

**FOR
AGENDA**

SM/09/264
Supplement 1
Correction 1

November 12, 2009

To: Members of the Executive Board

From: The Acting Secretary

Subject: **Review of the Fund's Transparency Policy—Background Paper**

The attached corrections to SM/09/264, Supplement 1 (10/28/09) have been provided by the staff:

Factual Errors Not Affecting the Presentation of Staff's Analysis or Views

Page 32, para. 63, line 1: for “12 percent” read “11 percent”
para. 66, line 7: for “33 percent” read “29 percent”
line 10: for “44 percent” read “21 percent”
line 11: for “15 percent” read “12 percent”
line 12: for “12 percent” read “15 percent”

Typographical Errors

Page 24, footnote 14: for “Prepared by Charleen Gust”
read “Prepared by Charleen Gust and Jung Yeon Kim”

Page 29, para. 56, Table, title: for “Countries with the Largest Number of Corrections in 2008”
read “Countries with the Largest Number of Corrections in 2007-08”
line 6: for “Australia” read “Australia (1)”
line 7: for “Australia” read “Australia (2)”

Page 29, Table after para. 56, second column, row labeled “0.1% = < > 1%”:

for “6”, read “7”

row labeled “30-99”: for “1” read “4”

row labeled “< 29”: for “1” read “8”

Questions may be referred to Mr. Hviding (ext. 34544) and Ms. Aylward (ext. 37807) in SPR.

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities.

Att: (3)

Other Distribution:
Department Heads

Box 4. Examples of “Gray Zone” Deletions

- *High market sensitivity.* For one small LIC member’s Article IV report, the sentence “That said, a high degree of exchange rate stability is appropriate at this stage.” was deleted on the basis that it was considered as highly market-sensitive. It is not clear that a reference to the need for exchange rate stability could result in disruptions to the foreign exchange market.
- *High market sensitivity.* In a smaller emerging market economy’s 2007 Article IV report, the statement “As a result, current account based models tend to show a very small undervaluation.” was deleted. Although references to misalignments have the potential of affecting exchange rate markets, a reference to “a very small undervaluation” could hardly trigger a large market reaction.
- *Premature disclosure.* On the basis that it was considered premature disclosure of policy intentions, the following deletion and redraft was implemented for the Executive Directors’ assessment section of the PIN for a larger emerging market economy’s 2007 Article IV: “Directors appreciated the authorities’ ongoing efforts to address these challenges, ~~but~~ and stressed that comprehensive and timely reforms would ease adjustment.” It is hard to see how the deleted text could be considered to reveal undisclosed policy intentions.

44. **In some cases, deletion requests may reflect a fear that the public will misunderstand or misinterpret the deleted text:**

- In one case, the member made the argument that showing information on the member’s program in a standard table including other exceptional access program countries could give the public the impression that the member was at risk of an immediate crisis. The member made this argument even though the report stated in several places that the member intended to treat the program as precautionary.
- In another case, the member claimed that a reference to a standard exchange rate shock used in all Fund debt sustainability analyses was highly market-sensitive due to possible misinterpretation by the public.

45. **In a few cases, large amounts of text were deleted, which is strongly discouraged by the policy.** In one case, an entire chapter of the Selected Issues Paper was deleted. Part IV of the Informational Supplement includes other cases of deletions with entire paragraphs removed that, in ex-post assessment, could arguably have been more parsimonious.

