GLOBAL FINANCIAL
GOVERNANCE & IMPACT
Report 2014

New Rules for Global Finance
About Us

New Rules for Global Finance is a non-governmental organization, with the aim to promote reforms in the rules and institutions governing international finance and resource mobilization, in order to support just, inclusive and economically sustainable global development. New Rules is a networking, idea generating organization that convenes critical actors and policymakers from developed and developing countries to identify politically feasible and technically sound solutions to systemic issues of international finance and resource mobilization which impede inclusive development. The US Internal Revenue Service recognizes New Rules as a tax exempt organization according to Section 501 (c) 3 of the US Internal Revenue Code.

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About this publication

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Executive Summary

This report is the second critical assessment of the major global institutions engaged in international financial rule-making: the Financial Stability Board (FSB), Group of Twenty (G20), International Monetary Fund (IMF), Organization for Economic Co-operation and Development (OECD) and World Bank. It is a collaborative effort by New Rules Board and staff, and several civil society organizations and academics who share our urgency regarding the need for a global financial system that incorporates the perspectives of low income countries (LICs) and generates positive outcomes for world’s poorest people.

We continue to use our “GOVERNANCE scorecard” to evaluate the four core elements of good governance: Transparency, Inclusiveness, Accountability and Responsibility. The scores are slightly higher than last year, due to new information from the institutions and revised assessments by independent analysts on accountability and responsibility processes, as well as a slight increase in their ex ante analysis of potential impact. Occasionally, authors and editors differed on scoring. Editors slightly adjusted scores in order to maintain appropriate scoring consistency across all institutions. Where discrepancies exist, authors’ scores are noted. Nevertheless, as Chart 1 shows, all institutions’ overall governance scores remain at moderate or poor levels.

![Chart 1 Governance Financial Governance Scores from 2013 and 2014](chart.png)
The G20 and OECD continue to perform especially poorly across all governance criteria. To address this, we recommend that the G20 should formally engage with the UN; design more inclusive representation; establish formal channels of engagement for low-income countries and other external stakeholders; become more transparent; establish a more comprehensive accountability framework; ensure ex ante and ex post evaluations are conducted regularly; and, create a formal external complaint mechanism. We do not feel that it is possible for the OECD to be sufficiently inclusive given the composition of its membership, and therefore recommend the establishment of a World Tax Authority under the UN.

Our principal recommendations for Governance can be found on page 9 while specific recommendations for each institution are in the text of respective chapters.

Last year’s report assessed the IMPACT of the institutions using an ad hoc framework. This year, in an effort to improve the impact analysis, we invited the institutions themselves and independent analysts to advise us on how to establish a better framework. Their primary recommendation was to use combating inequality as this year’s organizing theme. This is because inequality: has intensified under the current financial system where the rules and structures serve the interests of a few; has increasingly been seen as a core part of the mandate and responsibilities of global financial governance; and looks set to be a strong part of the post-2015 global development framework.

We have therefore considered qualitative and quantitative information to assess each institution’s contribution to reducing inequality, based on its mandate. The assessment uses a four point scale: 1-worsening impact on inequality; 2-no observable movement; 3-some progress; and 4-excellent progress. The results are not very encouraging, as Chart 2 shows.

In terms of impact, the best performing institutions are the FSB and the IMF:

- FSB member state regulators and Secretariat staff have been making considerable progress on addressing some root causes of the 2008 financial crisis, especially on Over-the-Counter Derivatives and

![Chart 2 Overall Impact Scores of Global Financial Rule-Making Institutions](image-url)
the new Global Legal Entity Identifiers System (GLEIS). However, progress has been very slow on cross-border crisis resolution, stopping institutions from being “too big to fail”, and reining in shadow banking.

- **The IMF** has made limited progress in monitoring and encouraging anti-inequality spending on education and health, and remains a key source of financing to combat inequality by offsetting global instability. It has also produced very positive policy pronouncements and research studies supporting the role of redistributive policies in reducing poverty and inequality, in turn making growth more sustainable. Yet on crucial policy issues such as employment and wages, progressive taxation and pro-poor financial systems, the authors could not find consistent evidence of policy advice yielding reduced inequality.

The **World Bank** and the **OECD** fall slightly behind, for the following reasons:

- The **World Bank**’s commitment to eliminating abject poverty and ensuring greater equality for the bottom 40 per cent by 2030, is grounded in its positive commitment to universal education and health care, and in its strong record of financing development programs. However, its policy assessment frameworks (Country Policy and Institutional Assessment (CPIA), Doing Business) and economic policy conditions are in some respects likely to be exacerbating inequality, as is its private sector support via the International Finance Corporation (IFC).

- The **OECD** has made some recent progress on curtailing illicit flows and combating tax evasion through its recent efforts to enhance exchange of information among tax authorities; and has over the years played a positive role in exchanging best practices on efficient and effective tax administration. However, it has made little progress on tackling tax avoidance, combating tax wars or promoting progressive tax policies.

The **G20**, which has had the lowest impact, has pledged great advances and demonstrated little progress at the global level, and most members have made only minor pledges and delivered less at national level. It deserves some credit for having reignited serious debate about the need for global tax reform and mandating the OECD work on illicit flows and tax evasion. However, it is neither monitoring nor acting against rising inequality, deteriorating employment conditions and falling real wages, and has done nothing discernible to promote either anti-inequality development policies, or concessional financing to combat inequality.

Our principal recommendations for Impact can be found on page 10, while specific recommendations for each institution are in the text of respective chapters.
Introduction

**A GLOBAL FINANCIAL GOVERNANCE AND IMPACT REPORT IS EVEN MORE VITAL**

For over a decade New Rules for Global Finance (New Rules) has engaged in reform of the institutions shaping global finance. We persist in asking: Who wins? Who loses? And, who decides? We continue to champion reform of the governance of these institutions, working to bring the voices of the excluded and affected peoples into the decision-making rooms; or as a poor second best, at least indirectly by getting their concerns and their wisdom inside the room. Those not among the deciders are likely to be the losers.

This second edition of the *Global Financial Governance & Impact Report* continues the immodest task of assessing the governance and impact of the institutions that write the rules for global finance: the Financial Stability Board (FSB); Group of Twenty (G20); International Monetary Fund (IMF); World Bank; and international tax rules-making bodies, focusing this year on the OECD.

Some might ask why this is important given that the world economy has largely emerged from the global financial crisis of 2008. The answer is that high-quality governance of global finance, ensuring that it has a positive impact on reducing global poverty and inequality, is even more vital if we are to accelerate global growth (which will be more sustainable if poverty and inequality are reduced), and avoid future crises which would throw such progress off course.

**HOW WE HAVE ASSESSED GOVERNANCE AND IMPACT**

Our method for assessing the quality of global financial governance has not changed from last year – though information available to support the assessments has improved due to close cooperation with the institutions themselves and additional groups of independent analysts. The basic criteria remain the same:

- **Transparency**: Any institution making rules that affect the entire world, must be held to the highest standards of transparency, so that those who make the rules will know the interests of and the potential impacts upon those excluded from the room; while those who are rule-takers can have maximum knowledge of how rules are made, whose interests are promoted, and whose rights protected. Each institution needs to make all documentation and data publicly available at the earliest possible stage, as well as providing all information necessary to explain their functioning and put stakeholders in touch with their representatives. For international tax rule-makers, we also consider the transparency of the policies the institutions promote: the current “system” favors secrecy so that the privileged or deceitful can hide and not pay their fair share for the common good.

- **Accountability**: Each rule-setting organization must be fully accountable to member and non-member governments and to citizens and civil society, in line with its mandate, constitution and internal rules, as well as objective best practices for governance and management. All segments of the institution need to exercise responsibly the authority granted to them as limited by their charters, and not to exceed it through the exercise of raw power. This requires designing, monitoring and implementing measurable accountability frameworks; having open and merit-based selection processes for leaders and senior management; and regularly reviewing the functioning and achievements of their governance structures and meetings in holding management to account.

- **Inclusiveness**: By rights all who are impacted by rules should have a voice in how they are made, evaluated, and amended. However, in a world of
billions of citizens, we must accept representative democracy. New Rules supports constituency models which make governance inclusive yet small enough to get work done. The key to an equitable constituency model is a sound, objective basis on which voice and votes are allocated. The powerful will always be represented; but the real challenge is how well each institution ensures the presence and voice of the less powerful and those in need. The representation of non-state or non-governmental interests is also vital: again, while the “for profit sector” will have resources to make its views known, the key concern should be how well each institution listens to the poor and their representatives, and the silent imperatives of the global commons.

- **Responsibility**: The external counterpart to Accountability is Responsibility. Each institution needs to ensure that its actions result in a stronger financial system that promotes more just and economically sustainable global development, especially for people in low income countries, without harm to the global commons. Responsibility requires that institutions assess *ex ante* for themselves whether their actions and recommendations are sure to have this positive impact; conducting independent *ex post* evaluations and impact assessments; and operating formal and independent complaint and anti-corruption mechanisms, with protections for complainants, and compensation for those harmed by any institutional action or inaction. It also requires that each institution learn from these assessments and change its behavior.

These four criteria are essential for good governance of any institution, especially when its actions and inactions significantly impact every country. Each governance section of this report analyses governance performance in detail, and uses a “Governance Scorecard” (available at the end of this report) to provide a summary assessment scale for each criterion, from “Poor” (1) to “Excellent” (4).

**STRENGTHENING OUR ASSESSMENT OF IMPACT**

The center of attention this year has been on improving our methodology for assessing IMPACT. We have worked closely with a wide range of independent analysts and staff from the institutions themselves, who reached a consensus that the key criteria should be how these institutions affect poverty and inequality, based on the prominence of these issues in the post-2015 development framework and their prominence in all discussions (inclusive development is the theme of the Bretton Woods Institutions (BWI) Annual Meetings at which this report is launched). Global finance has a huge impact on the lives of the poorest people, and through them on the sustainability of growth as the institutions themselves have increasingly realized.

This becomes evident from examining the mandates of the institutions and their most recent statements of purpose. For each it has been relatively easy to identify five clear ways in which they should be combating poverty and inequality, though sometimes less easy to identify what they did to accomplish those objectives.

The G20 heads of state have defined their task as to ensure “balanced, sustained, and inclusive growth”. To achieve this goal, the identified priorities of the G20 should be:

1. To address Global Tax Reform beginning with base erosion and profit shifting (BEPS), automatic exchange of information and public identification of beneficial owners of wealth;
2. To shift its focus toward Inclusive Growth, addressing inequality globally and within G20 countries;
3. To refocus its Development Working Group agenda around combating poverty and inequality, to make it more consistent with the post-2015 development framework;
4. To promote Decent Work/Labor Rights and higher wages, and minimum social protection floors; and
5. To mobilize long-term (especially concessional and official) development financing, including traditional official development assistance (ODA) and South South cooperation, innovative financing, and reducing the costs of remittances.

The Financial Stability Board is mandated by the G20 to promote and ensure global financial stability – as the Deputy Secretary General has said “for what stability achieves” in terms of promoting sustainable growth. Its priorities to achieve this goal were:

1. To end Too Big to Fail financial and insurance institutions;
2. To design and implement cross-border financial resolution regulations (to resolve bankruptcies);
3. To make transparent and regulate over-the-counter derivatives;
4. To bring shadow banking into the sunlight of transparency, regulation and stability; and
5. To organize the new Global Legal Entity Identification System (GLEIS) so every financial entity is identified and every financial transaction carries the “names and phone numbers” of all participants.

The International Monetary Fund works to ensure sustainable growth and the Managing Director has defined combating inequality as a core part of their mandate. It should be achieving these ends by promoting:

1. Inclusive growth and decent and well-remunerated employment;
2. More progressive taxes and more efficient tax collection, and combating tax evasion/avoidance;
3. Anti-inequality spending, especially on education, health, social protection and water, sanitation and hygiene (WASH);
4. Domestic and international financial systems that promote greater equality; and
5. Lending adequate (low-conditionality) funds to countries to overcome balance of payments problems.

The World Bank has rearticulated its mission as ridding the world of extreme poverty and promoting greater inclusion for the bottom 40 per cent by 2030. It should be achieving this by:

1. Defining strong targets for dramatically reducing inequality;
2. Redefining its policy assessment and policy-based lending to ensure they fight poverty and inequality; supporting universal free education and health services, and social protection floors;
3. Supporting the private sector in ways which reduce poverty and combat inequality;
4. Providing large amounts of loans and grants to countries requiring long-term development finance; and
5. The development of an overall framework to measure it own impact.

The OECD has long coordinated and advised on its member-states’ cross border tax policies. In 2013, the G8 and G20 expanded its mission to reduce the loss of income to all governments from tax avoidance and evasion through “Base Erosion and Profit Shifting”. We review the OECD’s achievements in:

1. Monitoring, measuring and reducing illicit financial flows and tax evasion;
2. Reducing major forms of tax avoidance;
3. Ending “tax wars” or “tax competition,” which results in a race to the bottom for national revenue;
4. Encouraging more efficient national tax administrations; and
5. Promoting progressivity in national tax systems.

Authors assessed each of these functions in terms of their success in reducing poverty and inequality. The four point scale rated: 1-increased inequality; 2-no movement or inability to measure progress; 3-some positive movement; and 4-excellent progress. The total points were then averaged for a score for each institution.

A broad framework was designed to guide assessment of impact (see end of report).

The authors and the editors acknowledge that, in spite of improvements, the methodology used in this Report is still imperfect. It relies on publicly available data, and much more could be done to increase what is publicly available. A diverse panel of experts contributed most generously to thinking about results and methodologies. We incorporated this advice into our assessment and our overall findings are below. New Rules once again welcomes all feedback, especially whatever will improve the data sources and the methodologies used to assess both the Governance and the Impact of these institutions. As public bodies designed to promote the public good of a financial system at the service of reduced inequality and poverty in low income countries—with staff and facilities paid for by public taxes—we welcome the collaboration of the staff, management and leadership of the institutions, as well as that of the informed, articulate, and even boisterous public.
Governance Remains Inadequate

Overall, the Governance Gap remains at 50 per cent. Of greatest concern is that all global financial-rule making institutions score worst in Responsibility.

Average Governance Score: 1.9 (out of 4)
Assessed as Poor, just below Moderate.

Governance Gap is based on the Total Aggregate Governance Score: 9.5 (out of 20)
Limited to No Impact

on reducing inequality or positively impacting the real economy, especially in low-income countries.

Average Impact Score: 2.1 (out of 4)
Assessed as None or Limited Impact, with slight positive impact
Some governance findings are similar across all institutions, and lead us to several principal, but generic recommendations:

- **Transparency** must encompass all discussions, which should ideally be transcribed and broadcasted live; websites must be easily accessible, with excellent search engines, in all UN languages; all meetings between institution staff, management and officers must be publicly documented, and all contact with parties having material interest in decisions must be documented including the content of discussion.

- **Inclusion** needs to be assured by establishing constituency systems in G20 and FSB; more representative economic and population formulas for voting rights in the BWIs (building on rapid implementation of the IMF reforms agreed in 2010); and greater diversity of staff, notably from non-OECD economies.

- **Accountability** requires selection of leadership and staff based on objective merit; separation of functions of CEO and Board Chair; biennial evaluations of the performance of governing bodies and top managers; and an accountability framework to which the institution can be held responsible.

- **Responsibility** dictates that all international financial institutions have a complaint mechanism to receive complaints from affected people; routine ex ante analysis of potential impact of measures on poverty and inequality; as well as regular independent evaluations of their achievements.
Impact

Impact Recommendations

- The G20 should monitor and combat inequality, improve employment conditions and raise minimum wages to bring full-time workers out of poverty, make taxes more progressive and raise social protection floors, focus its development framework on fighting inequality, and increase concessional funding flows.

- The FSB should ask the G20 to strengthen its institutional mandate, staffing and capacity, to allow it to galvanize agreement and enforce rapid progress on a global “regulatory floor” (minimum standard) which safeguards public interests and enhances equality of access to financing. Early priorities should be cross-border crisis resolution, stopping institutions from being “too big to fail”, and reining in shadow banking.

- The IMF should monitor poverty and inequality in its reports to G20, and set targets for reducing them in all country programs, by recommending increases in decent employment and wage levels, more progressive taxes and measures to combat evasion, much higher anti-inequality spending, and pro-poor financial systems. It should also sharply increase its lending capacity, especially with low-conditionality.

- The World Bank must set an ambitious target to increase the share of the bottom 40 per cent in national wealth (to match the top 10 per cent), and ensure this is implemented by: focusing its policy assessments and conditions on reducing poverty and inequality; committing to universal social protection floors; and making sure IFC finance is subject to an anti–poverty/inequality results framework as part of “One Bank”.

- Finally, the OECD could continue to exchange information on best practices among its members, and promote their involvement in improving tax policy and administration through their aid programs. However, a World Tax Authority would be much better placed to take a comprehensive overview of global tax policy, dramatically reinforce the fight against illicit flows and tax evasion/avoidance, combat tax wars, revise tax treaties and promote progressive tax policies to fight inequality.
In 1999, following the Asian financial crisis, the Group of 20 (G20) Finance Ministers and Central Bank Governors began holding annual meetings to encourage policy coordination between advanced and emerging economies. This arrangement continued until September 2008, when the Lehman Brothers financial firm collapsed, leading to the largest bankruptcy filing in US history. Iceland’s banking system subsequently collapsed, and the foreign exchange market froze. It became clear that the global financial sector was in danger of a total meltdown.¹

At the urging of French President Nicolas Sarkozy and UK Prime Minister Gordon Brown, US President George W. Bush convened the first G20 leaders’ summit in Washington, DC on November 15, 2008. The public rationale for elevating the finance ministers’ and the central bank governors’ forum to a leaders’ summit was that addressing the 2008-2009 global financial crisis required quick, decisive action.² In 2009, at the third G20 summit in Pittsburgh, leaders declared the G20 to be “the premier forum” for international economic cooperation.³ Today, the G20 represents 88 per cent of global GDP, two-thirds of the world’s population, and 60 per cent of the world’s poor people.⁴

Unlike the other global financial institutions evaluated in this report, the G20 has no central governing body or secretariat, no formal rules, and no permanent staff. Each year, leadership of the G20 falls to the host country government, which assumes the rotating presidency of the body. The G20 President sets the agenda and invites guest representatives from regional organizations and other non-G20 countries. The host country convenes working and expert groups, and decides when Sherpas and ministers (finance, labor, agriculture, etc.) will meet. (Sherpas are the personal representatives of heads of state tasked with coordinating the preparatory work.) The host country also decides how the G20 will relate to non-governmental stakeholders from civil society, labor, business, and other interests. The G20 recently established a Troika consisting of the current, previous, and succeeding host governments to better align summit agendas for consecutive years. However, there has been little observable reduction in the host government’s dominance over decision making.

While the G20 is often described as the world’s twenty largest economies, this is not actually the case. Spain, a “permanent guest” of the G20, has a larger economy than eight other G20 countries but is not a member of the group. Conversely, Argentina and South Africa are both members of the G20, even though they fall below the top twenty, at 21st and 33rd, respectively.

The G20 countries in Table 1 are listed by size of gross domestic product (GDP).⁵ The G8 countries are in bold and the BRICS (Brazil, Russia, India, China and South Africa) in italics. The GDP ranking of the bottom two countries is listed after the country.
At the 2010 Seoul summit, leaders decided to invite no more than five non-member countries to future summits. They further stipulated that at least two of the countries invited should be African.⁶ The G20 President typically invites countries that serve as the chairs of regional organizations, such as: the African Union (AU), the New Partnership for Africa’s Development (NEPAD), the Association of South East Asian Nations (ASEAN), the Global Governance Group (3G), Asian-Pacific Economic Cooperation (APEC), the Commonwealth of Independent States (CIS), and the Community of Latin American and Caribbean States (CELAC).

This form of “guest country” outreach has limited impact, however, as only three regional groups (AU, NEPAD, and ASEAN) are consistently represented at each summit, and the lead country representing each region changes yearly. The invited regional representatives are not full members of the G20, and as such have limited influence. In past years, guest countries have included Benin, Brunei, Cambodia, Chile, Colombia, Equatorial Guinea, Ethiopia, Kazakhstan, Malawi, the Netherlands, Spain, Switzerland, Thailand, the United Arab Emirates, and Vietnam.

While the G20 is clearly more representative than the G8, there is nevertheless significant criticism directed towards the G20 by NGOs, academics, and think tanks for its lack of inclusiveness. When the G20 was established in 1999 at the finance ministers’ and central bank governors’ level, members were selected not on a basis of shared, transparent, objective, or measurable criteria, but by their ability to “contribute to global economic and financial stability.”⁷ Following the onset of the 2008-2009 global financial crisis, the rush to upgrade the G20 to a summit of national leaders created significant governance problems. Efficiency was prioritized over legitimacy, and while this was an expedient decision at the time, the continued lack of a resolution on the issues of governance and representation can no longer be excused.⁸

**Recommendations:** To increase its inclusiveness, the G20 should:

- Define clear parameters for determining membership. The selection of members and the criteria through which they are selected should be transparent, and G20 member countries should be reassessed every five years so that G20 membership accurately reflects the world’s largest economies.
- Encourage greater engagement with external stakeholders. This includes using multilateral channels, such as the United Nations, to engage non-member countries.
- Establish formal channels through which external views, especially those of low income countries, can be taken into consideration and incorporated into decision making.
- Conduct regular public consultations with interested parties and share the consultation agenda in advance.
- Create more standardized criteria for determining which non-member countries are invited to each summit, taking into account important factors such as geographical representation.

