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To: Members of the Executive Board

From: The Secretary

Subject: **Code of Good Practices on Transparency in Monetary and Financial Policies—Progress Report**

Attached for the information of the Executive Directors is a progress report on the code of good practices on transparency in monetary and financial policies.

Mr. W. Alexander (ext. 35366) or Mr. Siegman (ext. 37906) is available to answer questions relating to this report.

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Department Heads



INTERNATIONAL MONETARY FUND

Code of Good Practices on Transparency in Monetary and Financial Policies: Progress Report

Prepared by the Monetary and Exchange Affairs Department

(In consultation with the other departments)

Approved by Manuel Guitián

September 21, 1998

At its April 1998 meeting, the Interim Committee endorsed a *Code of Good Practices on Fiscal Transparency* developed by the IMF and “encouraged the IMF Executive Board to examine the desirability of developing a code of good practices with respect to financial and monetary policies, in cooperation with the appropriate institutions.” In response, the staff is completing a draft of a *Code of Good Practices on Transparency in Monetary and Financial Policies*. This Progress Report summarizes the scope and focus of the Code under preparation, and notes some of the considerations that are being taken into account in drafting the Code.

The structure of the Code under preparation is similar to that of the Fiscal Code. It is based on four general principal categories: (1) clarity of roles, responsibilities and objectives; (2) open process of formulating and reporting on monetary and financial policy decisions; (3) public availability of information, possibly with some lags; and (4) accountability and assurances of integrity. For each category the Code will list a number of principles of good practice. These principles, in turn, will be supplemented by more specific good practices on transparency in monetary and financial policies. As an Annex to this Report, attached is a summary of good practices on transparency in monetary and financial policies of the Code under preparation.

A supporting manual to the Code will need to be prepared after the Code has received Board approval. The manual would offer more details on the principles of transparency contained in the Code and would offer guidelines to their interpretation and implementation.

The draft Code focuses on those practices that would enhance the transparency and accountability of central banks¹ with regard to their conduct of monetary policy and of central

¹The institutional arrangements for assigning responsibility for the conduct of a country's monetary policy differ among the Fund's membership. For most Fund members, this responsibility is assigned to a “central bank.” There are a number of countries, however,

(continued...)

banks and the other financial regulatory and supervisory agencies for their conduct of financial policies^{2 3}. It emphasizes ways to make the process and objectives of monetary and financial policies more open and comprehensible to the public and the markets. In addition, the Code identifies ways to achieve public accountability by the central bank and the other financial regulatory and supervisory agencies with respect to their operations and activities and the manner they conduct policy.

The case for transparency of monetary and financial policies is twofold. First, transparency encourages accountability and imposes discipline on policymakers. Good governance calls for holding the central bank and the other financial regulatory and supervisory agencies accountable, particularly if these agencies are to be given a high degree of operational autonomy within the governmental apparatus. Second, transparency can enhance credibility and thereby the effectiveness of monetary and financial policies. The benefit of enhanced credibility is that policy objectives can be achieved at a lower cost than would be the case if the policy commitment is not fully credible. In part, the benefits of increased credibility are gained by providing the private sector with a better understanding of how policymakers may react to developments in the economy and financial markets, thus making the monetary policy transmission mechanism more effective and helping in the formation of market expectations.

While the Code emphasizes good practices for the formulation and reporting of monetary and financial policies, its focus is on transparency. It is not designed to offer judgments on the

¹(...continued)

where this role is designated to a “monetary authority” or to a “currency board.” To facilitate presentation, the term “central bank” in this Code will refer to both the “classical” central banks and to “monetary authorities” and “currency boards.”

²The term “financial policies” in this Code refers to policies related to the regulation and supervision of the financial system.

³A wide range of institutional arrangements prevail among Fund members with regard to which unit of government carries exclusive or primary responsibility for the regulation and supervision of the financial system. In a few countries, an agency has been established with oversight and policy formulation responsibility for regulating and supervising an array of financial institutions and activities (banking, insurance, securities dealers, and equity, commodity, and future markets). For most countries, the oversight responsibility for the financial sector is shared among several agencies. Thus, responsibility for the conduct of bank regulation and supervision or for bank deposit insurance policies in some countries is assigned to the central bank, or to an independent bank supervisory or deposit insurance agency, or split among several units of government. Similarly, responsibility for the conduct of policies related to the oversight of certain categories of financial institutions typically is assigned to a specialized government agency. To facilitate presentation, the phrase “the financial regulatory and supervisory agencies” is used to refer to the institutional arrangements for regulating and supervising the financial system.

appropriateness or desirability of specific monetary or financial policy objectives or specific monetary or financial policies that countries should adopt. At the same time, the nature of policies is at least as important as their transparency.