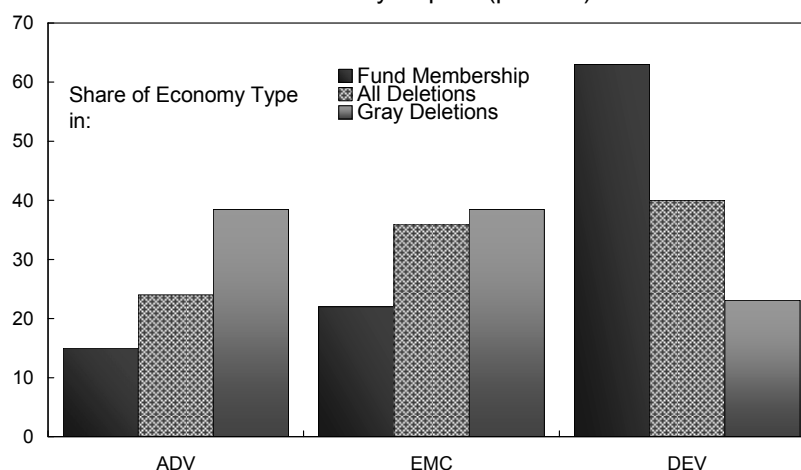
46. **Despite the relatively larger number of deletions for advanced and emerging market economies, the evidence on bias in the implementation of the policy is inconclusive.** During 2006–08, the share of advanced and emerging market countries’ reports with deletions was 13 percent and 22 percent, respectively, compared to only 6 percent for low-income countries. The higher number of deletions in emerging market economies (and to a lesser extent in advanced countries) may reflect that staff reports on these economies are more likely to contain information that could meet the criteria of being highly market-sensitive than staff reports for low-income members. Nevertheless, the ex-post review suggests that in 2008 the shares of all deletions and deletions deemed not fully within the policy were disproportionately higher in advanced and emerging market economies than in low-income countries (text table and figure), relative to these economy types’

representation in Fund membership. Of 50 individual deletions of information over 20 countries, 13 were judged ex-post to be light or dark gray, and advanced and emerging market countries each accounted for five of these gray deletions, while low-income countries accounted for only 3. Due to the relatively low overall number of deletions and, in particular, gray zone deletions and the lack of data on requests, no firm conclusion can be drawn from the staff review on any potential bias in this area.

Deletions to Country Papers (percent): 2008

	All countries	ADV	EMC	DEV
Within Policy	74	58	72	85
Light Gray	20	33	17	15
Dark Gray	6	8	11	0
	100	100	100	100

Deletions to Country Papers (percent): 2008



E. Corrections¹⁴

Corrections are a tool for ensuring reports are accurate. In many cases, however, the corrections do not unambiguously conform to the policy. Most of such “gray zone” corrections are made before the Board meeting, and most are for reports of advanced or emerging market countries.

Policy background

47. **The rules for corrections are intended to ensure that reports are factually correct, while avoiding negotiation of the language of staff reports.** Corrections are thus to be limited to: (i) data and typographical errors; (ii) factual mistakes; and

¹⁴ Prepared by Charleen Gust and Jung Yeon Kim.

56. The results from the sample of “top ten correction reports” indicate that corrections made in large and/or influential countries are more often in the dark gray zone than in other countries. Income level seems clearly relevant for the share of corrections in the dark gray zone: while, on

Countries with the Largest Number of Corrections in 2007-08

Advanced	Emerging Market Economies	Low-income Countries
United States	India	Macedonia, FYR
Switzerland	Malta	Vietnam
Japan	Mexico	Antigua and Barbuda
France	Ukraine	Angola
Australia (1)	Poland	Central African Rep.
Australia (2)	Malta	Seychelles
Belgium	Egypt	Syrian Arab Republic
United Kingdom	Chile	Maldives
Portugal	El Salvador	Oman
Germany	Uruguay	Guatemala

average, advanced and emerging market economy staff reports contained 2 and 3 dark gray corrections, respectively, no dark gray corrections were found in the low-income group. More specifically, the average number of dark gray zone corrections is significantly higher for countries with quota shares exceeding 1 percent than for countries with smaller quotas, those with higher GDP (size of the economy), and those who have a dedicated Executive Director at the Board, suggesting that size plays a role with perhaps also an independent element of “influence” as measured by the “Executive Director” effect.