The G20 must also take steps to improve transparency. One problem is the lack of public access to basic information and documents. Because the G20 lacks a secretariat, there is no central source that gathers and releases information and documentation related to the G20’s activities. Each year, the G20 host country maintains a website to serve as a hub of information for the summit. Unfortunately, the websites from previous summits are often closed shortly after the change in leadership.

Public disclosure of information regarding decision-making is limited. While the G20 will release

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**Table 1:** These rankings are derived from the most recent figures from the World Bank’s World Development Indicators database and reflect GDP in 2013.
declarations, communiques, action plans, and other official documents, the materials used to prepare these documents and early drafts are typically confidential and not accessible to the public.⁹ In instances where this information is disclosed, it is often neither timely nor comprehensive.

The G20 process is divided into the Finance Ministers’ Track and the Sherpas’ Track. The focus of the two tracks changes depending on the host country and since 2009 have included a range of issues:

Finance Ministers’ Track: Framework for Strong, Sustainable and Balanced Growth, Financial Reform, Global Imbalances, Infrastructure Investment, Trade (under both Finance and Employment Ministers)


Issues are handled by working or expert groups, or are discussed in ministerial meetings; however, there is no requirement to share materials or to issue reports describing or justifying these groups’ decisions. Each G20 government can release materials, statements, and communiques from the Sherpa, ministerial, and working group meetings, but they rarely choose to do so.¹⁰ It is left to the host country to provide a summary of these key decision-making meetings, which means that G20 transparency during any given year primarily depends on the host government. In the case of Russia in 2013, the releases were little more than announcements the groups had met, with few details on what was decided. This behavior, unfortunately, is fairly typical of host nations.

No host government has released a list of the country representatives attending the range of preparatory meetings, leaving civil society representatives to petition for the release of this information. In many countries, it is difficult or impossible to obtain specific information on representatives and decisions in the preparatory meetings.

Recommendations: To increase transparency, the G20 should:

• Ensure that information regarding decision-making is available to all external stakeholders. Establishing websites for G20 task forces and working groups could help achieve this end.
• Establish a formal channel through which information can be requested.

The G20 also needs to improve accountability around the implementation and monitoring of its decisions. Because their commitments are not legally binding and there are no enforcement mechanisms, G20 countries are not held properly accountable for failing to deliver on their commitments. As a consequence, there is often “a gap between rhetoric and delivery.”¹¹

Each G20 government is primarily accountable to itself, with some governments also accountable to their citizens. There are occasions when the G20 governments commit to the implementation of a policy or the submission of a report by a specific deadline. However, in many instances, the G20 has made commitments in a way that limits their accountability.

For example, most of its “commitments” have no firm deadlines and no benchmarks of progress. Paragraph 10 in the Los Cabos Leaders Declaration (2012), for instance, states that G20 countries “will implement all our commitments in a timely manner and rigorously monitor their implementation,” which provides no specifics for which they may be held accountable.

On the issue of green growth and sustainable development, paragraph 73 of the 2012 Leaders Declaration states that G20 countries “will self-report again in 2013, on a voluntary basis…” Self-reporting on a voluntary basis greatly reduces the availability of reliable hard data with which to judge progress.

Nevertheless, the G20 has made some progress toward greater accountability. The Anti-Corruption Working Group has released annual progress reports since 2010 and the Development Working Group conducted its first accountability assessment in 2013. Unfortunately, however, the G20 has not conducted assessments of progress in other areas. The G20 should create a comprehensive accountability mechanism that encompasses all aspects of its work.
Recommendations: To become more accountable, the G20 needs to:

- Establish firm deadlines for all of its commitments.
- Strengthen the Mutual Assessment Plan (MAP) and expand the Accountability Assessment Framework to assess progress in meeting all of the G20’s commitments.
- Adopt a standardized process for host countries to follow during their respective presidencies that ensures greater accountability of host countries and greater harmonization of year-to-year priorities.
- Create mechanisms to ensure that ex post assessments are being conducted regularly and that the G20 uses these assessments to change its behavior.

Under the current process, responsibility is difficult to assign due to two primary factors: the lack of a central organization or secretariat; and the reliance upon other financial institutions to implement (or not) G20 decisions. At the 2013 St. Petersburg Summit, for example, the country leaders delegated over 30 tasks to other institutions. The table below lists examples of assignments from the 2013 G20 Communiqué.¹²

If the G20 wants to ensure that its policies and decisions result in a stronger and more stable global financial system which promotes equitable and sustainable global development, it needs to establish monitoring and evaluation procedures to assess the impact and effectiveness of its actions and recommendations. The G20 should conduct ex ante assessments to determine whether its actions will positively impact other countries, particularly low income countries. The G20 should also conduct ex post evaluations and assessments to determine the impacts of its actions and recommendations. These assessments should take into account economic, social, and environmental outcomes. Furthermore, the G20 should use these assessments to change its behavior, when necessary.

While the G20 has conducted ex ante and ex post assessments of some of its actions, it does not conduct such assessments for all of them. The G20 should take steps to adopt a standardized procedure to conduct assessments and evaluate its impacts on all actions. Increasing responsibility also entails the creation of a formalized external complaint mechanism through which grievances from non-G20 governments and civil society may be heard.

Recommendations: To increase its responsibility, the G20 should:

- Create standardized procedures for conducting regular ex ante and ex post assessments on all G20 actions and recommendations.
- Create mechanisms to ensure that ex ante assessments are being conducted regularly and that the G20 uses these assessments to change its behavior.
- Create a formal external complaint mechanism through which grievances may be heard.

<table>
<thead>
<tr>
<th>Organizations</th>
<th>Tasks</th>
</tr>
</thead>
<tbody>
<tr>
<td>International Labour Organization (ILO)</td>
<td>Partner with the G20 Task Force on Employment to consider how G20 countries might contribute to safer workplaces. (Para. 34)</td>
</tr>
<tr>
<td>FSB</td>
<td>Monitor financial regulatory reforms impact on long-term investment financing. (Para. 38)</td>
</tr>
<tr>
<td>Global Forum</td>
<td>Establish a mechanism to monitor and review the implementation of the new global standard on automatic exchange of information. (Para 51)</td>
</tr>
<tr>
<td>OECD, Global Forum</td>
<td>Work with the Development Working Group to show how developing countries can overcome obstacles with the new automatic exchange of information standard. (Para 51)</td>
</tr>
<tr>
<td>IMF, World Bank</td>
<td>Assist low-income countries to develop prudent medium-term debt management strategies and enhance their debt management capacity. (Para. 57)</td>
</tr>
<tr>
<td>IMF</td>
<td>Develop proposals on how to incorporate global liquidity more broadly into the IMF’s surveillance work. (Para. 58)</td>
</tr>
<tr>
<td>FSB</td>
<td>Monitor, analyze and report on the effects of evolving regulator reforms on emerging markets and developing countries. (Para. 65)</td>
</tr>
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</table>
# G20 Governance Assessment

<table>
<thead>
<tr>
<th>Governance Element</th>
<th>2013</th>
<th>2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>Transparency</td>
<td>1.5</td>
<td>2</td>
</tr>
<tr>
<td>Accountability</td>
<td>1.5</td>
<td>2</td>
</tr>
<tr>
<td>Inclusiveness</td>
<td>1.5</td>
<td>1.5</td>
</tr>
<tr>
<td>Responsibility</td>
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<td>1.5</td>
</tr>
<tr>
<td>Total Score</td>
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<td>7</td>
</tr>
<tr>
<td>Average Score</td>
<td>1.5</td>
<td>1.8</td>
</tr>
</tbody>
</table>

**Governance Gap**

- Transparency: 2
- Accountability: 2
- Inclusiveness: 1.5
- Responsibility: 1.5
- Total Score: 7
- Average Score: 1.8

57%

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3. G20 Leaders Statement: The Pittsburgh Summit, 24 September 2009, paragraph 19. [https://www.g20.org/sites/default/files/g20_resources/library/Pittsburgh_Declaration_0.pdf](https://www.g20.org/sites/default/files/g20_resources/library/Pittsburgh_Declaration_0.pdf)
5. These rankings are derived from the most recent figures in the World Bank’s World Development Indicators database and reflect GDP in 2013. [http://databank.worldbank.org/data/download/GDP.pdf](http://databank.worldbank.org/data/download/GDP.pdf)
10. Some countries have been quite open in terms of sharing information. The U.S. anti-corruption team, consisting of staff from the White House, Treasury, Justice, and State, has been very open with civil society, sharing information and encouraging feedback.
For 10 years, the G20 was a relatively obscure meeting of finance ministers. In 2008 the global economic crisis thrust this Group of 20 into the limelight, upgraded it to a summit-level meeting of world leaders, and led to it being cast as the world’s premier economic forum.

The G20’s mandate is to promote ‘open and constructive discussion between industrial and emerging-market countries on key issues related to global economic stability’. Chairing of the G20 rotates on an annual basis. It is an informal forum – without a home or a secretariat – but with G20 countries representing around 90 per cent of global gross national product, 80 per cent of world trade (including intra-EU trade) as well as two-thirds of the world population, its influence on the world economy is unrivalled.

This influence goes hand in hand with the ability to make decisions that affect the poorest countries and have an impact on development, as most of the G20’s decisions have so-called ‘spill-over effects’ that can be positive or negative for non-members. In 2010 the G20 committed to a development agenda with the Seoul Development Consensus as a foundation. However, the G20’s lack of institutional memory means that many of its commitments are not followed through. Even where the G20 has published accountability reports (such as by the Development Working Group (DWG) in 2013), they do not go so far as to look at the real-world impact of the G20’s policies.

The G20 are global rule-setters, so they should measure and be accountable for the impact of their economic policy decisions (nationally, as a group, and in other institutions). This would be arguably more telling in terms of whether they will be a force for good in development in the coming 20 years.

On tax for instance, they should be committed to measuring the impact of profit shifting on their economies and on developing countries, and then measuring the impact of their policies in reversing this trend. That would be meaningful.

Responding to public pressure in several G20 countries, especially following tax scandals involving major multinational corporations such as Apple and Starbucks, in 2012 the G20 mandated the OECD Secretariat and its Committee of Fiscal Affairs (CAF) to initiate a set of reforms of the international tax system. In February 2013, the OECD published a report, addressing Base Erosion and Profit Shifting (BEPS). This report gave a damning analysis of the deficiencies in today’s global tax system, including the loopholes and secrecy that allow profit-shifting, and the failure of international rules to ensure that companies pay taxes where real economic activity takes place, and value is created. The G20 played a role in demonstrating the scale of the problem, and the need for international tax rules to be urgently reformed.

Building on this, in July 2013, the OECD launched its Action Plan on Base Erosion and Profit Shifting. The report identifies 15 actions to tackle BEPS, and assigns each action to concrete working parties and task forces, and sets deadlines for the delivery of the expected outputs.

The G20 Summit in September 2013 endorsed the OECD action plan and called on the OECD to produce guidelines in the coming years, and have taken a number of specific steps since initiating the process that have helped to progress this agenda. However they have not done...
enough to recognize the urgent need for developing countries to participate and benefit from tax reform.

The G20 have for instance agreed a new global standard for the automatic exchange of tax information. However, to date they have made no commitment to allow developing countries to benefit from this arrangement until they are able to fully reciprocate, indicating a lack of realism and urgency in ensuring tax reforms are supporting the countries that most desperately need to recoup lost revenue.

Developing countries have been consulted on the BEPS process, but the G20 and OECD have failed to give them the opportunity to participate fully in the reform process on an equal footing. The process has also been prone to influence by vested interests. Almost 87 per cent of the submissions to the OECD’s 2013 consultation on draft rules came from the business sector who were almost all opposed to country-by-country reporting.

**Recommendation:** The G20 must do more to show that they are serious about the urgent need for tax reform that matches the scale of the challenge identified by the OECD, and to ensure developing countries have an equal say and opportunity to benefit from reforms. The G20 will remain under public and media scrutiny to see through this agenda.

**Inclusive Growth**  
Score 1.5

After the G20 was established as a summit-level body in 2008, it set itself an ambitious agenda of promoting “shared”, “balanced” and in 2013, “inclusive” growth. Whilst never going as far as committing to economic policies that reduce economic inequality, the explosion of inequality in the last 30 years, along with the financial and economic crises, has certainly pushed the G20 to seek to get ahead of debates about a fairer global economy.

Economic inequality is a barrier to poverty reduction, and with G20 countries themselves being home to more than half of the world’s people living in poverty, this should be of immediate concern. Projections by Oxfam and Brookings have indicated that reducing inequality could lift millions of people out of extreme poverty in the G20’s emerging economies for instance.

Despite this, the G20’s actions have failed to match its ambitions or keep up with the demand for action, and most recently, the 2014 Australian Presidency has to date stepped back from the 2013 Russian Presidency’s focus on “inclusive” growth. Even “at home” this agenda is failing, with income inequality increasing in most G20 countries.

If the G20 is serious about tackling inequality as part of a fairer economic agenda that is in the interests of the majority – both in and beyond G20 nations – they must make more specific commitments. A promising start would be a collective commitment to measuring the benefit of national economic and development policy to the poorest 40 per cent, and to report publicly on this. The G20 are also well positioned to ensure that major institutions like the IMF and World Bank do the same, for instance getting the IMF to include Gini data in Article IV consultations.

The G20’s record on tackling gender inequality as part of their growth is equally questionable. Only one high-income country in the G20 – South Korea – has achieved greater income equality alongside economic growth since 1990. However, this growth is built on gender inequality in wages and discriminatory practices: South Korea ranks worst among OECD countries on the gender wage gap. Evidence also points to the role that economic policies which aim to close the gap between women and men can have on growth. For instance if women’s paid employment rates were the same as men’s, the US’s GDP would increase by 9 percent, and growth could increase by 20 percent across fifteen major developing countries by 2030.

**Recommendation:** The G20 should also support a post 2015 goal to reduce economic inequality by 2030, and commit to reducing income and wealth inequality in all countries.

**Development Goals**  
Score 2

Average global income per person has doubled over the last forty years. The proportion of the world’s population living in poverty has fallen significantly over the same period, but the absolute number remains high and the gap between the rich and the poor is still growing. The poorest billion people in the world have increased their share of world income since 1990, but from a tiny 0.2 per cent to just short of 1 per cent. And despite some progress, G20 countries are still failing the very
poorest people; in 2009, more than half of people living on less than US$1.25 per day were in G20 countries.¹³

Through the 2010 Seoul Development Consensus for Shared Growth, G20 countries raised hopes that they would deliver reductions in poverty and inequality for all, arguing that ‘for prosperity to be sustained it must be shared’. However the G20 needs to match action to rhetoric, and thus far their development agenda has been stymied by a lack of political will and a failure of multilateralism.

The DWG has largely been separated from the economic and political power of the Finance and Economics Ministries of G20 countries, meaning there has been a failure to connect and align the highly charged debates on global tax rules and economic policy to a development objective. The lack of momentum behind domestic resource mobilization is a case in point; significant progress cannot be made on this agenda without political commitment from Finance Ministries yet the debate has been largely confined to Development Ministries.

**Recommendation:** Rather than measuring the delivery of activities, the G20 must move to measuring and being publicly accountable for the positive and negative impact on development, including the spill-over of their decisions on non-G20 countries. This is far from the reality today.

The G20 has commissioned work on innovative financing for development, but has largely failed to follow through on the recommendations of the reports it has received. The G20 is to be commended for an initiative to reduce the costs of remittance flows within its existing strand of work on Financial Inclusion. However the real-world impact of this work is currently unclear.

The G20 has not picked up the remit of aid, but their membership does of course include G8 countries that collectively made a significant aid commitment in 2005 that was not delivered. The G8’s Deauville Accountability Report produced in 2011 claimed to have delivered $49 of their $50 billion promise, when in fact the OECD showed that the accurate figure – with inflation adjustment – was just $31 billion.¹⁵ Whilst this is not a G20 failure, it is a failure of some G20 nations to live up to their aid and development finance commitments.

**Recommendation:** All G20 nations should comply with their commitments to aid and development finance.

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Whether looking at G20 members, or the entire globe, or just at the poorest countries, unemployment continues at elevated rates. Youth unemployment is strikingly huge: on a global level 13.1 per cent are unemployed but in parts of the Middle East and North Africa it reaches 40 per cent. Overall participation in the global labor market has declined as people drop out or revert to the informal sector. Even where unemployed has improved, wages have stagnated or even declined.¹⁴ This reality challenges the strength of the G20 commitment to “strong, sustained and inclusive growth.”

**Recommendation:** The G20 should recommit its energies to strong, sustained and inclusive growth—with equity by providing and raising minimum wages that bring full time workers out of poverty, while raising the social protection floor for all.
G20 Impact Assessment

<table>
<thead>
<tr>
<th>Impact Criteria</th>
<th>2014</th>
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<tbody>
<tr>
<td>Tax Reform</td>
<td>2.5</td>
</tr>
<tr>
<td>Inclusive Growth</td>
<td>1.5</td>
</tr>
<tr>
<td>Development Goals</td>
<td>2</td>
</tr>
<tr>
<td>Labor</td>
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<tr>
<td>Development Financing</td>
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<tr>
<td>Average Score</td>
<td>1.9</td>
</tr>
</tbody>
</table>

¹ This chapter draws on several recently published Oxfam papers.
⁸ Ibid.
¹⁰ UN Women. Facts and Figures: Economic Empowerment. Available at http://www.unwomen.org
¹¹ Based on global GDP per capita in constant prices; World Bank Development Indicators Database (1970–2010).
¹³ Sumner (2010).
The Financial Stability Board (FSB) was created at the G20 Leaders Summit in April 2009, replacing its predecessor, the Financial Stability Forum (FSF). Whereas the FSF was primarily tasked with promoting compliance with existing international financial standards after the Asian financial crisis, the FSB was tasked with coordinating the creation and implementation of new financial standards in concert with sector-specific standard setting bodies. The task of the FSB has been immense.

The FSB burst on to the international financial regulatory scene with lofty promises as US Treasury Secretary Tim Geithner stated that the FSB would become “a fourth pillar” in global economic governance alongside the International Monetary Fund (IMF), World Bank (WB), and World Trade Organization (WTO). Geithner’s statement brought with it the promise of a renewed commitment to strengthening the international financial architecture and the resiliency of the global financial system. As the post-crisis reform process has unwound, the promise of meaningful and coordinated regulatory reform has waned and the same set of governance and regulatory challenges of previous crises remain.

In order to strengthen the participation of non-members, the FSB has established six regional consultative groups (RCGs) in the following regions: Americas, Asia, Commonwealth of Independent States, Europe, Middle East and North Africa, and Sub-Saharan Africa. The FSB’s RCGs have a relatively broad membership base with a large group of FSB members and non-members occupying a seat on each of the respective RCGs. The creation of the RCGs is a welcome addition to the exclusive regulatory club.

RCGs provide two important functions that are critical to the international regulatory regime. First, the aim of the RCGs is to create an effective mechanism that allows non-member countries to discuss the regulatory issues and systemic risks that their jurisdictions face.
Second, RCGs allow non-members to communicate their preferences on regulatory issues and their impact on local financial markets to the FSB and its members. A prevailing problem in the governance of global financial markets is that international financial standards have historically been created by an exclusive group of regulators from developed financial centers. Financial standards are then applied to local market contexts and they often fail to reflect the real differences between national financial markets, which ultimately hamper their effectiveness. Additionally, the regulatory decisions of developed financial centers can directly impact least developed, developing and emerging markets. For instance, national economies that are heavily reliant on commodity exports or imports are directly affected by derivatives market regulation through its impact on the global market price for certain commodities.

So, to what extent have RCGs been effective? The simple answer is that it is unclear. Since there is no public record of who attends each meeting, it is difficult to ascertain the extent to which non-member regulators find these meetings useful. Recent publications produced by Asian and Americans RCGs on a number of regulatory issue areas have provided a more in-depth discussion of salient policy issues. These publications have been promising as they indicate that there is a stronger degree of coordination and cooperation between RCGs. However, the impact that these discussions have on FSB decision-making processes is unclear. One of two co-chairs (one FSB member and one non-member) from each RCG report to the FSB plenary. However, this responsibility is not explicitly delegated to non-member co-chairs, which means it is likely that the FSB member co-chair reports on behalf of the RCG. Nonetheless, there is no formal channel for RCGs to ensure their concerns or recommendations will be considered by the FSB.

**Recommendation:** The FSB should strengthen the communication mechanisms between the FSB’s main decision-making bodies and RCGs. To do this, the FSB must develop a clear and transparent framework that outlines the constitution of RCGs and the way in which RCGs feed into the FSB’s standard setting and policy process. Another less obvious challenge is that some RCG members lack sufficient resources to attend international regulatory committee meetings. This can hamper some countries’ participation in standard setting and, ultimately, weakens the international regulatory regime in two ways: first by reducing the political buy-in of non-member countries; and second, through the creation of standards that are not best-fit for local financial, judicial and legislative contexts.

Relative to its predecessor, the FSB has improved on its inclusiveness by expanding its membership and through the creation of RCGs, which remain a weak mechanism for influencing policy outcomes. Strengthening these mechanisms would make a significant improvement to the inclusiveness of the FSB and the effectiveness of financial governance.

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**Transparency**

The FSB is one of the more opaque international economic governance institutions. The opacity of the FSB’s policy-making process is a double-edged sword. It has the potential to protect financial regulators from the pressure of private financial market actors. At the same time it has the potential to make the FSB less accountable to the wider public.

The FSB does publish a comprehensive list of consultation papers, discussion papers, financial standards, and thematic and peer reviews of the implementation of financial standards; it should be presented in an accessible format on its website. The FSB has also introduced regular consultative periods on initial drafts of financial standards to enable public comment, which are published at the end of the consultative period, unless submitters specifically request otherwise. This has significantly improved the transparency of the financial standard setting process. The FSB’s outputs are relatively transparent but how the FSB makes its decisions and conducts internal work is not.

