been put in place. We should be pushing, indeed requiring, countries that want to draw on IMF funds to be more open about their policies

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<sup>2</sup>In the IMF's loan to Russia in the summer of 1992, for example, the IMF made available \$1 billion, but under the condition that the money be held in the bank as reserves, and not actually be used.

<sup>3</sup>Despite the success of Estonia's currency board, the IMF has aggressively rejected a similar arrangement in Kyrgyzstan and in Mongolia, two countries where I have advised. The IMF also gave deeply flawed advice to Russia and the other CIS states in 1992 to maintain a common currency, despite the profound inflationary consequences, which were predictable and predicted.

to their own citizens as a condition for the privilege of using U.S. taxpayer dollars.

The U.S. Treasury has recently suggested that IMF loan documents are too sensitive to be released to the public. I would strongly reject this claim. The kind of information that is in an IMF agreement is almost always available in democratic countries in any case, and should be automatically available in all countries. It is true that some information is too sensitive to be released immediately, such as information on exchange rate and interest rate policy decisions to be carried out in future weeks. Moreover, sensitive negotiations may need to be pursued outside of the public glare, before agreements on controversial policy measures are reached. For these reasons, there is a plausible case for allowing a delay on the required release of IMF loan documents for a few months -- perhaps 6 months -- so that negotiations can be completed and "prior actions" in the financial markets can be undertaken. Governments may of course choose to release the documents earlier, and in most cases should.

In our own country, the Federal Reserve Board has found ways to reconcile the need for operational secrecy at the moment of decision-making with the equally pressing need for public scrutiny of those decisions, through the release of the minutes of FOMC meetings with a delay of six weeks, and through the Congressional oversight of Federal Reserve policy. That kind of pragmatic compromise makes vastly more sense than the blanket assertion that IMF loan documents deal with materials "too sensitive" for the public view.

### Recommendations

The Administration's request for \$100 million for the ESAF program should be supported vigorously as soon as the IMF makes the necessary changes to open the institution to public scrutiny. The U.S. Treasury should play a far more active role than until now in pressing for greater openness and accountability of the IMF. I would recommend the following steps.

(1) In order to establish the historical record of IMF activities - for economists, historians, policy analysts, politicians, and other interested parties -- all documents that were reviewed by the Executive Board before January 1, 1989, and including all loan agreements, should be made available to the general public. A general policy should be established to make available all such documentation on a routine basis with a lag of 5 years.

(2) With regard to new loan agreements from this point forward, all loan documentation reviewed by the Executive Board should be made available to the general public within 6 months of the loan approval by the Executive Board. This documentation would include

the formal Request for Purchase; the Staff Appraisal; the Letter of Intent; the text of the Purchase agreement itself; and other relevant documentation as might be presented to the Executive Board in connection with the loan. If there are urgent and specific reasons for not releasing a document, the member country could appeal to the Executive Board to vote a waiver, which would delay the release of the documents for an additional fixed period of time, perhaps an additional 6 months. Note that previous loans agreed to after January 1, 1989 and before the start of this new policy would remain confidential for the five-year waiting period.

(3) Other standard documentation reviewed by the Executive Board (Recent Economic Developments [REDS], Article IV consultations, policy framework papers, etc.) should also be released to the public within six months of review by the Executive Board. It is important to stress, however, that the key operational documents are related to loan agreements, and these are the documents for which public scrutiny and debate are most critical. Attempts to "open" the IMF by the release of the less-operational documents (e.g. Article IV consultations) would not be sufficient.

(4) The IMF should create an Independent Advisory Board composed of distinguished bankers, political scientists, economists, and former government officials with relevant experience, to act as an advisory body concerning the design and implementation of IMF programs. This IAB would make recommendations and comments to the Executive Board; commission independent studies and analyses on key issues (e.g. the design of exchange rate policies in the course of stabilization); and be available to member governments seeking an independent professional opinion on a central point of program design. The IAB could also be vested with more formal authority as a kind of independent review panel that would make recommendations to the Executive Board vis-a-vis the design and implementation of IMF lending programs.

(5) The U.S. should propose other mechanisms for increasing the scrutiny of IMF programs. For example, the IMF Executive Board should commission independent teams of experts to make recommendations in particular countries, with these recommendations put before the Executive Board, together with or in lieu of internal staff recommendations. Moreover, member countries should be encouraged, and given the formal opportunity, to invite independent teams of experts to submit recommendations to the Executive Board.

(6) As the U.S. might not be able to prevail upon other IMF member countries to support this new standard of openness, it might be necessary to instruct the U.S. Executive Director to vote against loans to countries that decline to comply with the requirement for public disclosure. Moreover, the U.S. Treasury should be directed to report to the Congress on progress in establishing the new disclosure regulations. The Congress can wait to authorize and

appropriate the ESAF funds until adequate disclosure policies of the U.S. Government and the IMF have been agreed.

(7) The U.S. Treasury should also be instructed to explore new ways, in the longer term, to mobilize financial support for member countries in crisis by tapping the private capital markets, rather than taxpayer-supported loans. For example, in analogy with companies in Chapter 11 bankruptcy, member countries in crisis might be given the opportunity to borrow from the private sector on a priority basis, so that the country's new creditors would be placed first in line for repayment, ahead of existing creditors. (Such debtor-in-possession financing with administrative priority, is typical in Chapter 11 bankruptcy, and is covered in the U.S. Bankruptcy Code, Chapter 11, § 364). Such an approach could trigger billions of dollars of private financial flows to financially distressed economies. There are several legal and policy complexities that would have to be sorted out in order to move forward on this kind of approach (e.g. whether to establish the approach through treaty, or policy of the IMF Executive Board, or other means), but the general direction is promising enough to merit the effort.