



Governance, and Legal and Institutional Arrangements

Based on Client Presentation

October 2010

Outline

- Wider institutional structures
- Coordination challenges
- Accountability

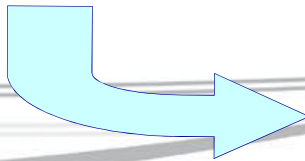
[For issues surrounding the DMO, see separate presentation]

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

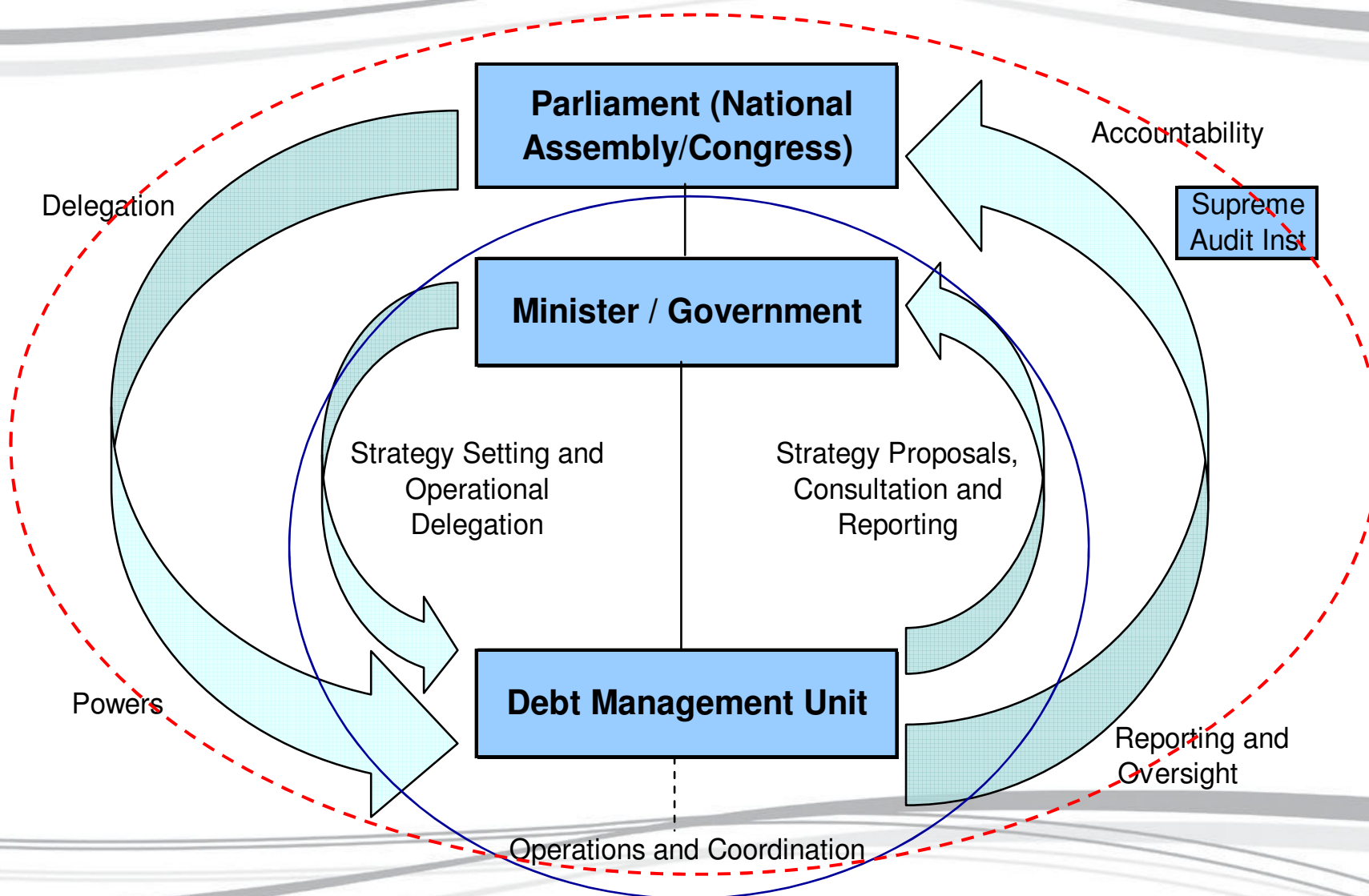


Chart Adapted from: World Bank Debt