Little information is available to the public regarding meetings of the FSB Plenary and the RCGs, providing neither meeting schedules beforehand nor information on who attended the meetings. A press release after the fact provides only a broad picture of the agenda discussed at each meeting. Meetings of the FSB’s key committees, within which the bulk of the FSB’s key decisions are made before being signed off by the Plenary, are similarly confidential.

International financial regulatory organizations have traditionally granted private financial market actors privileged access to the standard setting and policy-making process. Standard setting bodies have traditionally regarded financial firms as the primary stakeholders in standard setting processes as the regulatory burden falls largely on these actors and because financial firms
implement these financial standards through their internal processes. In truth, financial standards have a far broader array of stakeholders because financial markets and the allocation decisions that they impact affect the everyday lives of households, farmers, and the broader business community. Unfortunately, unlike other issue areas in the economy, the connection between finance and economic outcomes has been harder to conceptualize (see FSB impact section). This has meant that at both the domestic and international levels the balance of power between the lobbying power of private financial firms and public civil society heavily favors financial firms who have a direct material interest in the outcomes of international standards setting bodies. The FSB’s policy-making processes need to be sufficiently transparent so the public can be assured that parties with direct material interests (private financial firms) and other interested parties (e.g., academics and civil society) have comparable access to the FSB’s policy-making process and that the policy input from private financial actors is clearly disclosed. The FSB has made progressive steps towards the greater inclusion of civil society actors. Over the past year, the FSB has engaged with civil society on a number of occasions around the world including hosting FSB Watch – a coalition of public interest groups – in June 2014.

Recommendation: The G20 should update the FSB’s Charter to require the FSB to publicly disclose: 1) which actors or groups, both financial and civil society, and which financial regulators were consulted or otherwise participated in the policy-making process; and, 2) a list of FSB Working Groups that are responsible for financial standards. This list may be published after the FSB has released a financial standard rather than during the policy-making process to protect the integrity of the standard setting process.

ACCOUNTABILITY

Accountability Score 2

ACCOUNTABILITY

mandate and approves and/or guides the regulatory work program of the institution. The FSB reports annually to the G20 Summit on the progress it has made on assigned tasks. The FSB has also developed a number of internal and relatively informal decision-making procedures that ensure that the FSB’s decisions and outcomes reflect the interests and preferences of its members. The Secretariat is led by a Secretary General who serves a 5-year term and is answerable to the Chairman of the FSB. The Chairman of the FSB is appointed by the Plenary. The FSB’s main decision-making bodies are empowered to appoint their own chair and decision-making procedures have been described as a “rough approximation between consensus and general agreement.” There are around 25 secretariat staff who are seconded to the FSB from national regulators and by international institutions such as the IMF. A few (around 6) are full time FSB staff. The powers of each decision-making body to endorse financial standards and agree to their release ensure that FSB staff is held accountable to the member states.

The FSB is held accountable to the G20 and its member states but not to the broader set of stakeholders that are impacted by its decisions. There are real and meaningful reasons why standard setting bodies, like the FSB, have chosen to maintain exclusive memberships and to make those institutions accountable to its members. However, it is also important to recognize that the decisions made by these institutions have an immense impact on a wide array of stakeholders and that mechanisms must be created to ensure that the FSB is held accountable for those impacts and how they can be addressed.

As the previous sections have discussed, to ensure that the FSB is made more accountable it is necessary that the organization be made more transparent and more inclusive. In order for interested parties and affected stakeholders to effectively respond to the policy preferences and financial standards created by the FSB and its associated institutions, these actors must have access to the information used to make these decisions. Doing so will enable interested parties to communicate their views, to effectively criticize the decisions made by the FSB, and to draw attention to the impact of the FSB’s decisions on the affected parties. Furthermore, affected stakeholders must have access points to the FSB policy-making process to ensure that their views can be heard and effectively communicated to FSB policy-makers. Doing so will ensure that regulators and decision makers have full access to the information necessary to make informed policy choices.

Recommendation: The FSB should establish an internal working group that establishes the FSB’s external relations policy with the aim of designing effective mechanisms to ensure the FSB effectively and adequately engages and cooperates with its stakeholders.

RESPONSIBILITY
Governance & Impact Report 2014

The international financial regulatory regime has been plagued with the issue of non-compliance and the challenges of implementation. The FSB and other financial standard setters are soft-law bodies, denoting that their members are not legally bound to implement financial standards in the same manner that members of other multilateral organizations such as the IMF, WB, and WTO are required to. The FSB and the international standard setting regime lack a strong set of institutional mechanisms to ensure compliance with international financial standards.

The review of the FSB charter reiterated that the G20 intends to maintain the FSB’s soft-law status by stating that turning the FSB into a multilateral treaty-based organization was “not an appropriate legal form at this juncture.” The FSB continues to rely on the “naming and shaming” of non-compliant countries who are overseen by the FSB’s peer-review process for G20 countries, and the IMF’s Report on the Observance of Standards and Codes (ROSC) and Financial Stability Assessment Program for all countries. The problem with this approach, as revealed by the events preceding the crisis, is that coordination of national financial regulatory frameworks and the commitment to the adoption of international financial standards remains reliant on domestic political processes. A 2011 IMF Review of the Standards and Codes Initiative concludes that the effectiveness of the ROSC in addressing critical gaps in domestic regulatory frameworks is highly dependent on countries exhibiting “strong ownership and internalization at all levels.” The same can be said for the implementation of G20 post-crisis reforms.

Throughout the post-crisis reform process, domestic politics have often overruled international consensus. The continued weakness of the international regulatory regime allows states to avoid responsibility for their non-compliance with international financial standards. Binding themselves to a hard law international regime would provide states with the opportunity to resist domestic political pressures and commit to the adoption of best practice standards, as well as ensuring a level playing field between domestic financial systems. A core concern of states is that international financial standards and associated review processes do not reflect the unique structure of domestic financial systems or legal traditions of each jurisdiction. These are valid concerns that should be addressed by the current international system. Doing so would make states more willing to accept a binding commitment to international financial standards. There remain a number of important and reasonable political and regulatory barriers to the international system creating a binding commitment to the implementation of financial standards. This is a long-term political project that is incredibly ambitious.

The FSB has maintained a strong commitment promoting compliance with international financial standards. It is time for the FSB to recognize that national regulatory differences exist and that this has an impact on the management and governance of financial stability. The FSB should dedicate a working group to determine the impact of differences in national regulatory frameworks on the stability of the international financial system and to identify innovative mechanisms that recognize these differences, manage their impact, and mitigate their impact on the resiliency of financial firms. The 2008 global financial crisis revealed the impact of counterparty risks for stability of individual financial firms and the financial systems as a whole. Integrating the impact of diverging regulatory frameworks in the counterparty risk of foreign financial firms would provide an effective mechanism to reflect the risks of differences in regulation and promote adherence to international financial standards and norms. However, this would require financial regulators, particularly prudential bank regulators, to strengthen cooperation and information sharing mechanisms. Domestic legislative and judicial barriers to the effective sharing of information on financial firms remain. In an era of near unfettered financial globalization, this is a relic of the past and needs to be addressed.

Recommendation: During the FSB’s planned review of its representation, the FSB should propose to the G20 to expand the Plenary membership to include seats for non-member co-chairs of the six RCGs. This would ensure a strong voice for regional representatives and increase the overall effectiveness of financial regulatory reform.

¹ Alejandro Vanoli, “FSB: Current Structure and Proposals for a More Balanced Representation,” in The Financial Stability Board: An Effective Fourth Pillar of Global Economic...
The IMF’s ROSC program was created after the Asian financial crisis in response to the G7’s push to strengthen the implementation of financial standards. The IMF assesses countries on their implementation of international financial standards as defined by the FSF’s Twelve Key Standards for Sound Financial Systems. These financial standards are predominantly created within standard setting bodies in which the majority of input and power over decision making processes reside in the hands of the G10 (before the crisis) and the G20 (after the crisis). The IMF’s ROSC program places pressure on countries to implement financial standards that were created without their participation.

³ FSB key committees include: Steering Committee, the Standing Committee on Assessment of Vulnerabilities, the Standing Committee on Standards Implementation, the Standing Committee on Supervisory and Regulatory Cooperation, and the Standing Committee on Budget and Resources.


An inadequately governed financial system has severe consequences for the real economy. The economic and social costs of the 2007-08 financial crisis were (and continue to be) enormous. Since then, income inequality has intensified, unemployment has soared, and the gains in global poverty alleviation have come under threat. To mitigate, if not prevent, such consequences in the future, global efforts have focused on strengthening the oversight and resilience of the financial system. This section will assess the Financial Stability Board (FSB), the institution responsible for coordinating these global efforts, and the impact of financial reform on the real economy. As Rupert Thorne, FSB Deputy Secretary General, said in a conversation with civil society in April 2014:

“We should not think about ‘stability’ as an end in itself, but on what stability achieves.”

This assessment will focus largely on the level of “safety and soundness” in the financial system for two reasons: First, a safe and sound financial system means less risk to the real economy and lower probability of future financial crises. Second, the “safety and soundness” of the global financial system is an “essential pre-requisite” for long-term investment finance, according to a 2013 FSB report. Less risk and greater long-term investment would both help to increase employment, reduce inequality and achieve sustainable development goals.

To increase “safety and soundness,” the FSB has identified five vital reform areas: 1) Too-big-to-fail, 2) Cross-border Bank Resolution, 3) Over-the-counter (OTC) Derivatives, 4) Shadow Banking, and 5) the Global Legal Entity Identifier System (GLEIS).

Therefore, and for the purpose of this assessment, greater progress in these reforms will indicate greater “safety and soundness” in the financial system. The ultimate objective is to assess how “safety and soundness” impacts the real economy.

In this assessment, each reform area is evaluated by separate analysts who were asked to:

1) Assess the progress of each of these reform areas, according to three “progress criteria” (FSB Role, Status of Reform, and Substance of Reform); and

2) Assess how progress in reforms has affected “safety and soundness” and to identify how this level of risk impacts to the real economy, especially for developing countries.

Risk or “safety and soundness” is assessed on a 4-point scale: 1-Negative, 2-None or Limited, 3-Slightly Positive and 4-Very Positive. When assessed to be in between two scores, half-points are assigned.

NOTE: This year’s report does not assess the FSB on Trade in Financial Services, Sovereign Debt or Taxes, as it did in 2013. Although the FSB has the mandate to address these issues through its responsibility for global financial stability, the 2014 report only assesses the top five areas of work prioritized by the FSB. Authors are members of FSB Watch, a global coalition promoting the public interest in global financial rule-making, and have prepared these assessments after face-to-face consultation with FSB Secretariat staff.
The “too-big-to-fail” (TBTF) issue arises in the context of the failure and distress of large and complex financial institutions (LCFIs) - or “systemically important financial institutions” (SIFIs) - that, by virtue of their size, market importance, and interconnectedness could cause significant dislocation within the global financial system and economy. The economic impacts that their failure could create would be so severe that they would put pressure on national authorities to bail them out in order to avoid financial instability and economic chaos.

The large-scale bailouts using public funds that were observed in 2008-2010 presented serious problems of moral hazard. They created an implicit subsidy for the bank, as counterparties were willing to provide funds on easier terms, and encourage excessive risk-taking by banks. The downside of these risks was absorbed by the public.

Role of FSB: Moderate
Since the G-20 Seoul Summit decision to adopt a framework to reduce the moral hazard of SIFIs (SIFI Framework), the FSB has made important contributions to this effort.

A major contribution of the FSB has been designing methodologies for assessing global systemically important banks (G-SIBs) and insurers (G-SIIs). To date, 28 G-SIBs and 9 G-SIIs have been designated. Higher loss-absorption capacity, more intensive supervision, and resolution planning requirements will apply to all these institutions.

As of the end of 2013, the FSB had strengthened cooperation on TBTF at the global policy development level – generating agreement on 33 per cent of proposed reforms. Another 50 per cent are near completion at the policy level. Much of this positive momentum can be attributed to the FSB. However, considerable gaps remain with implementation at the domestic level. There also has not been adequate progress at the FSB to remove obstacles and generate cooperation on information sharing agreements.

More broadly, the FSB has provided little guidance on whether agreed-upon reforms are adequate to end TBTF.

The FSB also has not explored the possibility of more far-reaching structural reforms which could help reduce the moral hazard of TBTF, despite important efforts at the national level along these lines, including the US Volcker Rule, the UK Vickers Commission reforms, and structural reform efforts in the EU. The FSB could play a valuable role in improving communication and consensus on these reforms and integrating them into the international regulatory consensus.

Status of Reform: Moderate
A newly strengthened capital regime requiring additional “going-concern loss absorption capacity” (GLAC) for G-SIBs has been finalized and in many cases the G-SIBs are building the extra capital ahead of schedule.

Many jurisdictions are implementing enhanced supervision for risk management, risk aggregation, and risk reporting. There has also been some progress in advancing the FSB’s “Key Attributes of Effective Resolution Regimes.” For example, the EU Bank Recovery and Resolution Directive will soon be adopted. While differences between the EU and US approaches remain, both plan to require TBTF banks to hold enough loss absorbency capacity to cover or “bail-in” their losses.

At the same time, there is evidence that banks have not yet made internal changes required to make resolution feasible. US financial regulators recently rejected the resolution plans of major US global banks on the grounds that the plans were unrealistic and did not reflect the kind of structural changes necessary to make resolution successful. It seems likely that similar problems exist in other G-SIFIs as well.

Substance of Reform: Limited
Although some key reforms are progressing, there is concern that these reforms are inadequate to end TBTF. While loss absorption has increased, it has done so from a low base and many economists believe that SIFI capital levels remain well below optimal levels. Significant doubts also remain about capacities for cross-border resolution. Some regulators argue that more changes are necessary to ensure that there is sufficient “bail in” debt held by global banks to facilitate a resolution while protecting taxpayers. Others believe additional steps are necessary to ensure that foreign subsidiaries can either remain operational or be resolved without triggering conflicts between different national supervisors (see section below on Cross-Border Resolution).
Impact Assessment: 2 (Risks Remain the Same)

The most recent IMF Global Financial Stability Report estimates that the total implicit subsidy for TBTF banks run into the hundreds of billions of dollars - that is billions of dollars committed to supporting the financial sector at the expense of infrastructure, healthcare services, education programs or international aid.

In addition, based on BIS studies, another banking crisis could cost the global economy around US $44 trillion. This would be devastating to the real economy, where the poorest people and countries would absorb a disproportionate amount of these costs. Until the FSB and national regulators agree on a way to end TBTF, an inclusive and sustainable economic recovery from the last financial crisis is severely threatened.

Recommendation: To reduce the probability and severity of another financial crisis, which would intensify unemployment and income inequality, the FSB must hold national regulators accountable for fully implementing TBTF reforms.

Cross-Border Resolution

Key Attributes play an important role in assessing the stability of the system.

Status of Reform: Moderate

The Key Attributes have not yet been fully implemented. FSB peer reviews in 2013 showed that implementation within FSB’s membership were still in the “early stage.” Until now some countries (e.g., US, EU, Switzerland, Japan) included Key Attributes while designing the resolution framework for their jurisdictions, especially when deciding on a harmonized set of tools granted to the resolution authority, such as: resolvability assessment (RAP), coordination and cooperation in “resolution planning and resolution actions” (RRP), additional loss absorbing capacity (bail-in), and burden-sharing and institution-specific “cooperation agreements” (COAG).

All FSB members have committed to full implementation of Key Attributes by end of 2015.

A positive aspect from the TBTF reform process is the creation of a standard to address loss-absorbing capacity. This “bail-in” means TBTF bank failures can be resolved without threatening public funds. During the G20 summit in St. Petersburg, leaders tasked the FSB with assessing “gone-concern loss absorbing capacity” (GLAC), for the purpose of bailing-in TBTF banks. The FSB intends to make a formal proposal for GLAC along with minimum requirements for SIFIs to the G20 during the Brisbane Summit in November 2014.

Quality: Not Adequate

The Key Attributes represent a major step forward. Considering the international efforts, much has been achieved, mainly by the creation of Crisis Management Groups (CMG) between home and host countries, and implementation of institution-specific arrangements between the home and host to govern preparation of RRP. However, it is probable that in a crisis situation authorities may choose not to work together. In the absence of binding arrangements on burden sharing, dispute resolution and sanctions for non-compliance, agreements will count for nothing.

Any cross-border resolution process requires extensive cooperation between national authorities. Major problems are likely to arise if host authorities, especially in jurisdictions where a SIFI has a systemic presence, are not participating in the CMG for the SIFI. FSB Key Attributes state that “host authorities should not pre-empt resolution actions by home authorities” meaning

Katarzyna Hanula-Bobbit, Finance Watch

The recent financial crisis demonstrated that disorderly failure of systemically important financial institutions (SIFIs) has destabilizing effects on the economy as a whole. An insufficient resolution process for a SIFI can have severe implications for the countries that host SIFI branches and subsidiaries. The FSB is responsible for coordinating global efforts to address the challenges of cross-border resolution.

Role of FSB: Excellent

FSB has managed to draft new international standards for effective resolution regimes aimed at providing robust alternatives to a zero-failure regime for SIFIs. The FSB’s “Key Attributes” provide guidelines for the basic elements that must be included in any effective resolution framework that will both safeguard financial stability and minimize the use of public funds.

FSB has also initiated a peer review process to assess implementation of the Key Attributes. Together with the methodology assessment (yet to be developed), the FSB’s
that the right for a host country to act on its own is limited. This is a particular concern for developing countries, which will have even less leverage in the resolution process.

**Impact Assessment: 2 (Risks Remain the Same)**

If host authorities have limited access to information and little voice in the resolution planning process it may contribute to negative outcomes for that jurisdiction. This is of particular concern for developing countries where there is a significant presence of SIFIs and domestic financial systems are less resilient. If this issue is unaddressed, cross-border resolutions could lead to dissolution of subsidiaries in other countries – at the expense of economic stability, small businesses and depositors in that host country. To prevent such losses, host countries may be forced to use limited public funds to bailout SIFI subsidiaries. This, of course, threatens government spending on education, healthcare, infrastructure and social programs.

**Recommendation:** As a safeguard for developing economies with fragile financial systems, the FSB should identify which countries are most vulnerable to the failure of SIFIs and Regionally Important Financial Institutions (RIFIs) and facilitate stronger coordination between these host countries and SIFI home countries.

Steve Suppan, Institute for Agriculture and Trade Policy

**Role of FSB: Limited**

The FSB has enhanced the dialogue between major jurisdictions on OTC Derivatives reforms, but has been less successful in generating meaningful cooperation. Europe and the United States remain far apart on common standards for derivatives trading.

The FSB can agree on best practices and the infrastructure required to implement reforms, but if FSB members attempt to seek a competitive advantage for the SIFIs headquartered in their jurisdictions, reforms could unravel – at the cost of the safety and soundness of the entire financial system.

**Status of Reforms: Limited**

Legislation has been passed in most FSB member states, but regulations are far from implemented and resistance to regulation remains intense. However, if normative and data-based reforms are fully implemented, there is a good chance that OTC derivatives markets can be effectively regulated.

The 7th FSB report to the G-20 finance ministers on OTC derivatives reform characterizes progress on the 2009 reform commitments as “uneven.” Reform has been impeded by legal and technical difficulties of agreeing on how to coordinate the regulation of markets estimated to transact US $700 trillion of gross notional value (initial face value of contracts traded) annually. The difficulties are of two kinds, normative and data related.

The FSB reports on what its member governments are doing to improve data aggregation, risk management and transparency in the OTC derivatives market. However, the FSB does not report on the financial services industry lobbying that results in exemptions, waivers, exclusions, definitions, regulatory budget cuts, lawsuits against regulators and other tactics that impede normative reform and the improved reporting of trade data. As a result, there has been limited progress in implementing legislation mandating OTC derivative reforms. The FSB should authorize the Secretariat to compile and evaluate FSB regulatory exemptions and litigation and the impact of both on implementation of G-20 reform commitments.

**Quality: Adequate**

The FSB Aggregation Feasibility Study Group (AFSG) produced a strong consultation paper on options to make it possible for member country regulators to standardize, aggregate and analyze OTC trade data across borders. The AFSG policy options for aggregation are technologically feasible, and progress on the Legal Entity Identifier (LEI) suggests that the aggregation proposal is likewise legally feasible. However, FSB Watch anticipates that there will be both industry and political resistance. The FSB should authorize and agree how to finance and administer cross-border trade data aggregation.

**Impact Assessment: 2.5 (Risks Remain the Same, Slight Positive Impact)**

The financial risks of most, if not all, retail financial products are “securitized” in the derivatives market. These products, such as mortgages, credit cards, payday loans and others have visible and direct effects on the non-financial (“real”) economy, particularly on households and small businesses. Therefore, if derivatives data reported by financial institutions to regulators is not comprehensive, in near-real-time and uniform, regulators cannot determine the drivers of price volatility. As a result,
the real economy remains vulnerable to derivatives price
and interest rate moves.

Commodities derivatives comprise less than one per cent
of the value of the global OTC market, according to the
BIS. However, the impact of commodity derivatives on
the real economy, including food and energy security, is
far larger than its very small fraction of the total OTC
derivatives market. Even with the recent exit of several
SIFIs from the derivatives price-influential warehousing
and trading of physical commodities, the real economy
remains vulnerable to SIFI commodity derivatives trading,
not just in FSB member jurisdictions, but wherever SIFIs
operate and food is sold across borders.

