



# **Governance, and Legal and Institutional Arrangements**

Based on Client Presentation

October 2010

# Outline

- Wider institutional structures
- Coordination challenges
- Accountability

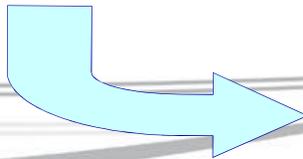
*[For issues surrounding the DMO, see separate presentation]*

# Governance

Governance is *“The legal, administrative and accountability structures – formal and informal – within which policies are made, executed and monitored.”*

## The Tools of Governance

- Legal Framework
- Policy co-ordination, decision-making, objective setting
- Delegation and accountability
- Transparency, disclosure and reporting
- The risk management framework
- Institutional organisation
- Oversight and audit



Apply in the specific institutional context (inc legal framework)

# Governance in Debt Management

- Governance has a number of components
  - The structures that shape and direct the operations of government
    - Broad legal apparatus (statutory legislation, ministerial decrees, etc) that defines aims, authorities, and accountabilities
    - The role of Parliament or National Assembly
  - The policy process
    - How decisions are made – both at a high level and day to day – who makes them and who is consulted
  - The management framework
    - The formulation and implementation of strategy, business planning, operational procedures, risk management, capacity building, and internal reporting responsibilities
  - The accountability, audit and wider reporting framework