Management Performance Acceptance Tool

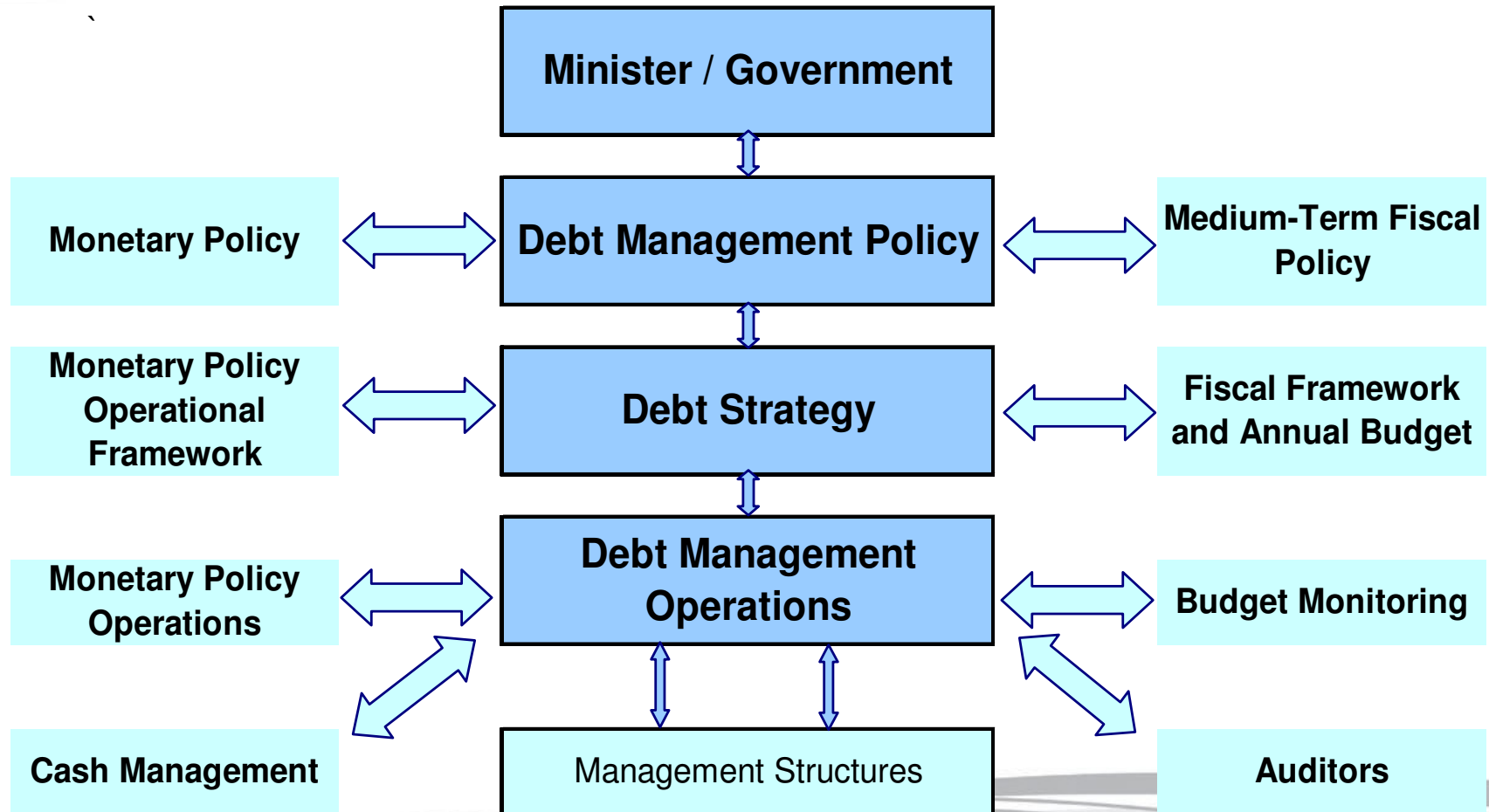
Legislation: the Options

- 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

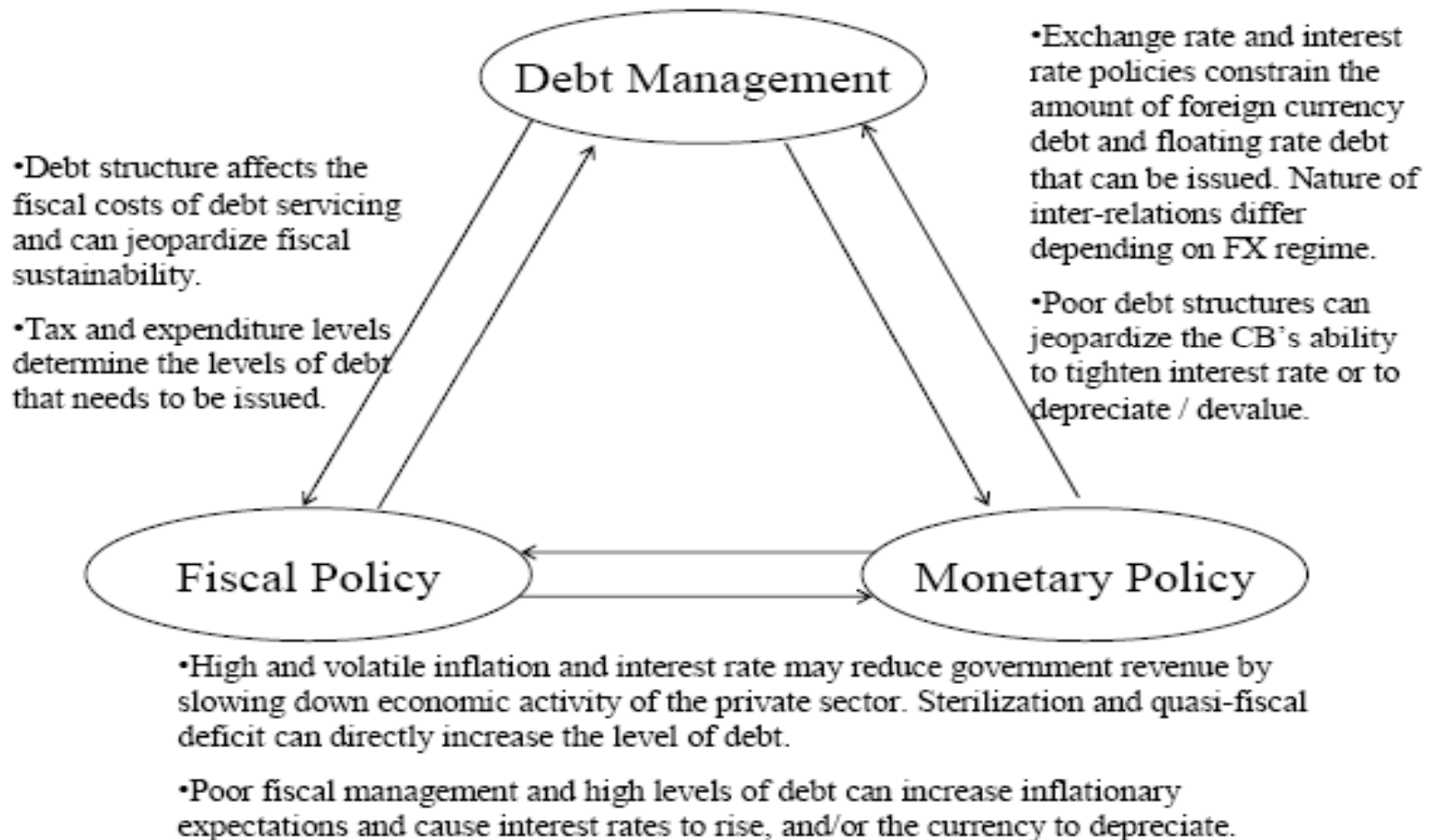