Market and regulatory failure in commodity derivatives
has a particularly severe impact for low-income countries
dependent on imports for a critical margin of food
security. There are currently 55 low-income countries
dependent on food imports, according the Food and
Agricultural Organization (FAO), and 1 of 9 people in the
world are still undernourished. Therefore, it is critical that
the FSB contribute to safeguarding developing economies
from the unpredictability of commodity prices.

Recommendation: The FSB should establish and enforce
effective limits to SIFI and other large financial institution
dominance of commodity derivatives trading.

Markus Henn, World Economy, Ecology & Development

Regulation of shadow banking is rightfully seen as
important though it is not even clear what it is exactly.
The FSB has proposed a broad definition of shadow
banking as bank-like credit intermediation activity that is
not covered by banking regulation. This encompasses
many capital market activities, including hedge funds,
private equity funds and sophisticated vehicles. According
to the FSB, shadow banking “can have important
advantages and contributes to the financing of the real
economy” but it “can also become a source of systemic
risk.”⁷ As in other areas of finance, this is not just a
problem for advanced economies.

Even though some types of shadow banking seem to have
specific importance in advanced economies⁸, some forms
have also grown rapidly in emerging economies.⁹ Non-
bank lending practices are sometimes seen as rather
beneficial as they provide financial services to more
people than regulated banks do – boosting efforts to
increase financial inclusion. However, new households
gaining access to finance are often unknowingly exposed
to the high risks in shadow banking. A 2014 UN Report
notes that stronger monitoring is needed to “ensure
consumer protection.”¹⁰

Role of FSB: Limited
The FSB has done considerable work in mapping the issue,
producing important analysis on the size and nature of
the problem, and releasing some of the first policy
frameworks. The FSB’s greatest achievement thus far has
been facilitating an agreement on an information-sharing
process, but this does not include money market funds.
The FSB’s work only started in 2011 and it is still working
on many frameworks such as for minimum haircuts. At
this time, it seems that the FSB has no ambitious mandate
or cannot itself put enough pressure on its members. To
strengthen cooperation, the FSB should: Strengthen data
gathering and monitoring; be more proactive in
identifying risks, and be vocal when risks emerge;
 improve quality of security financing rules and standards;
and monitor interaction between shadow banks and
offshore affiliates.

Status of Reforms: Limited
Given the FSB’s rather broad definition of shadow
banking, the reform landscape is not easily overseen.¹¹
However, it can be said that the reforms that have
specific links to the financial crisis have only moved
forward slightly. This includes:

- Limits to securitization, mainly by requiring reten-
tion of capital in the balance sheet, e.g. 5 per cent
in the EU.
- Laws on hedge funds (alternative investment
funds), such as those in the EU.¹²
- Laws on money market funds, such as a draft in
the EU, a new law in Chile, and a recent regulation
in the United States.¹³
- Laws on security transaction financing, like repos,
security lending or re-hypothecation (FSB calls
them “secured financing contracts”), e.g. a draft
law in the EU¹⁴ and new regulations in Singapore
and Malaysia.
- Laws on some risky transactions by banks and the
relation of banks to funds, for example in bank
separation laws which have been finalized in the
US, Germany, France the UK and Belgium. The EU proposed a draft law.¹⁵ China regulated the off-balance “wealth management products” of banks.

- Regulation of non-bank deposit-taking institutions and finance companies.¹⁶

This progress is positive, but large gaps remain in shadow banking oversight. For example, a comprehensive framework for data collection from offshore financial centers does not exist.¹⁷

Quality: Inadequate

The shadow baking reforms are the least successful amongst the FSB’s range of reforms. Despite its outstanding role in the crisis, shadow banking still goes almost untouched. And while the core of shadow banking in the EU and the United States still exist, new activities in emerging economies, especially China, add new risks to the global financial system.¹⁸

- The EU hedge fund law is weak as it does not touch upon the funds’ business model, while the United States has not changed anything. Regulation of finance companies in the Americas remains heterogeneous.

- Securitization laws are insufficient, particularly due to low balance sheet capital retention requirements.

- The risky ties of banks to investment funds are insufficiently addressed in the bank separation laws and law proposals due to many exemptions and incomplete coverage.

- The ties to special purpose vehicles are not clearly addressed in the bank separation laws. Furthermore, the Basel III leverage ratio, actually intended to cover all risks, was watered down in January 2014 and does now not comprehensively prohibit off-balance sheet vehicles.

- Money market funds remain lightly regulated in the United States, and in the EU the respective draft law has been stopped in the parliament in March 2014, and it is unclear if it will ever be finalized.

- The EU laws on security transaction financing mainly intend to increase transparency but rules on haircut regimes are missing as there are no global standards yet.

Impact Assessment: 2 (Risks Remain the Same)

As the Deputy Governor of the Reserve Bank of India put it in a speech in June 2014, “When non—bank financial entities undertake bank-like functions, large risks are created which could potentially be destabilizing for the entire system.” There is little reason to believe that there is more adequate regulation or monitoring of the shadow banking system. At this time, the benefits from shadow banking – whether it be financial inclusion or greater financing of SMEs – appear to be outweighed and threatened by the potential risks. Without greater progress in reform efforts, coordinated by the FSB, the risks concentrated in the shadow banking system continue to threaten the real economy in both developed and developing countries.

Recommendation: To safeguard advances made in financial inclusion, the FSB should document the degree to which consumers and small businesses are exposed to shadow banking, especially in developing economies. If vulnerability is high, the FSB design targeted reforms that address these risks.

Global LEI System Score 2.5

Navin Beekarry, George Washington Law School

The Global LEI System (GLEIS) will give every financial entity a unique identifier code (the LEI) that will contain specific information about that entity. The objective of the LEI is to ensure that there is greater transparency of financial entities and to improve regulators’ ability to monitor and mitigate systemic risks. An effective GLEIS will enhance transparency and accountability for all financial entities and transactions – whether related to government contractors, mining companies or criminal organizations. It is estimated that developing countries lose almost US $2 trillion annually due to the opacity of financial entities and transactions, which facilitates illicit financial flows, money laundering and misallocation of natural resource revenues.¹⁹

Role of FSB: Excellent

The FSB has been essential to the progress of the GLEIS. In its capacity as the GLEIS Secretariat, it facilitated the implementation of the G20 decision to establish the GLEIS. Accordingly, it set up the GLEIS governance structures and successfully moved the LEI process from the policy stage
into operational readiness. As of June 2014, the institutional framework of the GLEIS was completed and ownership and oversight of the GLEIS transitioned to the Regulatory Oversight Committee (ROC). Although the FSB will no longer act as the Secretariat of the ROC, it will remain a full member of the ROC.

**Status of Reform: Excellent**
A significant indicator of progress is the development of the institutions responsible for the oversight and operations of the GLEIS. The ROC, the Central Operating Unit (also known as the GLEIS Foundation) and pre-LOUs (local operating units) have been established and are operational. Within the ROC, a Committee on Evaluations and Standards provides recommendations on technical standards. So far sixty countries are represented on the ROC and COU.

The implementation phase adopted a collaborative approach and successfully integrated government, private sector, NGO and academic participation pursuant to the G20 decision. Importantly, governments and the private sector have been fully participating in the GLEI process.

The Executive Committee of the ROC and the Board of Directors of the Foundation are operational, and pre-LOUs have started issuing pre-LEIs which means financial market participants are registering. The establishment of 19 pre-LOUs at country level in less than 2 years indicates a high level of interest and participation. Twelve additional pre-LOUs have already been granted prefixes to support operational platforms. So far, pre-LOUs have issued over 300,000 pre-LEIs to entities from more than 150 countries. In addition, regulators such as the Commodities Futures Trading Commission (CFTC), European Securities and Markets Authority (ESMA), and European Banking Authority (EBA) now mandate the LEI. This level of “buy-in” is essential for the GLEIS to be successful.

A key component of the GLEIS is, of course, the data. On this front, data standards have been adopted for the LOUs and the compilation of LEI data has already started. Data standards and aggregation are not perfect, but it is very positive that they being established.

**Quality: Not Adequate**
Although the LEI process is moving forward quickly, there are several important aspects that remain unaddressed – or not included at this time – which are necessary if the LEI is to achieve its ultimate goal of increasing transparency in finance. These unattended aspects include: 1) Reliability and accuracy of data still to be tested; 2) Public use of data still to be ascertained; 3) Regulatory compulsion for other countries that are not willing to cooperate still an open issue; 4) Privacy and secrecy of financial data in some jurisdictions still unresolved; 5) No development so far on LEI relationship data; and 6) Achieving public objectives such as systemic risk monitoring, beneficial ownership assessments and data aggregation still untested.

Without addressing these substantive issues, the excellent progress in moving the LEI process forward could be jeopardized.

**Impact Assessment: 2.5 (Risks Remain the Same, Slight Positive Impact)**
With increasing activity in securitization, shadow banking and OTC derivatives, the strong systemic risks are still present. At this point, the LEI process is not ready nor able to offset these risks. This means the real economy remains largely exposed to the opacity and systemic risks in the financial sector, similar to those that culminated in 2008 in severe economic loss and hardship for so many people – in developing and developed countries alike.

The GLEIS has the potential to address major challenges related to financial transparency, regulatory oversight and illicit financial flows. However, until the substantive issues are addressed and the LEI is fully operational, there are a number of ways the real economy remains at risk: secrecy and opacity persist; inability to determine and assess risk and exposures of transactions and counter parties; threat to credit flow; investors and businesses at risk with no protection; regulators remain unable to monitor risks; and, illicit financial flows go undetected.

**Recommendation:** Given the economic and social costs of opacity in finance, especially for developing countries, the G20 and FSB member countries should mandate that the ROC address the issues of relationship data and beneficial ownership before the GLEIS is fully operational.
Other Relevant Issues for Financial Stability

Sovereign Debt, Trade in Financial Services and Taxes are not assessed in this year’s report. However, the FSB needs to consider the influence of these issues on global financial stability and address them appropriately.

**Sovereign Debt**

Given the regulatory hole in sovereign debt markets and their role in triggering instability (as demonstrated by the EU periphery markets such as Greece and Cyprus), the FSB should incorporate sovereign debt in its work and recommendations. In particular, the FSB should: address the classification of sovereign debt as zero-risk weighted assets; promote safer securitization of debt products and more transparent bond markets, especially secondary bond markets; and monitor Exchange Traded Funds that track sovereign debt.

Additionally, as part of its work on Credit Rating Agencies (CRAs), the FSB should consider the particular implications and relationships between credit ratings and sovereign debt.

**Trade in Finance Services:**

Based on leaked documents of international trade agreements, it is clear that the agenda being promoted in trade negotiations (i.e., “freeze” financial reform process) conflicts directly with the agenda being promoted by the FSB. Without a shift in trade negotiations regarding financial services, the authority of national financial regulators could be undermined. The FSB should designate staff to track ongoing trade negotiations and brief regulators from its member countries. Whenever a major conflict or concern arises, the FSB should issue a public response.

**Taxes**

The FSB does not work directly on tax issues, but it should be reducing the complexity and opacity in finance which directly contributes to tax evasion and illicit financial flows. The 2014 RCG Americas report* on shadow banking notes: “a comprehensive framework for data collection from offshore financial centers does not exist. This creates an important gap in the FSB’s global shadow banking monitoring exercise.” The FSB should address this gap since it threatens both financial stability and the ability of countries to collect revenue.

Overall Impact Assessment of the FSB

Greater “safety and soundness” in the financial system means less risk to the real economy and a better environment for long-term investment financing – both of which are critical for achieving inclusive and sustainable economic growth. The FSB has accomplished much that is deserving of praise, but has this been enough to create a more safe and sound financial system?

Unfortunately, this assessment finds that the overall impact of the FSB on the financial reform process and its outcomes has remained limited. According to the most recent FSB status report, only 36 per cent of reforms have been completely agreed to at the policy development level and about 25 per cent are either un-developed or under-developed. Differences in national interests and regulatory regimes, as well as industry resistance, are noteworthy barriers.

The FSB’s limited success in advancing international cooperation on core reforms, and some inadequacies in quality, has possibly weakened the impetus for action among its member countries, which are ultimately responsible. As a result, many of the risks that spawned the recent financial crisis still exist and the real economy remains vulnerable in many ways to the whims of the financial system. Developing countries, with little voice in the reform process, remain disproportionately vulnerable to these enduring risks.

Recommendation: The FSB should request that the G20 strengthen its institutional capacity and power to galvanize agreement on and enforce a global “regulatory floor” (i.e., minimum standards) that safeguards public interests, especially in countries with fragile or developing financial systems.
Costs of the financial crisis, in the US alone, are estimated to be more than $12.8 trillion. Better Markets, Inc. 2013


Structural banking reforms refer to separation or limitation of activities, intra-group exposure limits, and local subsidiary capital requirements.

Since the end of 2009, the G-SIBs have increased their common equity capital by about US$ 500 bn, amounting to close to 3 per cent of their risk weighted assets.


Ibid.

For a more extensive evaluation, see, for example, the FSB’s RCG reports on Asia and the Americas.


See the RCG reports on Asia and the Americas.


2013 FSB report on Status of Implementing Reforms.
The IMF’s highest governing body, the Board of Governors, meets annually, and the International Monetary and Finance Committee of the Board holds biannual meetings. An Executive Board, comprised of 24 resident Executive Directors (ED), at the IMF headquarters in Washington, DC, conducts most of the business of the Fund, meeting several times each week, and largely on the basis of papers prepared by IMF staff. The Managing Director (MD) is the Chair of the Board as well as its senior employee - the Chief Executive Officer. The MD selects the Deputy Managing Directors, who chair the Board when the MD is absent.

There has been no substantive change in IMF transparency policy over the past year. The one bright spot is in the Fiscal Affairs Department new Fiscal Transparency Code, whereby governments are encouraged to make both revenue and expenditures publicly available in clear language and in a timely manner. This work will continue into 2015 focusing on extractive industries.

The two major black boxes remaining at the IMF are Board discussions (verbatim transcripts) and within its Capacity Development Institute (CDI). Minutes of Board meetings are released after 5 years and are available through the archives, but there are no verbatim transcripts.1 Citizens of a member country still cannot know what their Executive Director has said on any issue, although some EDs release their formal prepared statements to national audiences; there are no informal comment in the context of actual Board discussions. The CDI encompasses both technical assistance and training. When a country makes a specific request of the Fund for such assistance, nothing is public unless that country takes the initiative to make it public; this is the inverse of other Fund documents where they are presumed public unless a country intervenes.

In 2013 the Board agreed that IMF publications should be released in a more timely way, and while it still allows countries to exclude material, the newer standards seem to restrict such exclusions to genuinely “market sensitive” information². The bottom line is that material released by the IMF is sanitized, despite being characterized as a public, intergovernmental institution, funded by governments and therefore by taxpayers.³

Recommendation: The IMF should publish all documents, including Board minutes and summaries, including monitoring and evaluation reports, of technical assistance and capacity building programs, and missions.

The Board of Governors is fully representative in that it is comprised of one representative from each member-country who is either a Finance Minister or head of the Central Bank. The IMFC and the Executive Board represent countries through a “constituency system”. Under its current rules, the five largest economies (and therefore
the 5 largest shareholders), each have one seat, as do China, Russia and Saudi Arabia. The remaining 16 seats are divided among 180 countries. Western Europe has 8 chairs (9 when Spain is representing its constituency with Mexico and Venezuela), while 46 Sub-Saharan countries have only 2. By including all member-states while retaining relative efficiency, the IMF constituency model is one which should allow a reasonable degree of inclusiveness and participation.

However, its execution has many failings. The allocation of chairs, and the voting shares (and therefore voice) given to each chair, both derive from the measurement of a country’s “economic size”, through a quota formula. These shares determine how much each country contributes to the common capital of the Fund and how much each country may borrow from the Fund. Ordinarily the Board decides matters by consensus, but crucial issues such as quota increases, changes in shares, and changes to the IMF’s Articles need to be approved by an 85 per cent majority, and the US is the only single country with sufficient votes to block such decisions.

For many years civil society and developing countries have criticized the quota formulas for its “democratic deficit”, in terms of not giving enough voice to developing countries, and to countries which are borrowing from the Fund, because population is excluded from the formula. Given recent rapid growth in the share of major emerging market and developing countries (EMDCs) in the world economy, and their increasing public criticism of the quota system, it became untenable by 2010. The Korean G-20 Summit offered a two-step process to increase the share of emerging economies in quotas and votes, reduce European chairs by 2, and protect low income countries’ tiny voting shares. However, despite leading the push for these changes in Korea, the US Administration has subsequently failed to secure Congressional approval for these changes, thereby putting IMF governance in a long-term stall. Emerging countries have therefore been increasingly harsh in their criticism of the institution, with the most recent BRICS summit declaring themselves “disappointed and seriously concerned with the current non-implementation of the 2010 International Monetary Fund (IMF) reforms, which negatively impacts on the IMF’s legitimacy, credibility and effectiveness.”

Finally, the most worrying recent development has been that the G20 has effectively become the de facto executive committee of the Governors, setting the agenda of the IMFC and the whole institution, and leading the IMFC to work mainly on the “how” of executing G20 decisions. As discussed in the G20 section of this report, the G20 itself is not remotely inclusive – and therefore neither are the most important decisions on the IMF.

A year ago the IMF seemed to be working to enhance and systematize it relations with civil society organizations. The new handbook on IMF staff relations with CSOs, which was expected to be published this year, has not emerged. Recommendation: The IMF should reform its quota system more fundamentally to take account of population as well as economic size, increase the number of chairs allocated to emerging and developing countries, recruit its Managing Director competitively and transparently, and accelerate efforts to diversify staff recruitment.

Management and staff selection also undermines inclusiveness. In spite of repeated efforts to have a more transparent selection process, in practice the IMF Managing Director is formally elected by the remainder of the Executive Board. The First Deputy MD is American, and other senior posts are shared out largely among other major shareholders. G24 and African Ministers have frequently complained about the under-representation of developing countries in management and staffing. Efforts to encourage mid-level entry from developing country ministries and central banks has somewhat reduced this imbalance, but there is a long way to go. The concentration on recruitment direct from orthodox economics courses also limits the diversity of thinking in Fund analysis, and even more so in Fund practice.

In order to ensure that Board, Management and Staff adhere to the goals and best practices of the IMF, regular and reliable evaluations of performance must occur. While there are routine evaluations of staff performance by managers, such accountability is largely absent at the top of the institution.

Once an Executive Director is selected (appointed by the largest economies; elected within constituencies which usually select the nominee of the largest member of the constituency), the Articles of Agreement and By-Laws provide no means whereby that ED can be removed for his/her two-year term, regardless of private or public pressure.
professional conduct. The EDs appointed by the 5 largest member states can be removed rather simply by a political decision, not necessarily the result of performance evaluation. There is no job description for an ED, nor criteria for selection or for assessing the execution of their tasks. The Board of Governors exercises little oversight of the Executive Board as a body.

Since the selection of Dominique Strauss-Kahn in 2007, the Managing Director has an Executive Board-prepared description of the qualifications the person should bring, and a stipulation that the MD is bound by the rules of ethics for senior management and staff. There is no periodic performance evaluation of the MD by the Executive Board; the person remains MD so long as his/her political sponsors are satisfied with the person’s performance.

A positive aspect in IMF accountability is the Independent Evaluation Office (IEO), which the Executive Board established after the Asian Financial Crisis in 2001. The IEO is genuinely independent of Management, reports directly to the Executive Directors, and sets its own agenda (though it is not allowed to review ongoing work). Regrettably, the Executive Board has not exercised sufficient oversight over implementation of the IEO recommendations – which are approved by the Board itself. Management periodically reports generally that all Board-approved recommendations have been accomplished or are on schedule for a timely completion, even when recommendations are repeated in subsequent evaluations.¹⁰

In sum, the Governors do not evaluate the IMF as a whole, nor does the Executive Board; the Executive Board does not evaluate the MD and ignores Management’s undercutting of the IEO, the single independent entity set up to evaluate programs and activities. Occasional internal self-evaluations by the Strategy, Planning, and Review Department are self-critical, but do not seem to result in policy or behavior changes nor rarely in punishment for any responsible individuals and never in compensation for those negatively impacted by wrongful policies or actions.

**Recommendations:** The Board of Governors should establish a committee responsible exclusively for periodically overseeing a review of the performance of the Executive Board. The Executive Board should meet with the committee to consider its reports and recommendations.

The Executive Board should design a formal, periodic process of assessment of MD performance, including through the use of expert outside advisors. Such evaluation should include an assessment of the MD’s management skills. The MD should also solicit Board input into periodic evaluations of the performance of the Deputy Managing Directors.

**Responsibility**

| Score | 1.5 |

Affected stakeholders should be able to hold the IMF responsible for negative consequences of its policy recommendations. The Fund maintains it is not possible to determine any causal connection between the policy conditions associated with receiving IMF funds and any subsequent pain or suffering endured by the residents of the country in question. This rationale rests first on the assertion that the chain of causality is too complex to be reliable. Second, the Fund cannot be held responsible for policies that are “formally” set by the government, in tandem with the IMF. Third, countries approach the IMF when they are already in desperate economic straits, and are largely responsible for problems of their own making.

This is not a tenable position. The Fund makes strong policy recommendations and should be expected to conduct ex ante analysis of the impact of these on stakeholders, especially on inequality, especially given the many complaints over the years about its programs from people and countries living with them. In 2002 the Boards of the IMF and World Bank jointly agreed to conduct Poverty and Social Impact Assessments (PSIA).¹¹ However, the IMF Board allocated minimal funding for this purpose, and since then very little analysis has been conducted in the context of policy advice and TA, except of individual tax and subsidy measures. The IMF Research Department has conducted far more analysis of the poverty and distributional consequences of policy programs and measures, but there is no systematic assessment of the impact of the programs recommended on inclusive growth, poverty and inequality as part of program formulation. This assessment should also be considered for the overall impact of Fund advice on the global economy.
Finally, under current arrangement there is no option for individuals, communities, or countries that may have suffered harm from Fund promoted policies to register their complaints. Nor can they expect any compensation: as an intergovernmental body, the IMF and its staff enjoy full legal immunity.

