Opinion: The World Bank and the IMF need to keep reforming to become fit for purpose

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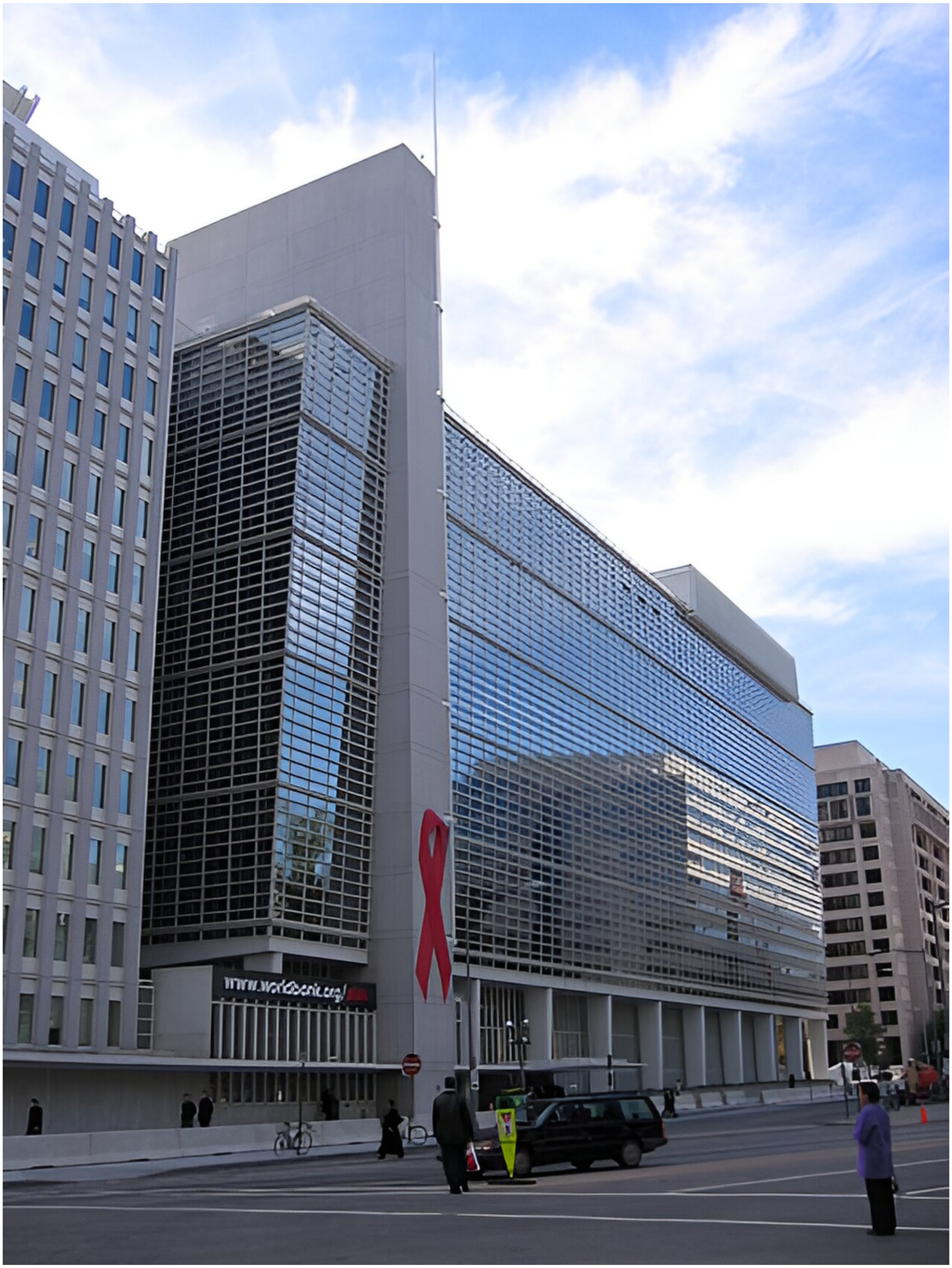
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The World Bank HQ Main Complex. Credit: Jaakko H./Wikimedia Commons,

The World Bank and the International Monetary Fund are being challenged to make substantial reforms so that they become fit for purpose in the 21st century.

Some suggest that they cannot be sufficiently reformed and should be shut down. Others, including myself, contend the world needs effective international financial institutions. If they did not exist, we would have to create them. Consequently, we must try to make them more credible, legitimate, inclusive, responsible and effective. The challenge is doing so within the constraints of their founding treaties.