Governance: Coordination Challenges



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

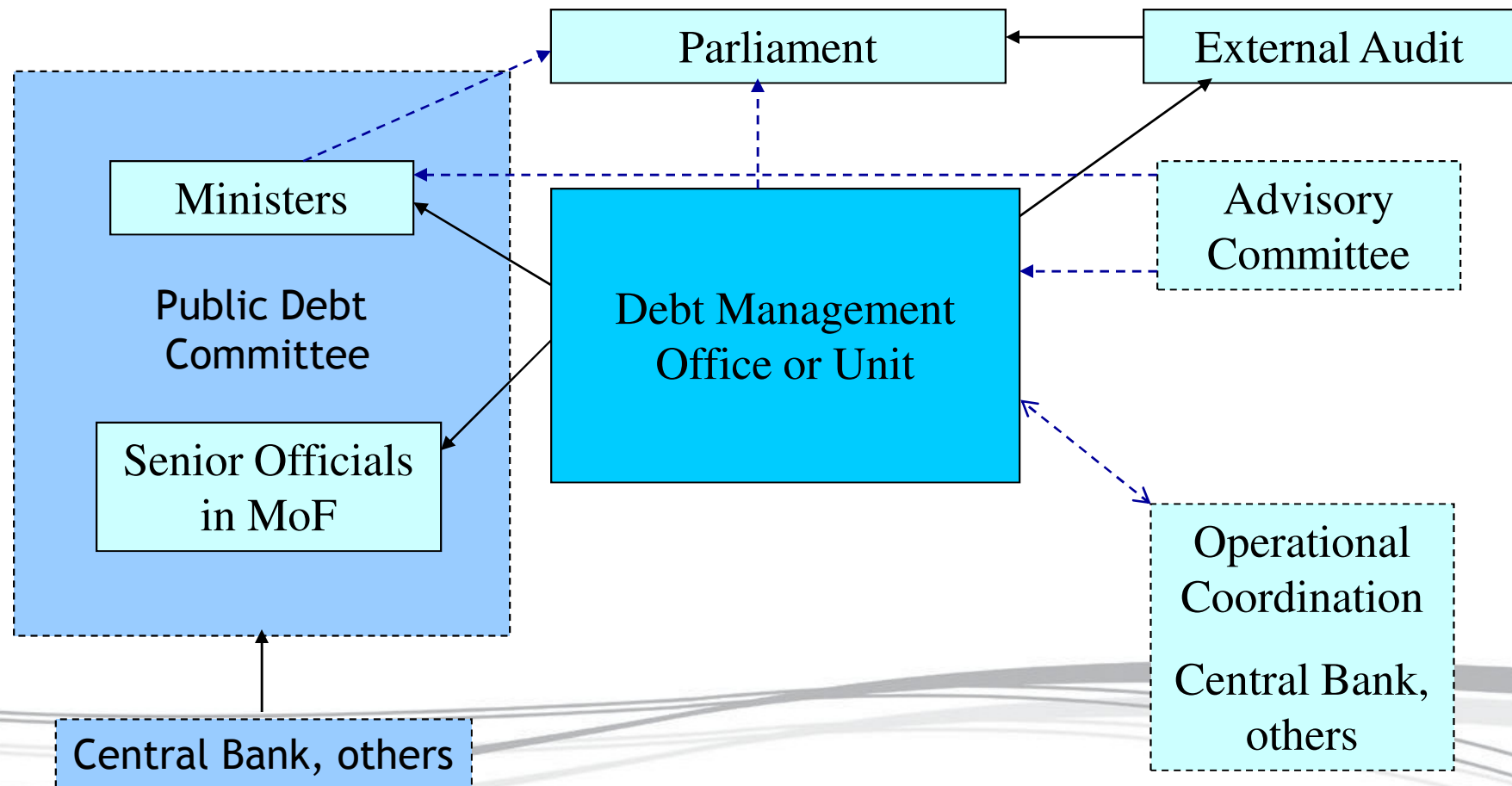
Operational Coordination

- 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