**Recommendation**: The IMF should conduct full PSIA of its recommendations (with a particular emphasis on fiscal measures related to tax, spending and subsidies) for all country programs, and establish a complaints mechanism similar to that of the multilateral development banks.

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**IMF Governance Assessment**

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<thead>
<tr>
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</tbody>
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**Governance Gap**

46%
¹ The 2013 IMF Transparency Review provided for the archives to be prepared for electronic sharing on the Fund’s website. The timeline for such disclosure was not provided.
⁴ In order of voting shares held: the United States, Japan, Germany, France and the United Kingdom.
⁵ “In some instances, the G20 acts like a caucus inside the IFIs – for instance, with regard to reform of the IMF governance and voting system.” By Nancy Alexander, “Governance of the G20,” in this publication, 2013.
¹¹ In 2001, a framework operationalizing this [PSIA] vision was set out in a joint paper, “Strengthening IMF-World Bank Collaboration on Country Programs and Conditionality,” together with a corresponding staff guidance note. The IMF Board formally approved this work in 2002.
The IMF’s mandate is to promote international monetary cooperation, relatively stable exchange rates, and balanced growth of international trade. The combined results are expected to be high levels of employment and real GDP growth. In recent years the Fund has increasingly focused its mandate on reducing poverty (in low income countries (LICs) since 1999);¹ and on generating more “inclusive” growth in high (HIC) and middle income countries (MIC).² The IMF Managing Director has explicitly said:

“I hear people say, ‘Why do you bother about inequality? It is not the core mandate.’ Well, sorry, it is also part of the mandate. Our mandate is financial stability. Anything that is likely to rock the boat financially and macroeconomically is within our mandate.”³

To achieve this mandate, the IMF provides member countries in balance of payments difficulties with loans (and a “seal of approval” for policies which are designed to have a catalytic effect on increasing funding from donors, lenders and investors). As of August 2014, the IMF had lending or policy support programs with 28 LICs, and 13 MICs/HICs, under which it agrees with country authorities on a set of “policy conditions” or “conditionalities” to improve economic policies in return for the loans. It also conducts economic surveillance, to track the economic health of countries, alerting them to risks and providing policy advice, and technical assistance, training and research to help improve economic management.⁴

In this light, and in line with this Report’s overall impact assessment criteria, we assess the Fund for its impact on poverty and inequality through the types of policy recommendations it makes which can reduce inequality (on employment, decent work and wage levels; on progressive budget revenue; on pro-poor/anti-inequality spending; and, on pro-poor financial systems), as well as its ability to mobilize low-conditionality money which can help to finance these interventions.⁵

The way the IMF helps countries design macroeconomic policy has a key impact on whether growth is inclusive, and on reducing poverty and inequality. The IMF sets specific growth targets in its programs, based on what it regards as achievable given the level of financing available to the country, the potential impact of large growth-oriented projects, and possible trade-offs between growth and inflation: however, it does not set targets for poverty or inequality.

As discussed in this Report last year, independent and IMF analyses has shown reasonable real GDP growth, which has slowed since the global economic crisis and remains well below the 7 per cent levels needed to halve poverty;⁶ and a sharp fall in poverty since the 1990s. However, independent analysis suggests that IMF programs have managed to assist only marginally with inequality. Gini coefficients⁷ stayed high in IMF program and non-program countries, and rose in both groups in 1990-2000. Although they fell slightly in program countries after the Poverty Reduction and Growth Fund

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Matthew Martin, Development Finance International
(PRGF) was introduced, the difference with other countries was marginal. Overall, IMF programs are not consistently correlated with significantly higher growth, or (in the last decade) with faster falling inequality, than non-IMF program countries. IMF program countries do seem to show faster poverty reduction, though this advantage has diminished in the last decade.

It is striking that, while insisting growing inequality is a major risk for sustainability of growth and development worldwide, and greater equality leads to more sustainable growth, the IMF has not done any in-depth multi-country analysis of the impact of its programs on inequality, and has acknowledged that its analysis of growth and anti-poverty/inequality strategies in LIC programs and surveillance is insufficient. Much more needs to be done to ensure IMF programs produce faster growth and reduced poverty and inequality. These efforts represent a major challenge for the IMF in the post-2015 global development agenda.

**Recommendation:** The IMF should conduct systematic *ex ante* analysis of its programs’ impact on poverty and inequality, and set targets for reducing poverty and inequality as part of each country program.

The IMF has also increasingly emphasized that employment, especially youth employment, with decent wages and conditions, are vital to reducing poverty and inequality and ensuring sustainable and accelerated growth. However, the IMF continues to appear to lack a clear policy to promote employment, or to include clear targets in its programs for increasing employment, balanced with the objective of reducing inflation. Critics (and the Fund itself) have noted the IMF’s past and current preference for labor market “structural reforms” and greater flexibility, which is also reflected by its systematic use of the controversial World Bank “Doing Business” labor policy index in its programs. Critics and the Fund itself have also indicated that there is no evidence or consensus in analysis that such reforms work to increase employment or income of workers. On the other hand the Fund has given no systematic attention to ensuring “decent employment” by enhancing workers’ rights or paying reasonable minimum or “living” wages – although in some recent advice to OECD countries such as the UK and US, the IMF has recommended substantial increases in minimum wages.

The most recent IMF analysis of these issues recommends “more systematic diagnostic analysis of growth and employment challenges and identification of the most binding constraints to inclusive growth and jobs, so as to provide more tailored and relevant policy advice; more systematic integration of policy advice on reforms of tax and expenditure to create conditions to encourage more labor force participation, including by women, more robust job creation, more equity in income distribution, and greater protection for the most vulnerable; and enhanced advice on labor market policies based on empirical evidence and greater collaboration with the World Bank, OECD and ILO on the impact of these policies on growth, productivity, job creation, and inclusion.” However, though the Fund has prepared a “toolkit” for work on growth, labor and inclusion issues for country teams, it is not clear that this leads to consistent policy suggestions to authorities.

**Recommendation:** The IMF should work with the World Bank, OECD and ILO to set standards for national employment and minimum wage policies. It should systematically assess the impact of proposed labor market policies on inequality, poverty and decent work, as well as on employment creation, and set targets for employment and minimum wage levels consistent with reducing inequality and poverty.

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**Tax Policy Score 2**

In the last two decades, most of the focus of IMF tax policy advice and technical assistance has been on increasing revenue collection levels as a proportion of gross domestic product (GDP). This has met with considerable success: for example, in Sub-Saharan Africa (though by no means all of the increase can be attributed to the IMF), revenue collection rose from 21 per cent of GDP in 2002 to 28 per cent of GDP in 2008, before falling back to 25 per cent of GDP in 2013 as a result of the economic crisis.

However, the IMF has been criticized for focusing excessively on “efficiency” to mobilize maximum revenue, and not considering the “equity” of its policy advice (i.e., whether the tax is progressive; or is a level playing field for foreign and domestic enterprises). The lack of consideration for equity was reflected in composition of tax collections in 1990-2010:

- There was a strong preference for reducing revenues from trade taxes, in line with broader global trends towards trade liberalization. These were usually progressive due to higher consumption of imported goods by wealthier citizens.
The IMF failed to resist a “race to the bottom” globally in reducing “direct” (corporate and individual income) taxes, which are more progressive. Indeed in many countries it suggested reducing tax rates to keep economies “competitive”.

Little was done about widespread proliferation of exemptions from paying taxes, due to tax incentives (especially for foreign investors), and bilateral trade and investment treaties between OECD and developing countries. Though the IMF sometimes spoke out against high exemptions, these were rarely rationalized in IMF program conditions.

Equally little was done to assist countries to combat tax evasion and fraud, transfer pricing and profit shifting, which have resulted in a dramatic fall in the amounts of tax paid by major companies even without cuts in rates.

As a result, there was an increase in government reliance on “indirect” taxes on consumption (sales taxes and value-added taxes), which were likely (unless goods consumed by the poor were exempted) to hit poorer citizens harder.

This trend has been moderating in more recent IMF programs, with some countries being encouraged to increase the share of revenue coming from direct taxes, especially from extractive industries, and others to reduce or eliminate corporate tax exemptions, or to introduce exemptions from consumption taxes for goods consumed by the poor. The IMF has also been providing more technical assistance to help collect higher tax amounts from major corporations; making speeches about making income tax systems more progressive and making greater use of property taxes; and doing excellent research about the negative impact of OECD tax policies on developing countries. However, there continues to be a lack of systematic analysis of the equity or “incidence” of taxes on different income groups, and focus on eliminating the major tax gaps due to exemptions, treaties and evasion, as the basis for Fund policy suggestions.

Recommendations: the IMF should conduct systematic analysis of tax incidence, and focus country programs and TA on reducing inequality by making tax systems more progressive, combating tax evasion, and increasing property and wealth taxes. At a global level and in OECD country policy reviews, it should oppose cuts in corporate and income taxes, and oppose measures which result in reduced developing country revenues.

From a long-term perspective, there has been a marginal increase in education and health spending under IMF programs between 1985 and 2009: this reflected a fall in the first decade, followed by a rise largely due to the Fund’s requirement that debt relief funds be spent on these sectors. Nevertheless, spending levels in most countries remain far short of those needed to attain the Millennium Development Goal. In addition, several recent independent reports have demonstrated that since the global economic crisis, spending on education, health and a broader range of MDG-related sectors (agriculture, social protection, water and sanitation) has performed less well for countries with IMF programs. This is partly due to the fact that after an initial stimulus response to the crisis in 2009-10, overall spending in IMF programs stagnated or fell as a proportion of GDP, and is recovering only slowly, in part due to IMF advice stressing the need for fiscal consolidation to reduce budget deficits and keep debt levels down.

Since 2000, the IMF has monitored levels of social spending, partly in order to track how the proceeds of debt relief are being spent. Since 2009 it has gradually extended this monitoring so that all Poverty Reduction and Growth Trust (PRGT) -eligible countries now commit to “social spending floors”. However, there are major problems with the methods it uses, with dramatically different proportions and types of spending being monitored. In most cases this is limited to education and health, and pays little attention to three other types of spending which are crucial to combating inequality and poverty – smallholder agriculture, social protection, and water and sanitation. In addition, the social spending floors are only indicative policy benchmarks, with no analysis of performance in program reviews.

No such monitoring exists for higher-income countries – many of which have been suffering dramatic cuts in social spending in the wake of the 2008 global economic crisis. Furthermore, the IMF does not publish any annual comparative multi-country data or analysis which allows it to assess current trends in social spending.

Another key spending issue has been the balance between investment and recurrent spending, and especially a tendency by IMF missions to recommend reductions in recurrent spending, through cuts in real wages, or reductions of staffing levels, including in the social sectors.
The IMF made a specific undertaking not to include wage bill cuts as specific performance criteria in programs except in exceptional circumstances, yet continues to suggest them as part of policy discussions in almost all countries, resulting in a predominance of wage bill cuts in recent programs.¹⁸

**Recommendations:** The IMF should analyze the incidence of spending on inequality and poverty; recommend increases in the spending which will most reduce poverty and inequality, with a particular focus on education, health, social protection and water and sanitation; and monitor spending trends annually across all countries.

The IMF plays two roles in financial sector reform and stability. At the global level, it produces analysis (and provides advice to the G20) on potential risks to global macroeconomic and financial stability from financial developments – principally through the “Global Financial Stability Report” (GFSR). It was heavily criticized for its failure to foresee the global financial crisis and has since beefed up its analytical and surveillance capacities. Its reports and speeches by the Managing Director regularly criticize the slow pace of G20 agreement and implementation on financial sector regulations, and place more stress on potential downside risks – most recently on the risk of overdependence on pumping liquidity into financial sectors, rather than ensuring that they promote growth and are therefore more sustainable.¹⁹

At the national level, the IMF is the main organization responsible for assessing financial development and stability in LICs, through its Financial Sector Assessment Program (FSAP), and for seeing that Financial Stability Board (FSB) recommendations and global regulatory standards and codes (such as Basel III) are implemented in LICs. However, as discussed in the chapter on the FSB, this agenda is set by developments emanating from the global level, leading to over-emphasis on banking sector reform and concerns about access to banking services, and insufficient emphasis on other non-bank financial institutions with a longer-term and more stable investment perspective, such as insurance, pension funds, micro-finance, or community-based financial systems. The Fund’s work is also moving at the same slow speed as FSB global discussions in terms of adapting recommendations to the post-crisis environment, especially in LICs.

Equally important, there is no consideration in IMF global or national financial sector assessments of equity in access to financial assets and saving/borrowing instruments, and cost of financial intermediation. Underlying IMF financial sector recommendations is an assumption that integrating poorer citizens into the commercial banking system is the most efficient way to increase their access to financial products, in spite of widespread global evidence that such systems automatically discriminate against and marginalize the poor.

**Recommendation:** The IMF should base its global and national financial sector analysis on the impact of reforms on inequality as well as stability. It should prioritize national-level reforms which will enhance access to savings and investment for the poorest citizens, such as low-cost micro-finance and community-based financial systems.

The other crucial role of the IMF in combating global inequality is its role in mobilizing low-cost and low-conditionality financing to help countries offset and recover from economic crises and instability (from which poorer citizens generally suffer more sharply). It was created to have a fundamental position in combating global inequality between surplus and deficit countries by providing financing to smooth adjustment in reducing deficits.

However, one of the biggest problems for borrowing countries is that the IMF has had increasingly (and woefully) insufficient funds to help them combat balance of payments difficulties. The problem for individual countries remains that loans to them are limited to a percentage of their membership quotas in the IMF. Quotas have fallen increasingly behind growth in world GDP, trade or capital flows, and are now only a very small part (often under 10 per cent) of the amount an individual country needs to combat a crisis, not at all commensurate with the high influence the IMF has on country policies, since many donors (or in Europe other lenders such as the EC or EIB) make their flows dependent on an IMF “seal of approval”. IMF resources for low-income countries were doubled by the G20 in 2009, allowing it to lend US$3.8 billion a year during the crisis, but have now fallen back to the pre-crisis level of US$2 billion a year on the false assumption that a smaller number of countries are
content to borrow the very low levels of IMF funding available. Quotas have been supposed to be increased once more as part of the deal linked to reforms in IMF governance, but have been stalled since 2010 by lack of approval from the US Congress.

In addition, over the last few decades, there has been an increasing concentration of financing on facilities under which loans come with higher levels of conditionality. The availability of low-conditionality financing has dwindled to the point where it offers virtually no relief from “exogenous shocks” which hit economies due to no faults in economic policy.

Alone among international organizations, the IMF also has the capacity to create global liquidity, by issuing Special Drawing Rights (SDRs), which are added to country reserves and protect the balance of payments and budget from crises. They do not carry any policy conditions and therefore give countries more scope to adjust to crises using their own policy preferences. As with quotas, issuance of SDRs which was common and large-scale in the 1970s, disappeared during 1981-2009. A large new issue in 2009 multiplied the amount of SDRs by four, and helped many countries overcome the effects of the global financial crisis, but they still remain a tiny fraction of global liquidity.

**Recommendation**: The IMF should increase its lending base by implementing the 14th and 15th General Reviews of Quotas by January 2015, and thereafter increase quotas and issue SDRs automatically in line with growth in world GDP, trade and capital flows. It should also dramatically increase the proportion of its funds available without conditionality to combat “exogenous shocks”, and thereby reduce the degree to which countries are expected to react to these shocks through anti-growth austerity measures.

### IMF Impact Assessment

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<td>Inclusive Growth</td>
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<tr>
<td>Tax Policy</td>
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<td>Government Spending</td>
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<td>Lending</td>
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¹ IMF. Articles of Agreement, Article I, Purpose; International Monetary Fund, (n.d.). http://www.imf.org/external/pubs/ft/aa/pdf/aa.pdf See also notes 5 and 6 below for the role of the IMF in reducing poverty and promoting growth. For a description of IMF lending and policy support relationships with low-income countries, see the 2013 Report.


³ Ibid.

⁴ For more details, see International Monetary Fund - Overview. (n.d.). http://www.imf.org/external/about/overview.htm

⁵ The Report therefore does not assess IMF performance on debt issues, on inflation and monetary policy issues, or on external sector issues – which were assessed in last year’s GFGIR. Though these policies can also have important impacts on inequality, the focus here is on the policies with the clearest and most direct impact on inequality.


⁷ Gini coefficient is the statistical value that represents income inequality. Higher values are associated with higher levels of income inequality.


¹¹ See Action Aid, forthcoming, Reducing Aid Dependence through Revenue Mobilization.


¹³ Oxfam International, Development Finance International and New Rules for Global Finance are currently cooperating on more detailed research into IMF tax policy advice, due for publication in Spring 2015.


This article assesses the quality of governance of the World Bank in light of changes in the past year.

In 2013, the World Bank Group committed to twin goals¹ which guide the Group’s new strategy:² eliminating extreme poverty by 2030 and boosting shared prosperity. The World Bank Group is composed of five organizations, each of them having a specific mission. This article focuses on the World Bank, i.e., the International Bank for Reconstruction and Development (IBRD) and International Development Association (IDA).³

IBRD and IDA’s highest governing body, the Board of Governors, meets annually and its Development Committee meets biannually. The resident Executive Board with 25 Executive Directors meets several times each week. The President chairs the Executive Board and leads Management.

The IBRD gets its capital base from its members and uses this to borrow money on financial markets to on-lend to middle income countries. The profits on these loans and the return from its equity largely fund the operations of the IBRD, including staff salaries.⁴ IDA provides grants and concessional loans for low income countries and some lower middle income countries. IDA is funded through a portion of the profits from loans made by the IBRD and the International Finance Corporation (IFC) and by contributions from donor countries, which meet every three years to approve new funding “replenishments” and new priorities.

In 2009, the World Bank adopted a Policy on Access to Information,⁵ which was revised in 2013. The policy includes a process for making information publicly available as well as an appeals process when someone challenges a document’s inclusion on the exception list. The 2009 reform declassified some 17,000 documents and created a searchable database of more than 100,000 documents.⁶ The Bank also agreed to release more extensive summaries of Board meetings, with the condition of approval by the Board. What the Bank sorely needs now is an adequate search engine to sort through all these materials. Google is the better option for finding information on the Bank website.

Since the 2013 revision of the policy,⁷ verbatim transcripts and statements of Executive Directors may be declassified if their content is not covered by the list of exceptions. Even then they can only be declassified 10 to 20 years after the date of the record.

These reforms are only a small step towards the repeated demands from CSO groups to make Board discussions fully transparent. Citizens remain unable to track the opinions expressed at Board meetings by their own governments.⁸ A policy of disclosure with a regime of exceptions is only half of an ideal transparency policy, which also requires that affected or interested peoples can access relevant information. It also requires proactive translation into relevant languages throughout the decision processes. Now there is only access to final documents. Minimal
Information is available during the negotiation and development of loans. Although this is partly the responsibility of member countries, the Bank should make sure this information is publicly available.

Recommendation: National Parliaments and CSOs must have real time access to information regarding pending loans, and Board meetings should be publicly broadcast, with documents released in advance.

Voting shares at the World Bank Group differ between its constituent parts. IBRD and IDA are basically linked to the capital countries contribute, which in turn, has been the result of a series of ad hoc agreements. At the IBRD each member has a voting power equal to the sum of its basic votes plus share votes. Basic votes give each member an equal share of 5.5 per cent of the total voting power. The share votes therefore represent a full 94.45 per cent of all votes. IDA does not have basic votes; all its voting shares are distributed according to the subscriptions paid into the Bank. Share votes were initially linked to IMF voting shares though this has not been maintained. Over the years capital increases have created the opportunity for some countries to increase their relative share of the Bank and therefore their voting power,⁹ the result of a negotiated process in the Board.¹⁰ Currently, reviews of the Bank’s shareholding and renegotiations of quotas take place every 5 years, rather than on an ad hoc basis.

In 2010, the members of the Bank decided to increase its capital by US $86 billion. According to the Bank the objective of this capital increase, the first for the past twenty years, was to increase the capacity for the IBRD to perform its operations. In addition, a selective capital increase of US $27.8 billion would also reform voting power, with an increased weight for developing countries.¹¹ The Bank claims that this reform brought a 3.13 per cent increase in the voting power of Developing and Transition countries (DTCs), bringing them to a combined 47.19 per cent of voting power. However, the DTC category is itself an historical anomaly not based on any sensible definition of what a DTC is: it includes 16 high income economies. In reality, the reform brings the total voting power of high income economies to almost 61 per cent of the votes, while middle income economies remain under 35 per cent, and low income economies have 4.46 per cent.¹² It is also important to note that the 78 countries eligible for IBRD loans have collectively more than 25 per cent of the voting power.¹³

Those voting shares in the Board of Governors are also reflected in the Executive Board. The five largest shareholders of the Bank – United States, Japan, Germany, France, and United Kingdom - appoint one executive director each. Three countries – China, Russia and Saudi Arabia – elect their own executive director while other member countries are represented in constituencies. Among the 25 directors, 15 come from high-income economies and 10 from middle-income economies.¹⁴ In practice low income countries are represented by EDs from either middle income or high income countries. The consequence is an important imbalance between borrowing and non-borrowing countries in the Board of Executive Directors, in favor of the latter.¹⁵

Civil society groups have also expressed their disappointment with the reform. A coalition of European NGOs has called for equal voting shares for non-borrowers and borrowers as the first stage of a broader reform. They consider that future reforms should be designed to embrace democratic principles and implement the Bank’s mandate.¹⁶

The World Bank Presidency remains a de facto American position, even as the IMF Managing Director is a European position. Both positions should be open to all candidates, regardless of nationality and selected solely on merit. Similarly World Bank staff, especially senior staff, should better reflect the diversity of member countries and a range of training and background beyond graduate degrees in economics from prestigious US and European universities.