The draft Code covers both monetary policies and financial policies (i.e., policies related to the regulation and supervision of the financial system). Some have suggested that financial policies should be segregated from monetary policies and that the Code, therefore, should have separate monetary and financial policies sections or that there should be two separate codes, one for monetary policies and another for financial policies. Doing so, besides resulting in a code/codes that would be repetitive and bulky, would draw too sharp a distinction between monetary policy and supervisory responsibilities. These two sets of policies are interrelated and often reinforcing, with the health of the financial system affecting the transmission of monetary policy and vice versa. The draft Code, therefore, treats transparency for monetary and financial policies in one integrated code.

The Code will be of sufficient breadth that it can span and be applied to a wide range of monetary and financial policy frameworks and good practices associated with them, and thus to a wide range of the Fund membership. Elements of the Code are drawn from a review of good transparency practices used in a number of countries and discussed in the professional literature. The Code thus represents a distillation of concepts and practices that are already in use and for which there is a record of experience. The Code, nevertheless, will make allowance for the prevailing diversity of the Fund's membership in institutional arrangements with regard to monetary and financial policies, different legal traditions, and levels of development. For some of the principles of good practice, therefore, the Code will specify that these are applicable to a set of countries and not to others, and are, therefore, addressed to particular groups of countries. Similarly, the Code recognizes that given differences in the level of development among Fund members, some of the good practices to be listed in the Code are currently beyond the reach of a number of members. However, these practices will be included in the Code in the expectation that countries would aspire over time to introduce such good practices. The proposed manual to accompany the Code would indicate how members could adopt these good practices.

The staff has reached the stage in the preparation of the Code where it is ready to confer with other institutions on the focus and scope of the proposed Code, as suggested by the Interim Committee. It is planning a visit to the Bank of International Settlements, the international institution that has extensive and direct dealings with governmental institutions that carry responsibility for conducting monetary and financial policies, to exchange views on the proposed Code with its senior officials. In addition, the staff plans to consult with senior officials who have experience with monetary and financial policies at the World Bank and regional groups such as CEMLA, with the Secretariat of the "Willard" Working Party on Transparency and Accountability, and, in the course of ongoing contact, with a number of central bank and treasury officials, for their views on the proposed Code.

Summary of Good Practices on Transparency in Monetary and Financial Policies

I. CLARITY OF ROLES, RESPONSIBILITIES AND OBJECTIVES

- The broad objective(s) of monetary and financial policies and the status of the central bank and the other financial regulatory and supervisory agencies within the government should be clearly defined and codified in legislation.
- The operational framework that the central bank employs in pursuing the broad objective(s) of monetary policy should be described and explained to the public.
- Monetary policy should be implemented by using market-based instruments.
- The separation of monetary and fiscal operations should be established, consistent with the principles of the Fund's *Code of Good Practices on Fiscal Transparency*.
- Agency roles performed by the central bank on behalf of the government should be clearly defined and should not interfere with the central bank's monetary policy responsibilities.
- The conduct of policies by the financial regulatory and supervisory agencies should be transparent and should adhere to accepted practices and norms.
- The conduct of the central bank in its oversight role of the nation's payment system should be transparent.

II. OPEN PROCESS FOR FORMULATING AND REPORTING MONETARY AND FINANCIAL POLICY DECISIONS

- Where the central bank has a monetary policy making body, there should be regularly scheduled and publicly announced meetings of that body to assess underlying economic developments, monitor progress towards achieving its monetary policy objective(s), and formulate policy for the period ahead.
- Monetary policy decisions should be reported publicly through defined channels in a timely manner.
- The central bank should publish, with a preagreed maximum delay, a summary of its monetary policy deliberations.
- The central bank should issue periodic public statements on progress towards its monetary policy objective(s) as well as prospects for achieving them.

- Policy decisions by the financial regulatory and supervisory agencies should be reported through defined channels in a timely manner.

III. PUBLIC AVAILABILITY OF INFORMATION

- The central bank should release to the public monetary and financial statistics on a preannounced schedule, consistent with the Fund-endorsed data dissemination standard.
- The central bank should release its balance sheet on a preannounced schedule and provide the public on a lagged basis information on market transactions, consistent with the Fund-endorsed data dissemination standard.
- The central bank in the capacity as principal or agent should release to the public on a preannounced schedule detailed information on foreign exchange reserve assets, liabilities, and commitments, consistent with the Fund-endorsed data dissemination standard.
- Regulations issued by the central bank and the other financial regulatory and supervisory agencies should be readily available to the public.
- The central bank and the other financial regulatory and supervisory agencies should establish and maintain public information services.

IV. ACCOUNTABILITY AND ASSURANCES OF INTEGRITY

- The Governor of the central bank should be obligated to appear before the legislature at least annually.
- The central bank should publish an Annual Report.
- The central bank should prepare a full set of financial statements on a preannounced schedule, and have these statements audited by an independent external auditor.
- Information and data on the budget of the central bank should be made available to the public on a preannounced schedule.
- The central bank and the other financial regulatory and supervisory agencies should have codes and rules for the manner their officials and staff conduct their personal financial affairs.