Type of correction (average number per report)

	Within policy	"Light Gray"	"Dark Gray"
<i>By economy type</i>			
Advanced	8	2	2
Emerging	10	1	3
Low income	5	1	0
<i>By quota share</i>			
>= 1%	10	2	4
0.1 % =< > 1%	7	0	0
< 0.1%	6	1	0
<i>Level of Mission Chiefs</i>			
B-level MC	8	1	2
A-level MC	6	1	0
<i>Size of the economy, in GDP ppp in US\$ bn</i>			
>500	9	2	4
100-499	9	1	0
30-99	4	0	0
<29	8	2	0
<i>Appointed a Director at the Executive Board</i>			
Yes	10	2	5
No	7	1	0

57. **At the same time, it is difficult to determine to what extent this skewedness reflects a lack of evenhanded application of corrections rules.** Given that the requests are received in many different formats and media, it has proven impossible to construct good data on rejection of requests. Thus, it is not clear whether the bias discussed above is a reflection of a difference in gray zone requests or a different propensity by staff and management to accept such corrections. Moreover, the fact that a majority of the dark gray zone corrections is submitted before the Board meeting has two sides. This is good inasmuch as it allows the Board to see the corrections before the Board discussion. But it is potentially problematic in terms of evenhandedness, since such corrections do not generally go through the same inter-departmental review as corrections submitted after the Board meeting, and advanced and some emerging market countries probably have a greater capacity than lower-income countries to submit their corrections before the Board meeting.

F. Has Candor Been Affected by Increased Publication Expectations?¹⁵

Candor of the staff report submitted to the Board does not seem to be significantly affected by publication expectations, partly because sensitive material can be deleted.

Policy background

58. **Candor is critical for the Fund.** Candor in the Fund's dialogue with members, in reporting to the Board, and in communicating with the rest of the world is essential for high-quality and effective surveillance and programs. At the discussion of the [2008 Triennial Surveillance Review](#), Directors said that "surveillance is paying insufficient attention to risks, and communication about such risks has also sometimes been rather tentative." Many Directors felt that "surveillance communication should be bolder and should avoid excessive hedging, recognizing that such an approach does mean a risk of being proved wrong." The [April 2009 Communiqué of the International Financial and Monetary Committee](#) called for "improving the surveillance process through, inter alia, greater focus on the effectiveness of the policy dialogue and clear communications, with an emphasis on candor, evenhandedness, and independence."

59. **The tension between candor and transparency operates in several ways.** The expectation of publication can result in a less open exchange of views between the authorities and Fund staff, and/or self-censorship by the latter, weakening the candor in the substance of documents presented to the Board ("inside" candor). And undue use of deletions, or corrections that are primarily motivated by an attempt to "soften" the published report can undermine the candor of the published version of the report ("outside" candor), and thus expose the Fund to reputational risk. Arguably, though, the prospect of public scrutiny may also serve to bolster the independence of staff, with an eye on its professional reputation.

¹⁵ Prepared by Jung Yeon Kim.

60. **Assessing candor is tricky as there is no generally recognized metric for frankness.** In a fundamental way, candor refers to the relationship between an observable and an unobservable—what is written or said and what is thought or meant. While outside candor can to some extent be assessed by examining modifications data, no such tool exists for inside candor. And candor has to be evaluated in light of the information that the parties had at their disposal, which is often not known.

61. **In an attempt to overcome these difficulties, staff employed several approaches to shed some light on possible trends in candor.** A combination of staff document review and surveys was employed (see Appendices VI and VII for a fuller description). The document review compared different types of documents where one could, *ex ante*, expect to find different degrees of candor. Each document was reviewed independently by several staff members who had not been involved previously with the cases in question (in most cases there was a high degree of consensus between independent assessors). Candor was evaluated by assessing the prevalence of excessively hedged, qualifying, or unclear language that could indicate reduced frankness. Reports were also compared to (presumably candid) back to office reports and internal briefing notes. Surveys were used to get mission chiefs' perceptions of the degree of candor (see Informational Supplement for the detailed answers).