Recommendations: The voting power of borrowers and non-borrowers should be equal as a first step towards further reform; the President should be selected from all meritorious candidates regardless of nationality; and Staff should include diverse nationalities and professional preparations.

Accountability Score 2.5 *

*Author's recommended score: 2

According to the World Bank Articles of Agreement, its powers are vested in the Board of Governors. It means that World Bank’s staff and management are accountable
to the member states through their board representatives, themselves accountable to their citizens. However, the fact that voting power is dependent on economic weight and financial contribution to IDA gives greater accountability to those with greater financial investment in the Bank. This model creates a moral hazard problem: since donor countries, holding most of the power, do not borrow from the Bank, they are not accountable to citizens affected by the lending decisions, living in borrowing countries.

Another problem lies in the lack of accountability towards national parliaments. Legislators have limited access to documents regarding World Bank operations in their countries. Requirement of approval of operations by national parliaments and full access to information for legislators would also improve the balance of power between national governments and parliaments as well.¹⁷

While the Bank’s accountability continues to refer back to its member countries’ governments, a framework for CSO engagement exists in the Bank. Most World Bank country offices have staff dedicated to the relations with local CSOs. There are currently 120 World Bank CSO liaison officers around the world.¹⁸ Two units at headquarters support them: the Civil Society Team and the Participation and Civic Engagement Team. Although the Bank has made efforts to improve its engagement with CSOs, many efforts are still needed. On the positive side, the Bank has shown interest to better organize its relations with CSOs through reflection on how to improve those relations,¹⁹ regular review of CSO engagement,²⁰ the development of general guidelines for the consultations with civil society organisations,²¹ and a guidance note for engagement with stakeholders.²² Given the decentralisation of this engagement, guidelines are not always followed and its quality is inconsistent and should be considerably improved, especially in developing countries. During some consultations, CSOs have complained that their concerns are not properly being considered during the process.²³ Despite the existence of guidelines to conduct those consultations, there are no rules that provide minimum procedural guarantees or negotiated agreements on acceptable mechanisms. The creation of a new framework with universal engagement guidelines, monitoring mechanisms and CSO-controlled funding to facilitate CSO engagement would improve the Bank’s engagement with CSOs.

Recommendation: A new CSO engagement framework with universal engagement guidelines, monitoring mechanisms and CSO controlled funding to facilitate CSO engagement.

*Author’s recommended score: 1*

The World Bank has created several mechanisms to improve the accountability of its projects. Although this section focuses on the safeguards policies, currently under review, it is important to mention the existence of the Inspection Panel. The Inspection Panel is an independent recourse mechanism for people and communities who believe they have been, or are likely to be, adversely affected by a Bank-funded project. The World Bank safeguards and its Inspection Panel are the only mechanisms that affected people can use to hold the Bank to account. The World Bank and the regional development banks are the only inter-governmental financial institutions with complaint mechanisms open to affected people. They still fail to provide compensation to injured parties.

In order to appeal to the Inspection Panel, the World Bank—at the insistence of CSO campaigners over the years—has developed environmental and social safeguards policies, now the heart of the Bank’s responsibility to affected people for the impact of its projects. According to the Bank, the objective of those policies – currently under review - is to “prevent and mitigate undue harm to people and their environment in the development process”.²⁴ They provide guidelines for the Bank and borrower staff in the identification, preparation and implementation of programs and projects, including impact assessment.

The current review process of the safeguards policies aims at making them more efficient and effective in the way they are applied and implemented.²⁵ During the review process, CSO groups have expressed their concerns regarding the safeguards policies and wishes for the review’s outcome:

1. the necessity to include development policy loans in the safeguards application;
2. the importance of not weakening the framework (President Kim has committed to no dilution of the safeguards as a result of the review process);
3. more country ownership should not undermine high, common, minimum standards;

4. reinforcement of the impact assessment mechanisms; and

5. improvement of the safeguards policies on specific topics: human rights, climate change, indigenous peoples’ rights, rights of persons with disabilities, rights of children and access to justice.²⁶

The Bank has yet to adopt the reform of the safeguards policies. However, a draft proposal was recently presented by the Bank to its Executive Board.²⁷ CSO groups believe that it considerably weakens the current policies, in an attempt to speed up lending approval.²⁸ The Bank Information Center has developed an analysis²⁹ of the proposal and points out the following:

1. The Bank is proposing a loophole allowing governments to “opt out” of previously guaranteed protections for indigenous people, lowering the accountability of the Bank towards local communities;

2. Despite Bank promises that the reformed safeguards policies would include stronger protections for poor communities and those in “disadvantaged” or “vulnerable” groups, the proposal only contains general mentions of the need to consider impacts of projects on those who may be “disadvantaged” due to age, disability, gender, and sexual orientation or gender identity;

3. Despite assurances made by the Bank that environmental challenges would be adequately addressed in the policies, climate change is absent from the policies in term of impact assessment;

4. Policies protecting biodiversity have also been weakened in the proposal; as well as

5. Proposals to weaken a key protection, the current right of communities to comment early in the process on projects which, if adopted, would have great potential to significantly affect their lives and livelihoods.

Recommendation: The Safeguard Policies should be strengthened in the areas highlighted above, with no dilution of standards.

Overall assessment
In sum, the World Bank has improved on Transparency. For Inclusiveness, the Bank remains dominated by lender countries to the detriment of borrowers. The Accountability of the Bank suffers from the unbalanced voting power at the Boards of Governors and Directors, and the manner of selecting the President. In addition, national parliaments are not adequately involved in decisions affecting their citizens. While the Bank has made efforts to improve its engagement with CSOs, the quality of engagement with CSOs varies considerably. On Responsibility, the reform of the safeguards policies seems likely to undermine the Bank’s framework that CSOs around the world have worked for decades to construct to protect the voice and livelihoods of the poorest while sustaining the environment.
World Bank Governance Assessment

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Governance Gap

41%

* Author recommended a lower score. Editors adjusted score slightly up in order to maintain consistency of assessments across institutions. Criteria was applied more consistently in the 2014 Report as compared to the 2013 Report. This has led to a slight upgrade, as judged by the editors.

³ The new strategy requires the engagement of the International Finance Corporation (IFC) which lends to the private sector, in all country strategy documents. See the World Bank Impact section for discussion of IFC and development issues.
¹⁰ Ibid.


¹⁷ Or, in congressional systems, improve the balance between the Executive and Legislative Branches.


The World Bank’s overarching mission is “a world free of poverty”. In October 2013 its Board of Governors approved a new strategic agenda with two goals:

- Ending extreme poverty by reducing the percentage of people living on less than US $1.25 a day to 3 per cent by 2030; and
- Promoting shared prosperity by fostering income growth for the bottom 40 per cent of the population in every country.

The Bank will fulfill these goals by providing: i) loans, interest-free credits, and grants to developing countries to support a wide array of investments in education, health, public administration, infrastructure, financial and private sector development, agriculture, and environmental and natural resource management; and ii) policy advice, research and analysis, and technical assistance/capacity-building to developing countries.¹ This assessment of World Bank impact places particular emphasis on low income countries (LICs) (though it also lends to virtually all middle income countries).²

In what follows, the World Bank is assessed for the impact on poverty and inequality of its overall goals and their intended monitoring; its resources and the way in which they are allocated and delivered; its policy assessments and policy-based lending; its policies on various sectors and cross-cutting themes; and its private sector activities.

The goals also raise many questions. Why accept that 3 per cent of poverty will be impossible to end - if more could be done to provide immediate social protection to those affected by wars, natural disasters and other exogenous shocks? What will be done to tackle the growing bulge of “very but not extremely poor” earning between US$1.25 and US$2/day? Within the bottom 40 per cent, how will the Bank ensure most benefits do not accrue to those between the 35th and 40th percentiles? Above all, how much faster will the incomes of the bottom 40 per cent rise and to what share of national income? Oxfam and other CSOs are suggesting a goal of their share of national income matching that of the top 10 per cent in each country.

To monitor implementation, beginning on July 1, 2014⁵ the Bank has designed Corporate Scorecards: one for the World Bank Group (IBRD, IDA, IFC and MIGA) and one for the World Bank (IBRD and IDA). Each Scorecard has 3 tiers:

- The Results achieved by clients (borrowing governments) with the help of the World Bank.
The Performance of the World Bank Group as a whole and “World Bank” as IBRD and IDA in implementing the strategy, will “measure both operational and organizational effectiveness.”

How helpful will these scorecards be to future assessments of its impact on poverty and inequality?

Within the World Bank Scorecard, there is need for much greater clarity about the targets set for the Bank and how they will impact on poverty and inequality rather than just producing “outputs”. For example, in the target for miles of roads built, will feeder roads bringing remote rural people and goods to market, be differentiated from toll-motorways to which the poor have no access? Equally, how exactly will the Bank will assess results for gender equity, and for equity within access to and results from education and health?

As discussed in more detail in this Report last year, the World Bank scores highly for the scale of its funding. World Bank Group commitments rose from US$52.6 billion in FY 2012/13 to US$61 billion in 2013/14, largely due to a major increase in infrastructure-related lending. Of this, IBRD represented US$18.6 billion, up from US$15.2 billion, IDA US$22.2 billion (up from US$16.3 billion, continuing to exceed IBRD lending), and private sector US$20.2 billion (down from US$21.1 billion after a major recent increase). However, amounts available for commitment via IDA to low income countries are only US$52 billion. While higher in nominal terms than ever before, this represents only stagnation in real terms, and reflected only very marginal nominal increases in new donor funding.

IDA remains a major actor in official development financing (20 per cent of multilateral and 10 per cent of total flows) and could therefore have a strong influence on setting new rules for development finance. They also remain relatively cheap for countries and therefore minimize the debt-creating impact of borrowing. However, there are three resource issues:

- **Insufficient**: given their massive Millennium Development Goal (MDG) funding needs and preference for disbursements via multilateral institutions, LICs would have liked to see IDA funding levels rise much more. They also opposed the hardening of lending terms for IDA recipients, which was agreed to provide more funds for future IDA lending. CSOs remain somewhat divided on whether IDA should have more resources, with most preferring higher funding for UN agencies and regional development banks, especially in relation to climate change.

- **Poorly Allocated**: as discussed in detail in the 2013 Report, LICs and CSOs have major problems with the system through which resources are allocated, notably the “performance” Country Policy and Institutional Assessment (CPIA). If the Bank is to allocate resources in ways which tackle “harder to reach” poverty, and reduce inequality, future allocations will have to be based much more on needs in terms of poverty and inequality levels, and take more account of country vulnerability to economic, climatic or conflict shocks, resulting in a far higher share of funds going to “fragile states” (only marginal steps have been taken in this direction for IDA 17). The Independent Evaluation Group (IEG) report on 2013 Bank performance shows that IDA programs in Fragile and Conflict-affected States (FCS) out-performed regular IDA-borrowers and were on par with performance of IBRD borrowers, which should encourage the Bank in the direction of higher lending to FCS. The same types of allocation criteria will be needed to tackle the very high poverty and inequality in middle-income IBRD borrowing countries. The CPIA criteria themselves will also need to change dramatically, to place top priority on policy aspects which have been proven to combat poverty and inequality, such as progressive taxation, anti-inequality spending, equality and rights legislation, and decent work objectives. In all these senses they are less fit for purpose than they were last year.

- **Effectiveness**: according to LICs, IDA continues to perform well in terms of channeling its assistance via the recipient government budget; aligning its assistance with priority sectors in national development strategies; programming commitments and disbursements over a multiyear period; untying its assistance from any link to exports of individual countries; and being fully engaged in national and sectoral policy dialogue with countries. Yet they continue to criticize the low quality and capacity-building content of much of its technical assistance; complex and slow disbursement and procurement procedures; failure to channel its support via government public financial management and procurement systems, or to use government-led results tracking systems; its high levels of policy and...
procedural conditionality which delay disbursements; and low flexibility to respond to shocks (with a Crisis Response Window set at only 3 per cent of IDA resources). IDA continues to make efforts to streamline procedures and reduce delay, through greater use of national procurement systems, and decentralization; and to reduce conditionalities, but neither LICs nor CSOs see these as bringing fundamental change at country level.

**Recommendation:** the World Bank should aim for a real terms increase in the next IDA replenishment, in return for demonstrating that it can comprehensively revise its allocation system to be based on anti-inequality/poverty policies and needs, and dramatically improve effectiveness by using country systems and reducing conditionality sharply.

**Macro Policy**

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It is extremely hard to assess World Bank impact on poverty or inequality. Unlike the IMF, it has been very little involved in designing the macroeconomic framework in LICs in recent years, and lends to virtually all LICs, so it is hard to ascribe major macroeconomic impacts to World Bank projects or to compare countries with and without World Bank programs. The Bank has also conducted very little in-depth analysis of how its policy recommendations, programs and projects are impacting on these issues, and the IEG does not conduct institution-wide assessments of Bank activities on poverty or inequality outcome. However, the Bank in common with the broader donor community has seen acceleration of growth and reduction of poverty in most LICs, but much less progress on inequality.

The Bank has already indicated that for this to happen, it will need to pay much more attention to the distributional consequences of tax and spending policies (in cooperation with the IMF), as well as providing policy advice on social protection, job creation and financial inclusion to fight against inequality. However, in all of these areas its previous policies have been lacking in focus on tackling the key problems facing the poorest, in terms of:

- assisting with comprehensive social protection floors and investing in country systems and capacity, as opposed to topping-up targeted schemes for small groups (such as in-kind transfers, public works or school feeding programs);¹⁰
- decent work and employment and promoting higher minimum and living wages, job security and union rights; and
- ensuring that the poorest have equal access to financing rather than just being “included in” the financial sector.

An equally important issue is whether the Bank’s systems for assessing country policies, and the design of its policy conditions in its policy-based lending, are likely to achieve the goals of ending poverty and reducing inequality. As already analyzed above, the CPIA seems very inadequate for this purpose.

The “Doing Business” assessment of the private sector “investment climate” is also a crucial system, used not only to design World Bank Country Policies and policy-based lending conditions, but also by many other donor organizations in their policy and private sector work. It has been highly criticized by civil society for its focus on reducing numbers or levels of corporate taxes, and promoting “flexible” labor markets by minimizing labor protection and abolishing or reducing minimum wages. More details of how Doing Business damages worker protection are provided in Box 1. However, plans for a fundamental review of the assessment system in 2013-14, including consultations with LICs and CSOs have not been fully pursued, and the Doing Business 2014 report continues to use the same criteria: the only change has been that the Employing Workers indicator is no longer included in the aggregated summary index.¹¹ The focus on reducing corporate taxes also seems to be increasingly at odds with IMF recommendations in countries and its Spillovers report¹² about the need to avoid a “race to the bottom” in corporate taxation.

**Recommendation:** the Bank should comprehensively revise its policy assessment systems (CPIA and Doing Business), its Country Policies and its policy-based lending conditions to prioritize policies which will reduce poverty and inequality, notably progressive taxation, anti-inequality public spending including comprehensive social protection floors, and enhanced labor rights and wages.

**Sector Policy**

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**Education and Health:** LIC governments and CSOs welcomed the renewed commitment to universal education and health care by the new Bank President during 2012-13, and some of the President’s own speeches in which he emphasized that user fees for such services
should be eliminated or minimized to avoid excluding the poor. Yet education and health user fees continue within the poorest countries, as evidenced by a 2014 IDA education loan document for Sierra Leone. While the government abolished school fees, the costs of uniforms, books, supplies and “off the payroll” teacher fees continue to keep the poorest rural children from school. There is a need for an even stronger public commitment to free universal education and health for all, with this being prominent also in the assessment of country policies and country strategies: this would be a powerful influence on the whole donor community, given that the Bank is the world’s largest provider of “funds and expertise to education.”

The Bank needs also to be even clearer in its views on the relative desirability of public and private sector provision: CSOs and education/health experts have been highly critical of some proposals made by the Bank (and actions taken by the IFC) for delivering these goals through the private sector, on the grounds that they are typically less cost-effective and exclude the poorest, undermining equity and rights to education and health.

Agriculture. As is true of many other donors, it is not clear that the World Bank is placing enough focus on promoting the incomes on smallholders and poorer rural citizens, rather than enhancing production through larger farms.

THE WORLD BANK’S DOING BUSINESS AND WORKER PROTECTION

The World Bank’s Doing Business report, an effort to rank countries according to whether or not they have adopted business-friendly regulations, has been controversial since its launch eleven years ago. It has been criticized for encouraging governments to compete in rolling back worker protections, while penalizing governments who attempt to augment their taxes on business to pay for social protection and other needs. This is an especially alarming policy stance for the World Bank to take in low-income countries, the majority of which struggle with inadequate de jure and de facto worker protections and low tax collection rates.

In 2012, World Bank President Jim Kim appointed an expert panel, headed by former South African minister Trevor Manuel,* to review the appropriateness of the normative standards by which the report’s indicators judge countries as well as other aspects of its methodology. In the wake of an intensive public lobbying campaign by representatives of multinational business interests and proponents of free market ideology, President Kim adopted few of the recommendations for comprehensive reform delivered by the panel in June 2013.

Doing Business does not measure factors that might be particularly important to combating poverty and inequality in a low-income country — the adherence to the International Labor Organization’s core labor standards including the effective recognition of the right to collective bargaining, the elimination of forced labor, the abolition of child labor and the elimination of discrimination in respect of employment and occupation.

The report also does not measure important minimum worker protections in the areas of maternity or personal needs, access to social security, or occupational safety and health.

Instead, Doing Business has focused government attention exclusively on the ease with which employees may be terminated, keeping minimum wages at a low level, and ensuring that weekly rest, holiday with pay and limits on hours of work are not “excessive.” The labor indicator was suspended in 2009 because of strong criticism, but the report continues to publish data for the indicator in an annex. The Doing Business team claims that its normative standards in these areas do not penalize a country that complies with minimum standards contained in ILO conventions governing these areas, but the ILO itself has never endorsed this interpretation of its conventions.

Alarmingly, the Bank is moving to include the Doing Business indicators in its new Strategic Country Diagnostic process, thus setting the stage for them to be used as a template for setting Bank priorities when negotiating the Country Partnership Frameworks. This will pressure countries to adopt anti-labour regulations if they wish to borrow, and is a step in the wrong direction from the advice given by the panel of experts in 2013.

Peter Bakvis and Pamela Gomez,
International Trade Union Confederation (ITUC)

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This position is supported by the Bank’s own research, which argues against the Bank facilitating foreign investment in large tracts of farmland already in use by small farmers.¹⁶ This issue has been particularly confronted in the last year by the issue of large farms “grabbing land” from smallholders. On this, the Bank has public restated its commitment to voluntary UN guidelines, but it is not clear this will be reflected in operations by being adequately treated in revised safeguards, IFC supervision of the behavior of financial intermediaries, or in improved land acquisition contract transparency.

**Gender:** There is generally seen to have been some progress on “gender mainstreaming” and monitoring gender impact of Bank projects over the last decade. However, there is not nearly enough analysis of gender impact of country strategies and operations, or emphasis on measuring the achievement of project gender equality objectives and collecting gender disaggregated data. In addition, the Bank needs to do much more on maternal health care, on women’s economic empowerment, and on gender-based violence, and to make its policies, strategies and projects respond to women’s needs and rights, especially in providing high-quality jobs.¹⁸ Some of the current gender assessment tools are also seen to be inadequate, notably the self-assessment form for deciding whether a project is “gender-informed”.¹⁹

**Climate Change:** The Bank has been seen by LICs and CSOs until recently as insufficiently committed to combating climate change in its actual lending policy, continuing to make large investments in fossil fuels and not routinely assessing its projects and programs in depth for their potential impact on climate change. However, this appears to have been changing somewhat in 2013, with much greater focus on mainstreaming climate change, disaster risk management and low-carbon development in IDA countries, and an announcement that it will in general avoid financing coal projects.²⁰

**Recommendation:** The “One Bank” should strengthen its education and health policies and operational guidelines to ensure universal, free and publicly provided services are the priority for the World Bank and IFC. It should reorient its agriculture policy to focus on support for smallholders and poorer rural citizens, dramatically reinforce its work on gender and ensure combating climate change is fully mainstreamed in all operations.

Our assessment of World Bank Group engagement with the private sector, mainly via the International Finance Corporation (IFC) has not changed since 2013. A primary goal of IDA’s strategy for the next few years is to “leverage” greater private sector resources for development, given that its own funds will be stagnating or falling in real terms, and therefore the Bank could potentially have a massive impact on encouraging the private sector to combat poverty and inequality.