# Governance: the Framework

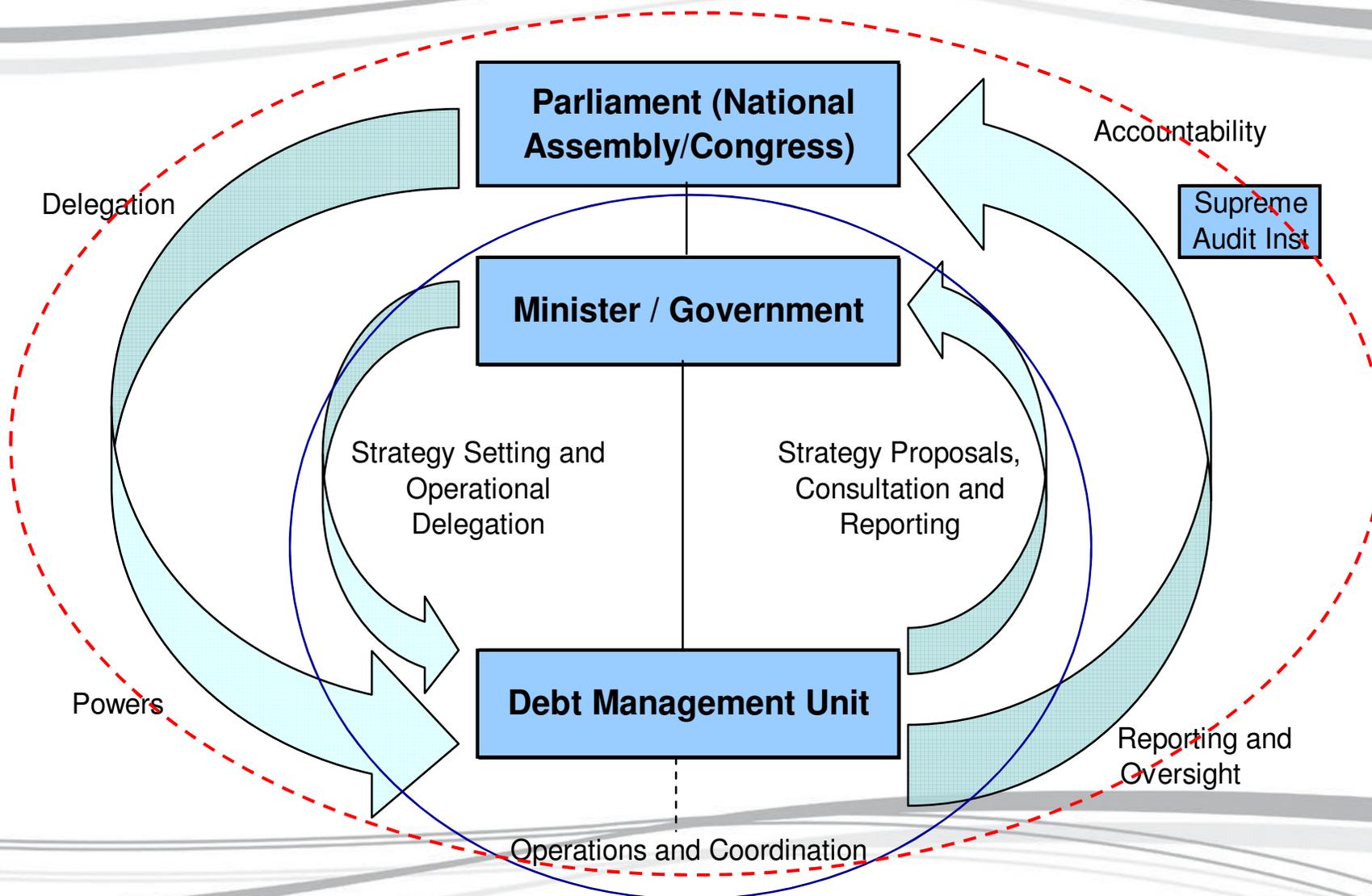


Chart Adapted from: World Bank Debt Management Performance Acceptance Tool

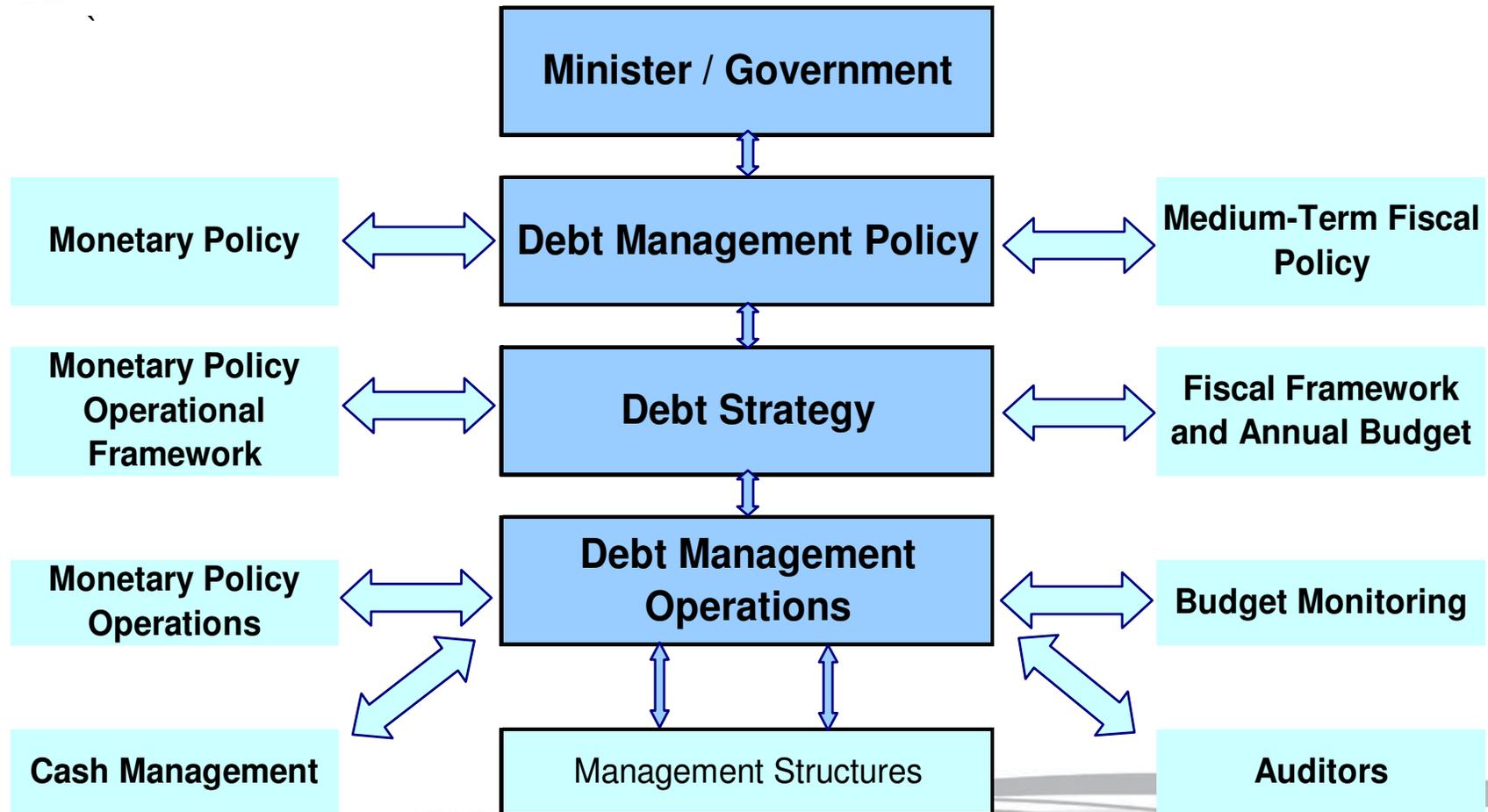
# Legislation: the Options

- Different countries have different frameworks: public debt legislation may be expressed in:
  - The Constitution
  - Public Finance, Budget, or Fiscal Responsibility Laws
  - Public Debt laws
  - A decree - or a “Code for Fiscal Stability” or similar (as in the UK)
- The most common practice internationally is for public debt to be in a Public Finance law
  - But Public Debt Laws are increasing in number
  - Should link also to laws on securities market, audit, etc
  - Note: Public Debt and Fiscal Responsibility Laws have different purposes
- Legislation must not be too prescriptive or detailed
  - Creates delay and uncertainty in decision making & execution processes
  - Constrains the scope for innovation in response to market developments
  - Parliament / National Assembly / Congress should not approve individual transactions; instead approve legislation and strategy; and hold ministers and officials accountable for its execution

# Legal Framework for Debt Management: International Practice

- Best international practice; the legislation
  - Addresses the state's authority to borrow, issue guarantees
  - Establishes a high-level objective
  - Identifies the Minister of Finance as responsible minister with authority to set specific objectives; to execute policy; and to make payments
  - Ensures Ministry of Finance has the necessary information
  - Sets reporting and accountability requirements
- May include a borrowing limit
  - A debt ceiling or an annual borrowing limit (net or gross)
  - Borrowing not to exceed capital expenditure (at least over the cycle)
  - But preferable for Parliament to set an annual borrowing limit in connection with the approval of the fiscal budget – links with Parliamentary control of the budget
- The introduction of a DMO may require additional legislation