This article is based on my book The Law of International Financial Institutions. It provides some background on these institutions and discusses the problems they are confronting and their potential for reform.

Some history

Prior to 1944, countries fixed the value of their currencies in terms of gold. This system collapsed with tragic consequences in the inter-war years.

The purpose of the 1944 Bretton Woods conference was to create a new international monetary order. It was an exclusive affair. Only 44 out of the then 99 officially recognized countries were represented. A large portion of humanity was living under colonial domination and didn't take part in the negotiations.

Four characteristics of this new international order are noteworthy.

First, it created the first rules-based international monetary system. The participating states agreed that the IMF would oversee the new order. In return, both the IMF and World Bank offered their member states financing. The financing came with terms and conditions and the IMF and the World Bank could hold the states accountable for failing to comply with them.

Second, the member states accepted that the governance of the institutions would be based on weighted voting, with each member state receiving a vote that corresponded to its economic size and financial contribution. This effectively modified the principle of sovereign equality which is at the core of the international legal order. A state could be outvoted and forced to comply with policies that it opposed.

Third, the legal status and powers of these new institutions was only clarified over time. Most significantly, they were given immunity to mitigate the risk that a member state would use its authority to interfere with their operations in that state. Therefore, they cannot be sued in any court in the world.

Fourth, the treaties are silent on their environmental and social responsibilities.

Evolution

By the mid-1970s, the two institutions were operating in a very different world. Many states in Africa and Asia had become independent and had joined them. They had different needs and priorities from the original member states. However, because of their relative level of economic development, they lacked the votes to change policies and priorities.

Second, the system created at Bretton Woods collapsed in 1973. It was replaced by a system in which markets played a great role in determining the value of currencies and each state could decide for itself how to conduct its own monetary policy.

Third, concerns about the environmental and social impacts of economic activity were beginning to grow around the world. It resulted in controversies involving projects funded by the World Bank and programs funded by the IMF.

Fifth, civil society organizations were becoming more important actors. They were concerned that the operations of these institutions were causing substantial harm to local communities and the environment. They began to campaign for the World Bank and IMF to become more transparent and accountable.

The two institutions have made some efforts to respond to these developments.

Governance. The number of member states increased by over four times between 1946 and 2023. However, the size of their boards of executive directors has only doubled. This means that it is harder for many states to have their concerns about policies, procedures and operations raised at the board level.

Consequently, the institutions are likely to be less responsive to the concerns of their smaller and poorer member states than to their richer and more powerful member states.

This problem is exacerbated by the institutions' declining financial capacity. When the IMF opened for business, its total resources were equivalent to 3% of a global GDP of about US$10 trillion (in 2011 dollars). Today, they are equivalent to about 1% of a global GDP of about US$100 trillion.

Responsibility. The institutions have acknowledged their responsibility for the environmental and social impacts of their operations and that there are some human rights issues that are relevant to their operations. However, they have struggled to develop an effective and sustainable approach to these issues.

One reason is that there is no agreement on which standards they should use in addressing these issues.

A second reason is that understanding these issues requires them to do impact assessments and to consult with affected stakeholders. But both require them to interact with a broader range of stakeholders in their member states than was originally envisaged. It may also require them to engage with groups that are opposed to the projects or policies.

In response, the World Bank has developed its own operational policies and procedures for its staff. They also educate external actors about what they can expect from the bank in regard to environmental and social issues. This is not always acceptable to their member states.

The IMF has maintained that, because it focuses on macro-economic issues and policy based finance, it is difficult to establish causal links between its operations and their environmental and social impacts. But it has now acknowledged that these issues can be "macro-critical" and that it needs to pay attention to them. It has not yet adequately explained how it will do this.

Accountability. The expanding role and responsibilities of the World Bank and IMF raise complex issues. There is a risk that they will make mistakes that result in some stakeholders having to assume an unreasonably high share of the costs of these projects or policies.

In 1993, the World Bank created an independent accountability mechanism, the Inspection Panel. Despite its shortcomings, it was an important international legal development.

The IMF has not established its own independent accountability mechanism. It is one of the few international organizations that does not offer its external stakeholders any means for holding it accountable.

What next?

The World Bank and IMF need to continue evolving if they are to remain fit for purpose in the 21st century. They need to develop governance arrangements, operational policies based on international norms and standards, and accountability structures that respond adequately to the challenges of climate, poverty, inequality and discrimination. Their richer member states need to provide them with adequate resources to fulfill their mission.

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