Nevertheless, there is so far little sign of such a change. According to LIC governments, CSOs and the IEG, IFC facilities remain too tailored to wealthier countries with better capacity to access funds, insufficiently differentiated according to country circumstances, over-concentrated on highly profitable sectors such as mining, petroleum, tourism and finance rather than manufacturing or agriculture,²¹ and too often partnering with large transnational investors.²² The IEG, CSOs and independent analysts have also pointed to its very limited impact on poverty,²³ and a “steep decline in performance” of its investments in the poorest countries.²⁴

Indeed, many have suggested that “the IFC follows a different logic and procedures that make its work largely incompatible with Bank operations. Though the IFC uses poverty alleviation rhetoric, its main driver is return on investments in private enterprises”²⁵ As discussed last year, IFC has also been criticized (including by IEG and the World Bank ombudsman) for its failure to track the environmental and social impact of its interventions, notably those which operate indirectly via financial intermediaries such as banks and investment funds. This is because it relies on client self-assessment and very limited reporting, which has been repeatedly criticized and downgraded by the IEG for being less reliable, accountable or transparent, for example on how net effects on employment levels (including second order impacts) are assessed.²⁶ IFC has never assessed the distributional impacts of its work.²⁷

Criticism has continued to grow from CSOs of the IFC’s growing move into public-private partnerships or private financing for what have previously been mainly publicly-funded infrastructure and social sector investments. These types of projects have long been demonstrated to be much more expensive and risky than public sector funding such as bonds, reducing revenue flows to
government, and risking crowding out other essential government spending or increasing debt burdens. In the social sectors, they can easily undermine the impact on the access of the poorest to services (education, health, low-cost housing, water and sanitation) and education — and IFC tracks only the overall impact of projects on access to services, not their impact on the access of the poorest.²⁸ The 2012 IEG report on the “Results and Performance of the World Bank Group,” showed that Bank effectiveness was lowest in infrastructure and public-private partnerships.²⁹

To reverse this logic, it has been suggested that the IFC should reform its business plan to set targets for funding small, medium and micro-enterprises; businesses owned by local entrepreneurs; businesses owned by women; and businesses in sectors which will have most impact on the employment and incomes of the poor (such as smallholder agriculture, manufacturing); and its Development Outcomes Tracking System (DOTS) to focus less on financial returns, and more on tax revenues generated and decent jobs created.

Two other areas in which the World Bank has not acted significantly to improve private sector behavior:

- Maximizing tax collection. It could for example insist that it would not do business with corporations which are based in tax havens, fail to report all their accounts disaggregated by country, or fail to pay full tax in host countries on projects they are executing with IFC funding.
- Maximizing decent job creation. It could set standards such as ensuring that all jobs in Bank-funded projects meet decent work criteria, including reasonable job security, living wages, and opportunity to join or organize unions.

Overall, World Bank continues to be doing little to promote new rules for private finance.

**Recommendation:** The World Bank should be a leading actor encouraging the private sector to help combat poverty and inequality. Its private sector operations should therefore focus on funding the businesses which will have the most impact on the lives of the poor, and be judged for their success in generating decent work and tax revenue.

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**World Bank Impact Assessment**

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<td>Sector and Thematic Impact</td>
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² Future editions of GFGIR may also examine World Bank technical assistance, research and statistics.
³ The Bank is about to announce a new strategy at the October 2014 Annual Meetings, and next year’s 2015 Report will assess the adequacy of that strategy.
⁴ http://www.brettonwoodsproject.org/art-572637
⁵ The World Bank Group includes the International Bank for Reconstruction and Development (IBRD), the International Development Association (IDA), the International Finance Corporation (IFC), and Multilateral Investment Guarantee Agency (MIGA). World Bank refers just to the first two: IBRD and IDA.
⁶ World Bank Group, World Bank Group/W Bank Corporate Scorecard, April 2014, p. 1. Staff working on the Scorecard claim that the Scorecard is a management tool, not appropriate for impact assessments. However, the IDA websites refers only to the Scorecard under a link called “Measuring Results.”
⁹ Ibid.
¹¹ http://www.brettonwoodsproject.org/art-572701
¹⁹ The most comprehensive and authoritative reporting on IFI gender issues is done by Gender Action, a civil society organization headed by Dr. Elaine Zuckerman. Gender equity is one of the key indicators in the Corporate Scorecard launched in April 2014 to monitor and evaluate both the World Bank Group and the World Bank (IBRD + IDA). See for example: Claire Lauterbach and Elaine Zuckerman, “Assessing the effectiveness of World Bank investments: The gender dimension.” WIDER Working Paper No. 2013/017, March 2013. At p. 15 there is a copy of the World Bank document used for scoring whether or not a Bank Project is “gender informed.” Ticking one of three boxes makes it so. http://www.genderaction.org/publications/assessingeffectiveness.pdf
²² For an example of this see the LIC communiqués cited in footnote 14 above.
²³ http://www.brettonwoodsproject.org/art-572001
24 IEG “World Bank Results and Performance 2012”
25 Mundy and Menashy, p. 33.
26 Ibid., footnote 17.
27 See also Mundy and Menashy at p. 29.
28 For more details on this, see Oxfam International, A Dangerous Diversion, at http://www.oxfam.org/en/research/dangerous-diversion; and
29 http://www.brettonwoodsproject.org/art-572003;
As discussed in last year’s report, three international organizations—the OECD, the IMF, and the UN Tax Committee—all claim leadership of the international tax “system” - and where everyone is in charge, no one is in charge. Last year we assessed all three organizations, and found poor average results, especially for inclusion and responsibility. This year we focus on the organization which has most recently been mandated to lead reforms on international tax issues (the OECD).¹ We then contrast this with governance by a much more desirable potential World Tax Authority under UN auspices.

For decades international tax rule-making has been dominated by the Organization for Economic Cooperation and Development (OECD) member states, which have shaped rules to suit their interests and those of the transnational companies originating from OECD countries. In 1956 the Committee on Fiscal Affairs (CFA) of the Organization for European Economic Cooperation (OEEC), forerunner to the OECD, took it upon itself to manage the rule-making processes required for international tax cooperation. As cross-border investment increased in the 1960s, the OECD took the lead in promoting a ‘soft law’ approach based on its non-binding multilateral model convention and other policy advice. Almost every tax treaty in existence today is based on the OECD’s model convention. It has also been given responsibility since 2000 by the G8 and more recently G20 for strengthening implementation of global standards on transparency and exchange of information for tax purposes (since 2009 through a Global Forum on Transparency and Exchange of Information for Tax Purposes), and for addressing tax avoidance through “Base Erosion and Profit Shifting” (BEPS) ² (2013). Despite the claims made for it (the OECD and G20 have described the Global Forum as “the premier international body for ensuring the implementation of the internationally agreed standards of transparency and exchange of information in the tax area”) the Global Forum has achieved only modest tangible success in a very small part of the global tax agenda.

In terms of its procedures, the OECD is relatively transparent. Research and policy papers are generally announced ahead of time. However, non-member-governments and civil society seem to have only limited opportunity to participate in the generation of papers; the for-profit private sector seems to have greater access and influence. Draft documents are not public, nor are public comments solicited. In turn, the Global Forum itself seems to be transparent in its agenda and meeting announcements, as well as in annual reports and other documents prepared for its meetings.

In terms of the OECD’s success in promoting policies to encourage global tax transparency, until recently most of its work has focused on promoting bilateral Tax Information Exchange Agreements (TIEAs) which provide information ‘on request’, a model that has proved almost wholly impracticable as a tool for detecting or deterring tax evasion. This is in part because they were designed with forthright participation by secrecy jurisdictions, and therefore became non-binding instruments whereby
Governments can request information about their citizens, but must specify the name of the individual, the institution within the tax haven, and the nature of the “offense.” Since tax havens cooperate in hiding the identity of the “beneficial owner,” such treaties rarely provide information leading to prosecutions. This is why since 2013 the OECD has been charged by the G20 with developing a new standard for automatic exchange of information (see Box 2).

Formal membership of the OECD currently covers only 34 countries. It engages with an addition 88 states through the Global Forum, and has striven to recruit more states to counter claims that the UN’s universal membership makes it the only legitimate political forum for agreeing international tax standards. However, only 18 of these states are low- or lower-middle income developing countries, and only two such countries are represented on the 18-member steering group of the Forum. In addition, the Forum is only consultative, and discusses only a small part of the global taxation agenda. Decisions on new standards are taken only by the OECD members. As a result, it remains very poor in representing the smaller and less wealthy global economies, though the OECD has announced that it has consulted 140 countries so far and plans “an enhanced engagement strategy” with these countries in finalizing and implementing the BEPS recommendations.

In terms of staff diversity, the Global Forum’s Secretariat is staffed by both OECD and non-OECD personnel. However, it remains part of the OECD secretariat, answerable ultimately to the OECD Secretary-General. In addition, the agendas and papers for meetings of the OECD Committee on Fiscal Affairs, which takes decisions, are prepared by the OECD secretariat Centre on Tax Policy and Administration, staffed entirely by OECD member state personnel.

The OECD actively engages with civil society through its Tax and Development Taskforce, but – as was noted in our 2013 assessment – some participating not-for-profit organizations continue to express frustration that their interventions are not heeded while those from the for-profit private sector, and from representatives of tax havens that are, or are politically related to, OECD member states strongly influence the eventual outcomes. The cost of participating in OECD events also inhibits civil society representation, and some developing country governments have also noted the high cost of engagement with the many ongoing events and fora.

### Accountability

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Given the decentralized, ad hoc nature of international tax rule-making and implementation, there is no overarching mandate or firm accountability framework for monitoring outcomes and results of tax-related undertakings, beyond delivery of reports to the G20 by the OECD and other international organizations, and OECD-organized monitoring of adoption of model tax conventions and compliance with tax information exchange and transparency standards.

Equally, there is no structure or regular process established for evaluating the impact of international tax rule-making policies and implementation on country economies, either within the OECD or for a broader group of countries. The nearest to performing this function is ex post research by the IMF on tax policy impact, and evaluations by the IEO of fiscal adjustment policies recommended by the IMF.

The OECD has its own internal procedures for selecting the Secretary-General – though this has produced reasonable diversity among member states, it is not a public or fully transparent process. As with the Bretton Woods Institutions, there are no regular independent evaluations of the performance of the Secretary-General, or the Director of the Centre for Tax Policy and Administration. There are in-depth evaluations of committees, including the Fiscal Affairs Committee; but it is not clear how frequent these are, nor have they been published. There is no publicly available evaluation of the performance or impact of the Global Forum.

### Responsibility

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The OECD has no formal procedures for receiving and processing complaints from those affected by its tax policies or standards, nor for compensating those harmed. In addition, it very rarely assesses ex ante the implications of its recommendations, especially for low income countries and for inequality/poverty within those countries.
Governance & Impact Report 2014

The UN Committee of Experts on International Cooperation in Tax Matters was given Committee status under the UN’s Economic and Social Council (ECOSOC) in 2003, following a recommendation of the UN International Conference on Financing for Development (Monterrey, Mexico, 2002), and springing from a longstanding UN Fiscal Committee. Committee members are nominated by UN member states to serve in a personal expert capacity for five years, with the UN Secretary-General selecting 25 experts from government nominations. For decades the experts have been disproportionately from OECD states, and many independent observers have noted that OECD experts tend to act as a bloc.

The Committee and its predecessor have suffered for decades from insufficient finance and personnel, and lack of political status. As a result, the Committee meets only once a year for 5 days. Attempts in recent years to strengthen UN work by establishing a standing inter-governmental commission on international tax cooperation have been considered by ECOSOC, but have not received support from the OECD countries. In practice, the UN’s most important contribution to international tax rule-making has been a UN model double tax agreement, which despite being largely based on the OECD standard, does allocate stronger taxing rights to developing countries that receive foreign investment (“source countries”).

It has become evident that the lack of functional and just rules on international tax, for taxing corporations and tackling tax havens of globalized markets, has dramatically diminished the power of elected governments to design equitable and progressive tax regimes, and seen a regressive shift of tax contributions away from capital onto labor and consumers, resulting in deeper inequality, erosion of social and political stability, and reduced employment opportunities. In an era when national tax regimes are highly interdependent, meaning that the tax policies of one country have “spill over” impacts on policy choices of other countries, there is an urgent need for a single rule-making body dedicated to enhancing international tax cooperation, and with a mandate to tackle international tax evasion and avoidance, and prevent tax wars. The organizations currently working on international tax policy lack a proper mandate, and either are unaccountable to the rest of the world (OECD/Global Forum), or have insufficient political authority to agree new rules (UN Tax Committee). The challenge facing the international system is to devise and implement an effective and legitimate governance response.

In the same way that the World Trade Organization set the rules for international trade, a World Tax Authority is needed to monitor the impacts of fiscal policies on trade and investment patterns, and to protect national tax regimes from the harmful practices of tax evasion and avoidance, as well as tax wars, and promote efficient and effective tax administration, and progressive tax policies. In 1999, former director of fiscal affairs at the IMF, Vito Tanzi, proposed that the prime function of such an organization should be to ‘make tax systems consistent with the public interest of the whole world rather than the public interest of specific countries.’

The most appropriate body to take on the functions of a WTA would be the United Nations, as an evolution of its Tax Committee. Among the priority tasks for a WTA could be to:

- Work with international accounting bodies to define a common basis for determining profits and taxable income;
- Help set rules for unitary taxation and allocating the profit income of transnational companies;
- Assist international exchange of taxation information;
- Help to protect national tax regimes from tax wars between states and establish dispute reconciliation procedures;
- Collate relevant statistics and act as a forum for discussion and sharing of best practices.

These tasks are essential in the interests of tax justice and would reinforce the autonomy of sovereign

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**BOX 1: THE CASE FOR A WORLD TAX AUTHORITY**
states, which has been seriously eroded by the current rules. A WTA could also carry out the task of recommending best practice standards in creating tax law, leaving the IMF and World Bank to disseminate best practice. This would make possible the establishment of an international benchmark for the achievement of tax justice against which progress could be monitored.

Finally, based on the GFGIR governance criteria, a UN-housed WTA would be clearly preferable to current arrangements.

- The UN tax committee is already highly transparent, with agendas, papers and decisions available online. There is no reason to believe this transparency would decline with the establishment of a formal agency.
- A UN body would be highly inclusive and open to all countries of the world – though of course a representation system for different constituencies would be needed to reduce the number of seats at the table. Its staff would be highly diverse, and its proceedings (following best practice of some UN agencies) could be open to civil society participation.
- Almost all UN bodies have accountability frameworks, as well as independent evaluation agencies.
- Most UN agencies have clear responsibility structures such as complaints procedures and compensation arrangements, and the best also conduct extensive ex ante analysis of the potential impact of their policy recommendations.

### Tax Governance Assessment

<table>
<thead>
<tr>
<th>Governance Element</th>
<th>2013</th>
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</thead>
<tbody>
<tr>
<td>Transparency</td>
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<tr>
<td>Accountability</td>
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<tr>
<td>Inclusiveness</td>
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<td>7</td>
</tr>
<tr>
<td>Average Score</td>
<td>1.5</td>
<td>1.8</td>
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</tbody>
</table>

**Governance Gap**: 56%
¹ This is because IMF governance has already been assessed in the IMF chapter, and the IMF’s role has largely been limited to advising individual countries on tax policies and administration, and providing research and statistics; and because the UN Tax Committee has little current influence and would not differ substantially in its governance arrangements from the proposed WTA.

² For detailed information on BEPS see: http://www.oecd.org/tax/beps.htm.

³ See http://www.oecd.org/tax/transparency/membersoftheglobalforum.htm for a list of the 122 forum members.


⁶ The recent OECD reports to the G20 on the impact of BEPS in low-income countries represent a small step in this direction – a mid-course attempt to assess potential impact on low-income countries and how they can be assisted to implement the BEPS action plan. They are available at http://www.oecd.org/ctp/oecd-and-g20-pursue-efforts-to-curb-multinational-tax-avoidance-and-offshore-tax-evasion-in-developing-countries.htm
Because there is no organization clearly governing international tax policy, or attempting to coordinate and set standards for national tax policy, there is no clear “mandate” which can be quoted for tax rule-making bodies and to which they can be held accountable. We therefore assess them on five criteria which developing countries, independent analysts and civil society organizations see as essential to reducing inequality and poverty: 1) fighting illicit flows and tax evasion; 2) reducing scope for legal tax avoidance; 3) combating tax wars; 4) effective and efficient tax collection; and, 4) progressive tax policy.

Official data on the scale of illicit financial flows are scarce, but one report by a New York-based economic investigation agency in 2012 estimated that private wealth of US $21-32 trillion is held offshore, escaping domestic taxes in the owner’s countries of residence.¹ The income tax losses from these sums are estimated at US $270 billion annually, which would go a long way to plugging the budget deficits of many countries. But this figure underestimates the gravity of the situation since it only applies to income tax, and ignores evasion of capital gains, inheritance, and wealth taxes. Imposing wealth taxes on this vast hoard, as proposed by economist Thomas Piketty,² would significantly reduce the extremes of inequality that have built up over the past 35 years.

These kinds of sums do not easily fit in suitcases:³ facilitating illicit flows of this scale involves a large and sophisticated financial infrastructure of compliant banks, law firms and other financial intermediaries. It also requires supportive offshore jurisdictions willing to furnish the environment of permissive laws, lax regulations and weak compliance practices that will shield the identity of the owners. Such places are known as secrecy jurisdictions: the relative scale of the abuses they permit (i.e., the degree of secrecy they allow) is assessed by the Tax Justice Network’s Financial Secrecy Index.⁴

There is a lucrative global market in providing financial secrecy, and a large private sector “pinstripe infrastructure” of enablers and intermediaries -- banks, accountancy firms, boutique law practices, and trust and company administrators -- has embedded itself in secrecy jurisdictions to facilitate individual and corporate tax abuse. Contrary to popular perception, not all secrecy jurisdictions are politically isolated tiny islands in the Caribbean or Alpine principalities. According to IMF data, in 2012 Britain and its satellite jurisdictions⁵ controlled 24 per cent of the global market of offshore financial services; the US (notably states like Delaware, Florida, Nevada and Wyoming which have highly secretive legal structures) 23 per cent; Luxembourg 12 per cent; and Switzerland, which has earned international notoriety for its banking secrecy and permissive tax regime, only 5 per cent.⁶ In other words a huge proportion of the global potential destinations for illicit financial flows, are controlled by powerful countries that dominate the policy processes of both the IMF and OECD.

Secrecy enables concealment of a wide variety of corrupt practices, including fraud, embezzlement, illicit political funding, insider dealing, market rigging and bribery – as well as tax evasion and tax avoidance. It enables powerful players to secure undisclosed special tax treatment, and creates a criminogenic environment by blocking investigation, prosecution and recovery of stolen assets.⁷ It distorts markets by shifting investment and financial flows away from where they will be most productive towards whichever jurisdiction supports tax evasion, or has the most lax regulation or criminal laws. It encourages
rent-seeking behavior by allowing insiders to reap gains from global markets while shifting costs and risks to others. This creates a world of higher risk, rampant crime and impunity, which means that secrecy jurisdictions play a key role in fostering and fuelling global financial crises, serving as cross-border transmission belts for shocks and contagion.

The most effective ways to tackle illicit financial flows involve requiring public disclosure of the ownership and control of offshore legal structures (companies, foundations, trusts, etc.), full international cooperation on information exchange, and improved accounting rules to require transnational companies to report on a country-by-country and project-by-project basis. The OECD has recently been given a lead role by G20 in trying to tackle illicit flows and tax evasion. Its proposals have gone part of the way to increasing disclosure by making country-by-country information exchange automatic among tax authorities (see box 2 for details).

**BOX 2: LIMITED PROGRESS ON INFORMATION EXCHANGE: THE ATIE PROPOSAL**

In February 2014, following a request from the G8 a year earlier, the OECD presented its report and recommendations for a new global standard for automatic tax information exchange (ATIE). The very fact of this report being prepared represents progress away from the OECD’s previous attachment to bilateral Tax Information Exchange Agreements using the “on request” model (see text for analysis of these). The content of the proposal also provides potential for significant progress on information exchange and transparency.

The OECD’s proposal for ATIE defines a wide scope for sharing information. It covers individuals, entities (including foundations and trusts, with special reporting provisions for all-important discretionary trusts⁸) and persons controlling passive non-financial entities. However, the effectiveness of this broader scope still relies on comprehensive beneficial ownership information being collected and shared in registries of trusts and shell companies. If adopted, this measure will represent a significant step forward towards greater transparency, though ownership information, including the identity of settlers and trustees of trusts, needs to be available on public record to deter potential abuse of offshore trusts.

The OECD report proposes two main innovations:
- a Competent Authority Agreement (a model agreement to be signed by jurisdictions willing to implement the ATIE standard together); and
- Common Reporting Standards providing minimal common rules to be followed on reporting content, and “due diligence” that certain financial institutions must conduct.

Both proposals could enhance transparency and cooperation between tax authorities, though concerns have been raised about the ease with which tax havens could block developing countries from participating in a multilateral Competent Authority Agreement.⁹

Overall, the OECD’s proposals for a standard for a multilateral ATIE standard represent a positive step towards improved transparency. However, the proposed ATIE model is intended by the OECD only to complement rather than substitute for “on request” TIEAs. In addition, critics have expressed concerns that the OECD’s proposals are designed in ways that will present barriers to effective participation by developing countries (requirements for reciprocity on information sharing, for example, could impose inhibitive costs on some countries). In addition, the proposal also leaves significant loopholes ripe for exploitation, such as the exclusion of a variety of secrecy facilities (e.g., safety deposit boxes, freeport facilities, and related storage mechanisms) which could encourage wealth hoarding of art objects, large denomination bills and similar mobile assets. Finally, on the negative side, the absence of provisions for sanctions is unlikely to encourage secrecy jurisdictions from continuing to block or hinder information exchange processes.
Recommendations: The ATIE proposal should be strengthened to make information public, be extremely clear that offshore trusts will be included on public registries of ownership, close remaining loopholes, provide for sanctions against non-compliant jurisdictions, and include intensive measures to assist developing country implementation.