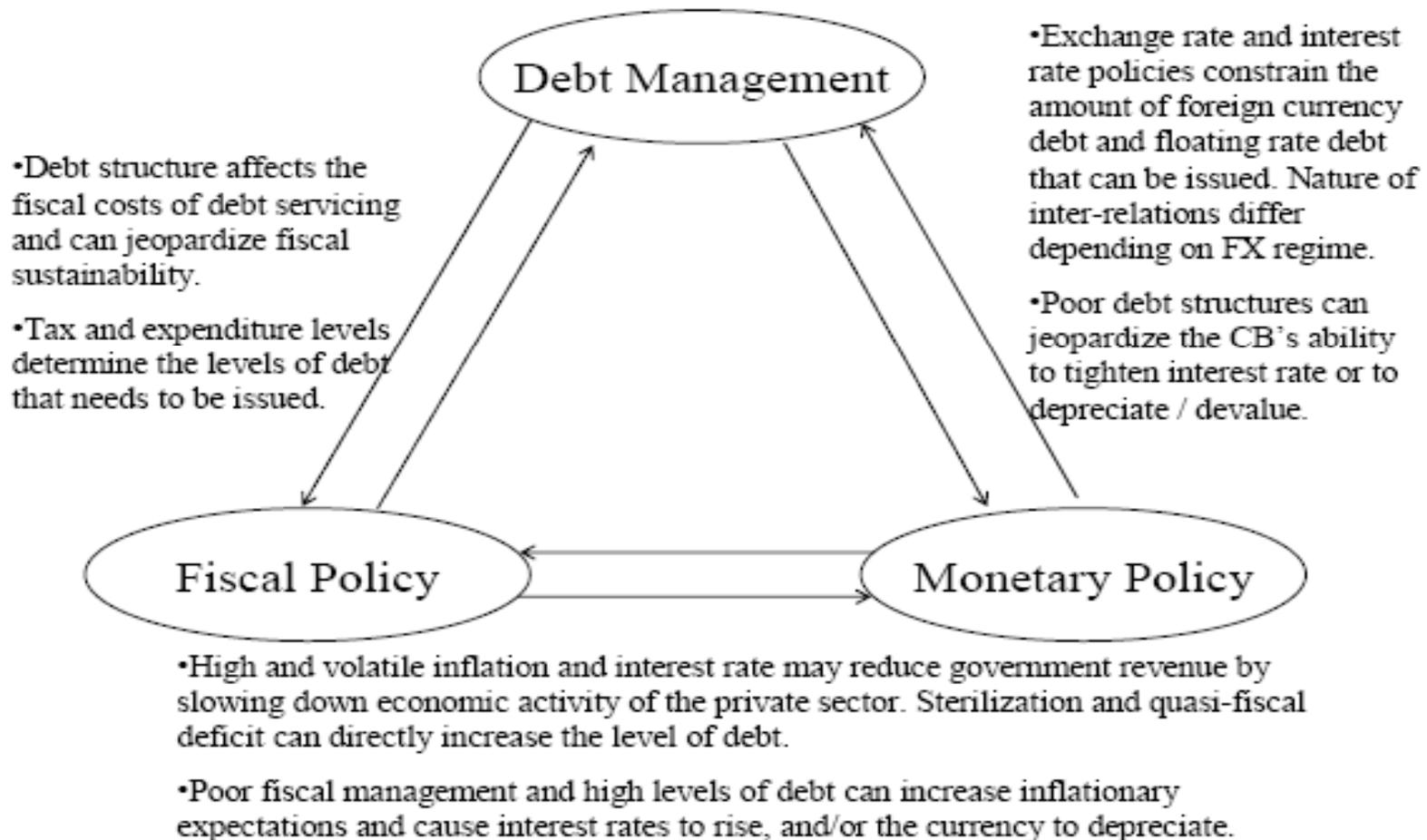
# Governance: Coordination Challenges



# The Macro-Economic Framework

- Growing consensus that debt management policy, fiscal policy and monetary policy should be treated as separate macro-economic policies
- The assignment of separate policy objectives and instruments enhances the credibility and effectiveness of policy
  - **Debt management objective:** to ensure that government's financing needs and payment obligations are met at the lowest possible cost over the medium to long run, consistent with a prudent degree of risk.
  - **Fiscal policy objective:** to achieve the least distorting budgetary policy that stabilises output and improves resource allocation and income distribution
  - **Monetary policy objective:** to achieve price stability, [while maintaining stable output]
- But
  - Effective policy decentralisation requires coherence of the overall policy mix
  - Separate policies only work if there are separate policy instruments that are independent of each other – rarely the case in emerging market countries
- Public debt management should therefore be integrated into a broader macro-economic framework of analysis that determines a consistent policy