Trends in candor

62. **The review of staff reports found no clear evidence that publication or publication expectations affected the candor in the reports that go to the Board** (Appendix V). Indeed, in some cases, the degree of inside candor appeared to be *greater* for published reports:

- Staff compared four staff reports for the 1997–98 Asian crisis cases with five staff reports for recent exceptional access crisis cases. All of the former were written with the expectation that they would not be published, since publication of staff reports was not provided for at that time. All of the latter were written with the expectation (met for all the reports) that they would be published, given the publication regime for exceptional access programs. Though direct comparisons are difficult, due to the differences across the countries and the topics covered, staff found that, if anything, the staff reports for the recent crisis cases tended to be more candid than the reports for the Asian crisis. The macroeconomic outlook and financial sector problems in these reports appeared more detailed with less-guarded language than in the Asian crisis reports.
- The review of “converter” cases, i.e., members whose publication status switched from non-publisher to publisher, and comparisons of reports for permanent non-publishers (not published since May 1999) and publishers also show no clear difference in candor.

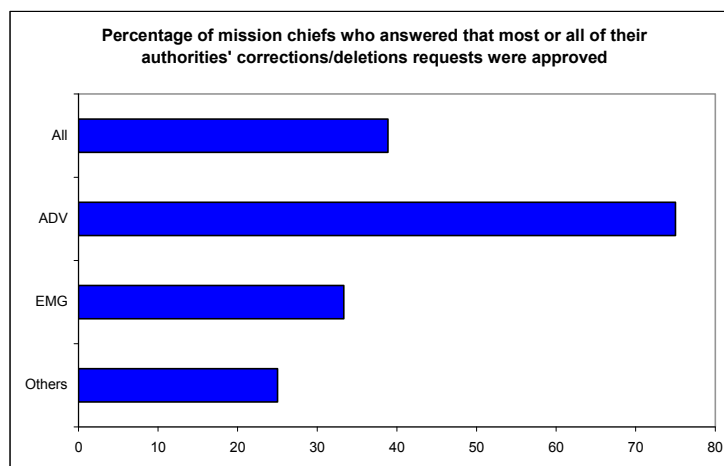
63. **At the same time, the survey of the mission chiefs suggests that the concern about candor cannot be dismissed entirely** (see Appendix VI and Section II of the

Informational Supplement). About 11 percent of mission chiefs who responded said they felt constrained in drafting a candid staff report by the expectation of publication.¹⁶ About 14 percent of respondents (partly overlapping with the previous category) indicated that the need to preserve a quality relationship with the authorities caused them to feel constrained in drafting a candid staff report. Concerns regarding the possibility/continuity of a Fund arrangement were not a constraining factor, nor were concerns about the risk of leaks.

64. **Overall, however, mission chiefs believe that the Transparency Policy helps protect both inside and outside candor.** Eighty percent of mission chiefs believe that the current deletions and corrections rules allow for the preparation of candid staff reports, interpreted as inside candor, i.e., vis-à-vis the Board. They also believe that the current rules provide adequate protection against adverse market reactions, and hence support outside candor.¹⁷

65. **Outside candor of staff reports is largely a reflection of inside candor, although modifications have been used to tone down the published version of staff reports.** As discussed in previous sections, deletions and corrections are sometimes used to soften the language in reports, in particular on exchange rate assessment and financial sector risk assessment. Notably, the ex post review of approved deletions suggests that for about 26 percent of deletions, the modifications distorted, albeit usually only slightly, a message of the report.

66. **Survey data suggest that both inside and outside candor may depend on type of economy, raising further concerns about evenhandedness.** The survey found that mission chiefs dealing with emerging market economies appear particularly sensitive to publication expectations (29 percent) and the need to preserve quality relationship with the authorities (21 percent), compared to less than 12 percent and 15 percent respectively for all mission chiefs combined. The survey also finds a higher percentage of mission chiefs in advanced economies, compared to emerging market economies or other developing countries, who said their authorities' requests for corrections/deletions were approved (text



¹⁶ These reflect the responses with “some” or “to a great extent.”

¹⁷ As noted earlier, this view may not be shared by some stakeholders for FSSAs and ROSCs; see paragraph 22.