Tax rules in most countries are highly permissive of tax planning that enables transnational corporations (TNCs) to shift profits from either the source countries where they extract most basic commodities and profits, or the home countries where they are effectively taking their decisions, to offshore tax havens. The largest corporations and wealthiest individuals have the wealth and will to hire armies of lawyers and accountants to hide their wealth from national tax collectors, and to provide a patina of legality for their stratagems to avoid tax. Some corporations maintain it is their responsibility to “their shareholders” to minimize tax payments.¹⁰ In most countries, lobbyists are paid by interested parties to meet ministers, parliamentarians and officials in order to support loopholes or tailored concessions for specific interests, or to block the closure of such loopholes.

Much of the attention to this issue in past decades focused on the practice of “transfer pricing,” whereby multinational corporations over- or under-charged different branches of their structures for goods or services supplied, in order to shift profits to lower-tax jurisdictions. The UN and OECD both devoted much attention to producing analysis and training materials to help developed and developing countries combat transfer pricing, but the OECD used an “arm’s length” method for calculating transfer prices which has proved impracticable in most circumstances. However, over time tax avoidance practices have become much more complex and multifaceted, including, for example, lending and repaying large amounts within companies to reduce tax burdens; charging unjustified licensing or other fees to affiliates; or claiming that internet-based sales took place in low-tax countries. In recent years pressure from civil society organizations and increased public awareness of the inadequacy of measures to overcome these avoidance measures, has led the G20 to commission the OECD to re-write the rules to enhance international cooperation against “base erosion and profits-shifting” (BEPS).

The OECD has in September 2014 produced its recommendations on the first 7 of 15 elements it was asked to tackle by the G20. They include action to avoid multiple deductions for a single expense, prevent the abuse of tax treaties, address transfer pricing issues, tackle the challenges of the digital economy, countering harmful tax practices, and developing a multilateral instrument which can be used to amend bilateral tax treaties. Its report on the impact of BEPS in low-income countries and the IMF report on tax spillovers have identified several areas which are not adequately covered by the current process, notably tax incentives, bias in tax treaties, and avoidance of tax on merger and acquisition activities. Some of these have been referred to the international organizations for further work, by the G20 Finance Ministers meeting in Cairns, but it is not yet clear how many of the OECD recommendations will command political consensus and be adopted by the G20.

However, it is hard to avoid the conclusion that much more fundamental measures will be needed to make a serious dent in corporate tax avoidance (let alone tax avoidance by high net worth individuals which has not been the subject of any significant work). These should ideally include the adoption of general anti-avoidance principles in national tax laws, making any transaction carried out primarily for tax reduction purposes irrelevant in calculating a company’s tax burden; and ensuring much greater clarity on where taxes should be paid by using unitary taxation calculations with taxes apportioned to countries on the basis of a formula taking account of employment, physical assets and production, and sales, as is already used among states within the US.

Recommendation: The BEPS discussion should be broadened to focus on reducing tax incentives sharply, ending bias in international tax treaties, and applying taxes to merger and acquisitions. Countries should be encouraged to introduce general anti-avoidance principles in national tax laws, and to use unitary tax calculation formulas.

The OECD and other international organizations have done virtually nothing to stop competitive “tax wars” among OECD countries (or developing countries). Over the 15-year period 1997-2012, corporate tax rates fell by almost 10 per cent in the world’s most populated countries, and 8 per cent in smaller countries. Income tax
rates also fell, as did the progressivity of different direct tax bands requiring wealthier corporations and individuals to pay more. Countries also engaged in tax wars which tried to minimize taxes on capital and wealth, and on the most profitable sectors such as natural resources, tourism and financial institutions (including through the provision of massive tax holidays or exemptions). All of these trends placed more strain on public finances in terms of balancing budgets, as well as transferring tax burdens within countries increasingly onto direct taxation of the less wealthy, and regressive consumption taxes. To a considerable degree these trends have been produced by a belief that “tax competitiveness” enhances foreign and domestic investment, even though there is precious little evidence to support this. Some of these trends may be beginning to moderate, with some OECD and developing country governments recently coming to power pledged to increase direct taxes, and some advice being given by the IMF and others to regional bodies to resist tax wars among their members. Yet too often the advice given to countries by international organizations remains that they should make high tax rates closer to the average of some comparable group of countries, and less attention is paid to excessively low rates.

Another form of tax war has been waged through bilateral tax and investment treaties. The rising economic dominance of transnational companies during the twentieth century drove countries around the world to conclude bilateral double tax agreements (DTAs), primarily for the purpose of avoiding taxing corporations twice and deterring investment flows. However, as already discussed, the typical bilateral treaty, based on the OECD model, gives preference to taxation in the headquarters country of the company rather than in the countries where it sources most of its raw materials, labor and profits. Bilateral treaties have been used as a key mechanism to deprive low-income countries of tax revenues. Worse still, in extremis due to failure of treaties to tackle risks of double non-taxation, and “treaty-shopping” – corporations looking for the worst combination of treaty rules, low tax rates and tax havens/secrecy increasing numbers of corporations are managing to declare their headquarters as being in (or earn most of their taxable income in) countries where they pay little or no tax. As an example of this, the Dutch Centre for Research on Multinational Corporations (SOMO) said in 2013 that “the use of the Dutch tax system by multinational companies had cost €771 m in annual lost tax revenue for 28 developing countries.”¹¹ This evidence was used for a successful campaign to convince the Dutch government to revise its treaties, but treaties are not changing dramatically in other countries – even though developing countries have repeatedly highlighted this as a crucial priority if they are to increase revenue collection. The OECD has included in its BEPS package some measures to avoid corporations escaping tax obligations entirely due to treaties, or engaging in excessive “treaty-shopping.” And, G20 countries need to go a great deal further in fundamentally revising treaty models, and in discouraging member states from exerting political pressure on poorer countries to provide tax exemptions for their TNCs.

**Recommendation:** There is need for urgent action to combat tax wars, by providing a stronger analysis and global consensus agreement on equitable and efficient tax levels. The OECD and home countries of TNCs need to revise their treaty models to favor taxation in “source” countries, and end political pressure for tax exemptions.

In terms of developing country tax collection systems, it has been the IMF and aid for technical assistance support, and more recently information-sharing and regional cooperation efforts organized among developing countries such as the African Tax Administrators Forum (ATAF) and the Inter-American Center of Tax Administrators (CIAT) (rather than the OECD), which have shaped efforts. As discussed elsewhere in this report (see IMF impact chapter), there has wrongly been perceived to be a tradeoff between effective and efficient tax collection/administration, and equitable/progressive tax policies. This stemmed partly from an ideological view in some quarters that high corporate and personal income tax rates encouraged tax avoidance and evasion, and so should be reduced (rather than increasing measures to combat avoidance and evasion); and partly from a correct belief that some types of rather regressive indirect consumption taxes (sales taxes and VAT) were much less easy to avoid and easier to collect, and therefore should be the prime focus for improving tax administration in developing countries which did not have comprehensive consumption taxes.

Nevertheless, there is no doubt that tax measures introduced by developing countries with the support of international organizations (or sometimes without their support) have succeeded in increasing tax collection rates
dramatically. For example, between 2002 and 2012, average revenue/GDP ratios rose in low-income Africa from 13 per cent to 18 per cent, and the number of low-income African countries collecting less than 15 per cent of GDP fell from 20 to only 9.¹² This has happened even in a broader context of reduction in revenues from customs duties, due to liberalization agreed in international trade negotiations. It reflects not just the introduction of regressive taxes: in some countries the IFIs helped to set high thresholds for paying VAT which exempted most micro-traders and businesses; in others they helped to increase taxation of extractives, and collection of progressive direct taxes. In addition, countries have taken many practical administrative steps which have certainly improved tax collection – including the use of independent revenue authorities, Tax Identification Numbers, strengthened large taxpayer units, and increased training, staffing and pay for tax offices, and greater emphasis on systematic enforcement of collection, as well as public information campaigns on why paying tax is vital.

Not nearly enough has been done, and it is easy to argue that the focus has been misdirected – that much larger increases in tax revenue could have been achieved by taxing large (especially extractives) corporations and individual taxpayers more effectively in terms of policy and enforcement, and combating tax evasion and avoidance. For these reasons, the score given in this area is of only mitigated improvement.

**Recommendation:** In pursuing future tax collection efficiency increases, emphasis should be placed on the largest potential sources of extra tax – large corporations and high net worth individuals, and tax evasion and avoidance – and efficiency concerns more carefully balanced with equity in order to fight inequality.

As discussed in the IMF and World Bank chapters, progressive taxation can be one of the most powerful policy levers to fight against inequality and reduce poverty, both directly by reducing post-tax income disparities, and by funding anti-inequality/poverty spending. The IMF and the World Bank have been the dominant global institutions in influencing developing country tax policies over the last 2-3 decades. They have spent several decades focusing on tax efficiency at the expense of tax equity, therefore encouraging increases in indirect consumption taxes; and (especially by the World Bank) encouraging reductions in corporate tax on mistaken grounds that this will encourage private sector growth and investment.

However, the prevailing wind appears to be changing. The IMF has made clear in its research and public statements that progressive taxation is an important tool for reducing inequality. It is now beginning tentatively to analyze progressivity of tax systems and to advise countries on making systems more equitable where they request such support, focusing especially on increasing returns from corporate and personal direct taxes for “large taxpayers” and natural resources extractive companies. The IMF is also strongly questioning corporate tax exemptions, and even the World Bank and IFC have toned down their earlier global and country advocacy of corporate tax reductions. These changes have yet to bear any major fruit or to offset a two-decade trend away from progressivity, but deserve some credit for starting to move in the right direction.

**Recommendation:** As raised in the IMF chapter, all governments should review their tax policies for their equity and progressivity, and resulting contribution to reducing inequality. Policy advice, technical assistance and research conducted by the international organizations should focus on this issue to support the post-2015 framework.
## Tax Impact Assessment

<table>
<thead>
<tr>
<th>Impact Criteria</th>
<th>2014</th>
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<tr>
<td>Illicit Financial Flows</td>
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<tr>
<td>Avoidance</td>
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<td>Tax Wars</td>
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<td>Tax Administration</td>
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<td>Progressive Tax</td>
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<tr>
<td>Average Score</td>
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³ Relatively little wealth is held in cash, though one estimate suggests that about US $1.7 trillion of hidden offshore wealth takes the form of high denomination “strong currency” banknotes, i.e., big bills such as the 1,000 Swiss franc note, the 500 Euro note, the US and Canadian $100 notes. See Henry, J. (2014) Big Bills, The American Interest, Volume IX, July/August 2014, Washington
⁴ Available at http://www.financialsecrecyindex.com/
⁵ These include Bermuda, the British Virgin Islands, the Cayman Islands, the British Channel Islands, Gibraltar, the Isle of Man, the Turks & Caicos Islands
⁸ For background information about trusts, including discretionary trusts, see here: http://taxjustice.blogspot.de/2009/07/in-trusts-we-trust.html Accessed 21 August 2014
¹⁰ The UK law office of Farrer & Co was asked by Tax Justice Network “to advise whether a person may be said to be under a ‘fiduciary duty’ to avoid tax.” Their opinion, written by David Quentin and delivered July 5, 2013 at a conference at the City University of London, was a resounding “No.” The opinion is available upon request from John Christensen of Tax Justice Network.
## IMPACT ASSESSMENT FRAMEWORK

<table>
<thead>
<tr>
<th>Functions</th>
<th>5 Core Areas of Work</th>
<th>Worsens Impact</th>
<th>None or Limited Impact</th>
<th>Slightly Positive Impact</th>
<th>Significant Positive Impact</th>
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<tbody>
<tr>
<td><strong>What does the institution do?</strong></td>
<td><strong>What is it responsible for?</strong></td>
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</table>

**G20**

How has the work of the G20, through its various functions, impacted the real economy, particularly inequality and poverty, in the poorest countries?

<table>
<thead>
<tr>
<th>Functions</th>
<th>5 Core Areas of Work</th>
<th>Worsens Impact</th>
<th>None or Limited Impact</th>
<th>Slightly Positive Impact</th>
<th>Significant Positive Impact</th>
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**FSB**

What impact has the work of the FSB, through its various functions, had on stability in the financial system and reducing the risks that threaten inclusive and sustainable growth?

<table>
<thead>
<tr>
<th>Functions</th>
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**IMF**

How has the work of the IMF, through its various functions, impacted the real economy, particularly inequality and poverty, in the poorest countries?
<table>
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<td>• Policy Assessments or Strategy Papers</td>
<td>• Overall Framework</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Tax (UN, OECD &amp; IMF)</strong></td>
<td><strong>Tax (UN, OECD &amp; IMF)</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>UN Tax Committee</strong></td>
<td><strong>UN Tax Committee</strong></td>
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<td></td>
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<tr>
<td>Global Policy Development</td>
<td>Global Policy Development</td>
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<tr>
<td>OECD</td>
<td>OECD</td>
<td></td>
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<td></td>
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</tr>
<tr>
<td>Global Policy Development</td>
<td>Global Policy Development (Global Forum and BEPS)</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>IMF</td>
<td>IMF</td>
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<tr>
<td>Policy Advice</td>
<td>Policy Advice</td>
<td></td>
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<td></td>
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</tr>
<tr>
<td>(see above)</td>
<td>(see above)</td>
<td></td>
<td></td>
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<td></td>
</tr>
</tbody>
</table>

How has the work of the World Bank, through its various functions, impacted the real economy, particularly inequality and poverty, in the poorest countries?

How has the tax work of the UN Tax Committee, OECD and IMF, through their various functions, impacted the real economy, particularly inequality and poverty, in the poorest countries?
## Governance Scorecard

<table>
<thead>
<tr>
<th>Governance Area</th>
<th>Poor (1)</th>
<th>Moderate (2)</th>
<th>Good (3)</th>
<th>Excellent (4)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Transparency</strong></td>
<td>- Limited access to basic information and documents</td>
<td>- Moderate access to basic information and documents</td>
<td>- Full access to basic information and documents</td>
<td>- Full access to basic information and documents</td>
</tr>
<tr>
<td></td>
<td>- Information disclosure is not timely or comprehensive</td>
<td>- Information disclosure is fairly comprehensive but not timely</td>
<td>- Information is fully disclosed in a timely manner</td>
<td>- Information is fully disclosed in a timely manner</td>
</tr>
<tr>
<td></td>
<td>- External stakeholders have no information regarding decision-making</td>
<td>- External stakeholders have limited information regarding decision-making</td>
<td>- External stakeholders have full information regarding decision-making</td>
<td>- External stakeholders have full information regarding decision-making</td>
</tr>
<tr>
<td></td>
<td>- Member countries have limited information regarding decision-making</td>
<td>- Member countries have full information regarding decision-making</td>
<td>- Member countries have access to all information and documents regarding decision-making</td>
<td>- Member countries have access to all information and documents regarding decision-making</td>
</tr>
<tr>
<td></td>
<td>- There is no channel to request information</td>
<td>- There is no channel to request information</td>
<td>- There is a channel to request information</td>
<td>- There is a channel to request information</td>
</tr>
<tr>
<td></td>
<td>- There is no official transparency policy</td>
<td>- There is an official transparency policy which is reviewed regularly</td>
<td>- There is an official transparency policy which is reviewed regularly</td>
<td>- There is an official transparency policy which is reviewed regularly</td>
</tr>
<tr>
<td></td>
<td>- No documents are translated</td>
<td>- Only basic documents are translated; 2-3 languages</td>
<td>- Major policy and country documents are translated; 6 UN languages</td>
<td>- All policies and country documents are translated; 6 UN languages</td>
</tr>
<tr>
<td><strong>Accountability</strong></td>
<td>- There is no internal oversight body</td>
<td>- Internal oversight body is weak</td>
<td>- Internal oversight body is strong</td>
<td>- Internal oversight body is strong</td>
</tr>
<tr>
<td></td>
<td>- There is no external oversight body established</td>
<td>- External oversight body is established, but is weak</td>
<td>- External oversight body is strong</td>
<td>- There is a periodic review/report of accountability</td>
</tr>
<tr>
<td></td>
<td>- There is no internal complaint mechanism</td>
<td>- Internal complaint mechanism is informal or ineffective</td>
<td>- Internal complaint mechanism is formalized</td>
<td>- There is an advanced institutional constitution</td>
</tr>
<tr>
<td></td>
<td>- No official whistleblower policy or protections</td>
<td>- Whistleblower policy and protections are weak</td>
<td>- Whistleblower policy and protections are enforced</td>
<td>- There is an advanced institutional constitution</td>
</tr>
<tr>
<td></td>
<td>- The structure and roles of internal bodies are unclear</td>
<td>- The structure and roles of internal bodies are poorly defined</td>
<td>- The structure and roles of internal bodies, executives, staff, etc. are clearly defined</td>
<td>- There is an advanced institutional constitution</td>
</tr>
<tr>
<td></td>
<td>- No review/report of accountability</td>
<td>- No review/report of accountability</td>
<td>- There is a periodic review/report of accountability</td>
<td>- There is an advanced institutional constitution</td>
</tr>
<tr>
<td></td>
<td>- No formal institutional constitution</td>
<td>- There is a basic institutional constitution</td>
<td>- There is an ex-post assessment of actions to consider economic and social impacts</td>
<td>- There is an advanced institutional constitution</td>
</tr>
<tr>
<td></td>
<td>- There is no ex-post impact assessments of actions</td>
<td>- There is an ex-post assessment of actions to consider economic and social impacts</td>
<td>- There is an ex-post assessment of actions to consider economic and social impacts</td>
<td>- There is an advanced institutional constitution</td>
</tr>
</tbody>
</table>

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*Governance & Impact Report 2014*
<table>
<thead>
<tr>
<th>Inclusiveness</th>
<th>Poor (1)</th>
<th>Moderate (2)</th>
<th>Good (3)</th>
<th>Excellent (4)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Responsibility</strong></td>
<td>• There is no <em>ex-ante</em> impact assessment of actions</td>
<td>• There is no <em>ex-ante</em> impact assessment of actions</td>
<td>• There is an <em>ex-ante</em> assessment of actions to consider economic and social impacts</td>
<td>• There is an <em>ex-ante</em> assessment of actions to consider economic, environmental and social impacts</td>
</tr>
<tr>
<td></td>
<td>• There is no external complaint mechanism</td>
<td>• There is an informal external complaint mechanism</td>
<td>• There is a formal external complaint mechanism</td>
<td>• There is a formal and tested external complaint mechanism</td>
</tr>
<tr>
<td></td>
<td>• Parties negatively affected by actions are not compensated or acknowledged</td>
<td>• Parties negatively affected by actions are acknowledged but not compensated</td>
<td>• Parties negatively affected by actions are acknowledged and compensated</td>
<td>• Parties negatively affected by actions are acknowledged and fully compensated</td>
</tr>
<tr>
<td></td>
<td>• There is no accountability mechanism for harm or wrong-doing</td>
<td>• There is a limited accountability mechanism for harm or wrong-doing</td>
<td>• There is a strong accountability mechanism for harm or wrong-doing</td>
<td>• There is a strong legally binding accountability mechanism for harm or wrong-doing</td>
</tr>
</tbody>
</table>

**Governance & Impact Report 2014**

<table>
<thead>
<tr>
<th><strong>Inclusiveness</strong></th>
<th>Poor (1)</th>
<th>Moderate (2)</th>
<th>Good (3)</th>
<th>Excellent (4)</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Distribution of power (seats and votes) is arbitrary; with no clear criteria</td>
<td>• Distribution of power has clear criteria but is skewed or disproportionate</td>
<td>• Distribution of power has clear criteria; and is proportionate</td>
<td>• Distribution of power has clear criteria; and is proportionate and equitable</td>
<td>• Distribution of power has clear criteria; and is proportionate and equitable</td>
</tr>
<tr>
<td>• Member countries have limited access to decision-making</td>
<td>• Distribution of power criteria is reviewed irregularly</td>
<td>• Distribution of power is reviewed and updated regularly</td>
<td>• Member countries have full access to decision-making</td>
<td>• Member countries have full access to decision-making</td>
</tr>
<tr>
<td>• Non-members have no access to decision-making</td>
<td>• Member countries have limited access to decision-making</td>
<td>• Member countries have full access to decision-making</td>
<td>• Non-members have moderate access to decision-making</td>
<td>• Non-members have moderate access to decision-making</td>
</tr>
<tr>
<td>• Criteria for membership is unclear; and there is no review of membership</td>
<td>• Criteria for membership is clear; but there is no review of membership</td>
<td>• Criteria for membership is clear and reviewed</td>
<td>• Criteria for membership is clear and reviewed regularly</td>
<td>• Criteria for membership is clear and reviewed regularly</td>
</tr>
<tr>
<td>• There is no engagement with external stakeholders</td>
<td>• There is limited engagement with external stakeholders</td>
<td>• There is deep engagement with all external stakeholders</td>
<td>• There is deep engagement with all external stakeholders</td>
<td>• There is deep engagement with all external stakeholders</td>
</tr>
<tr>
<td>• There are no public consultations</td>
<td>• Public consultations are irregular; privileged access for certain groups; short time frame for participation</td>
<td>• Public consultations are regular; accessible for all groups; reasonable time frame for participation</td>
<td>• Public consultations are regular; accessible for all groups; consultation agenda shared in advance</td>
<td>• Public consultations are regular; accessible for all groups; consultation agenda shared in advance</td>
</tr>
<tr>
<td>• External views are not acknowledged and/or incorporated into institutional policies</td>
<td>• External views are rarely incorporated into institutional policies or practices</td>
<td>• External views are incorporated into institutional policies or practices</td>
<td>• External views are incorporated into institutional policies or practices</td>
<td>• External views are incorporated into institutional policies or practices</td>
</tr>
</tbody>
</table>
Genuine transparency can breed strong accountability. With strong accountability, there is greater responsibility. And when individuals or institutions become responsible, they begin to think seriously about their impact.