# Monetary, Fiscal & Debt Management Policy: Interdependencies and Trade-offs



Source: Eriko Togo "Coordinating Public Debt Management with Fiscal and Monetary Policies: An Analytical Framework" (World Bank Sept 2007)

# Different Coordination Mechanisms

- In EU, Stability and Growth Pact in principle sets a ceiling on the annual fiscal deficit and debt level
  - Facilitates implementation of the desired monetary policy under a monetary union
  - Broke down because the EU is not structured as an economic union
- Some countries have Fiscal Responsibility Laws that include target deficit and debt levels
- Some have a Public Debt Committee
  - Chaired by Minister (or very senior official)
  - Considers and decides debt strategy; delegates execution; monitors performance
  - Ensures that all relevant interests and expertise are consulted – macro and fiscal teams in MoF, also Central Bank
  - All agree strategy – and leave debt managers to deliver within agreed operational framework and without day-to-day second guessing
  - Can assist co-ordination in institutionally fractured environment

# Delegation

- Ministers delegate implementation to debt managers
  - Specified parameters or objectives, e.g. portfolio or duration benchmarks
  - Related objectives (e.g. for contingent liabilities, debt restructuring)
- Identifying
  - Decisions that must be taken by Ministers; or can be taken by officials
    - Depends on legislation and administrative practice
  - Circumstances that require a revision, e.g. changes in fiscal position
- Policy delegation backed by:
  - Longer-term management objectives (capacity, administrative costs)
  - Preparation of an annual business plan
  - Management reports, publications and other information
- Benefits from defined delegation in terms of
  - Transparency and accountability
  - Faster decision-making
  - Less risk of challenge from other bodies
  - Increased sense of purpose and authority for the debt management function
    - contributes to capacity building

# External Accountability

- Reporting outturns against the published objectives
- Managerial and operational reports
  - Within the Ministry of Finance
  - Formally to Parliament
  - To market, on website etc
- Performance assessment
  - High-level – is it the right objective
  - Achievement of portfolio objectives
  - Meeting management and service objectives
- External Audit
  - Both propriety and cost-effectiveness or performance

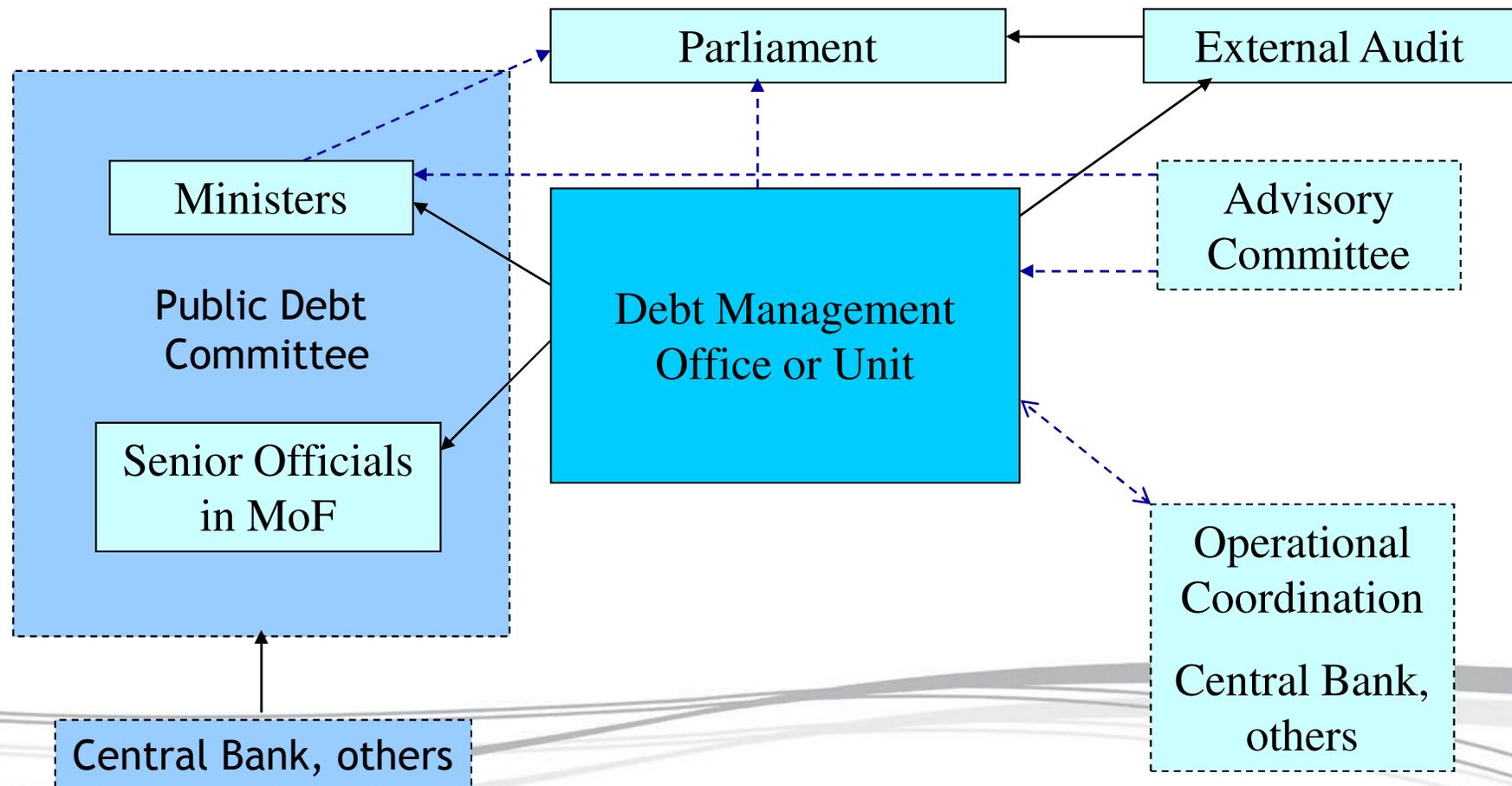
# Operational Coordination

- Fiscal authorities
  - Budget planning drives financing requirement
  - Budget monitoring in-year – flow of information to all responsible for debt (and cash) management functions
- Central Bank
  - Potential input to policy
    - Consistency of debt management and monetary policy objectives
    - Drawing on market knowledge
  - Operational requirements
    - Avoid confusing signals to market participants; or competing auctions
    - [Exchange cash flow forecasts]
  - Bank also supplies services
    - Fiscal agent for tenders or auctions
    - Registration and database services
    - Cash account manager (banking services, inc FX purchases)
    - Benefits of some kind of Service Level Agreement

# Cash Management and Debt Management

- Integration of (or close coordination between) cash and debt management functions ensures:
  - Debt issuance decisions are taken in the context of the seasonal nature of government's cash flows
  - MoF has overview of whole market – important when taking decisions about the future balance of short- and long-term debt, including Treasury bills.
  - In time, through active management of the short-term cash position, the combined function will be better placed to weaken the link between the timing of cash flows and bond issuance - allows pattern of bond sales to be announced in advance
  - Potential operational and risk management advantages
- Integration is increasingly the norm in OECD countries
  - Often with the formation of a debt office or similar

# External Governance Structure - Typical International Arrangement



# Role of External Advisory Committee

- Assurance to Minister (& Parliament?)
- Relevant expertise – support to Head of Office
- Oversight of internal control framework (e.g. Chair of Audit Committee)
- Alternative structures
  - Appointed by officials or ministers
  - Public or private reporting
  - Formal or informal decision-making responsibilities
- But beware:
  - Conflicts of interest
  - Interference not advice
  - Not common in emerging market countries