

The International Financial Institutions, Human Rights and Private Capture

*How Greater Commitment towards Human Rights Can Contribute to
Global Economic Stability*

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1. Introduction

The financial crisis that erupted 2008 in the United States, spread all across the globe and spilled over into the real economy, has unveiled the extreme volatility and interconnectedness of today's global economy. Since then, economic experts, accomplished authors and university professors alike have furthered their arguments as to the causes of this event: their analyses range from liquidity floods (Chandrasekhar 2011) to global imbalances (Helleiner 2011b), from excessive risk-taking behaviour of bankers (Lane and Maeland 2011) to ever-growing income inequality (Stiglitz 2012). Together, they paint a complete picture of the state of today's global economy. At its core, it is one in which private profits and social returns have become increasingly misaligned.

In the words of Stiglitz, “when markets work well [...] it is because private returns and social benefits are well aligned” (2012, 33). Tasked with achieving this balance are national and international regulatory institutions. At the heart of the global economy are the International Financial Institutions (IFIs) IMF and World Bank. Created in 1944 with the experiences of the Great Depression and WWII guiding its creators, it is their mandate to “assure global financial and economic stability” (Stiglitz et al. 2009, 91) and to promote sustainable development and inclusive growth (ibid., 92). Yet not only have they failed to prevent the crisis and to shore up those most vulnerable to it, but they have promoted “policies that are now recognized to have contributed to the creation and amplification of the crisis and to its rapid spread from the U.S., where it originated, to other countries around the world” (ibid., 87). The IFIs have actively contributed to the misalignment of private profits and social returns because they have been captured by private interests (Underhill and Zhang 2008, 536).

This has proven to be particularly harmful to their Member States in which the IFIs operate, for they directly impact the well-being of their citizens. Economic factors and social realities are closely intertwined, a fact recognized by the 1993 United Nations Vienna Declaration and Programme of Action on Human Rights. However, the IFIs are guided in their decisions only by economic

considerations (Bradlow 1996, 54). The meaning and scope of “economic considerations” is up for interpretation, and while the World Bank pays closer consideration to the human rights implications of its operations than the IMF, they both lack clear definitions and operating standards when it comes to human rights. This is problematic because their operations have over the last decades expanded more and more into the social and political sphere. As a result, the IFIs have come under criticism for not only disregarding human rights situations in the Member States, but exacerbating them (Abouharb and Cingranelli 2009, 48).

Private capture has caused the IFIs to prize special interests over the public good. The highest public good is respect for human rights. Since economic and social factors are closely intertwined, greater responsibility by the IFIs towards the promotion and protection of human rights will increase their capacity to fulfil their mandate. *How can the IFIs be reformed in order to prevent private capture and better promote human rights?*

2. Methodology and Operationalization

I will seek to analyse this question by undertaking a literature review on how the international financial institutions should be reformed.

Underlying this research question are two hypotheses:

H1: If the IFIs prevent private capture, they will better promote human rights.

H2: If the IFIs manage to prevent private capture and better promote human rights, they will contribute to a more stable economy.

Private capture shall be defined as the efforts of private financial actors to influence decision-making processes in their favour. As Stiglitz states rather polemically, “[...] private financial firms work to ensure that markets don't work well. [...] Their objective is simply to make markets work for them, to make them more profitable” (2012, 35). They do this by means of:

- lobbying
- intellectual capture
- revolving doors
- structural power

Only the transnational arena shall be of interest, meaning the efforts of private actors in directly influencing international organizations. While the financial industry has made efforts in lobbying the IFIs, they have not been very successful in doing so (Young 2012, 665). This research will thus

mainly focus on more indirect ways in which financial actors have captured the IFIs: intellectual capture, revolving doors and structural power.

Intellectual capture refers to the isolation of knowledge production and assimilation of interpretative options caused by ideological homogeneity (Tsingou 2014, 4). This is facilitated by a phenomenon referred to as “**revolving doors**”. The IFIs and private financial actors have established a close link which has led to IFI officials and bankers moving from one professional ecology to the other (Seabrooke and Tsingou 2009, 3). The transfer of skills is viewed as positive by the IFIs, for they rely on the technical expertise and knowledge of the bankers. In the complex and constantly innovating financial sector, private actors are uniquely positioned to provide IFIs with the technical knowledge and information needed to regulate financial markets. Regulation requires expertise, and that is most easily found among people from the industry (Admati and Hellwig 2013, 204). They wittingly exploit their **structural power**.

The efforts of private interests have led the IFIs to disregard their mandate of balancing private profits and social returns. In so doing, their operations have often worsened human right situations in member countries. The IFIs have, within the scope of their mandate, two ways of furthering human rights:

- **promotion** of human rights in their Member States
- **protection** of human rights

The first involves efforts to improve human rights conditions in their Member States, the latter concerns “the obligations of the IFIs to help stop human rights abuses perpetrated by their Member States” (Bradlow 1996, 51). Since “sustainable development cannot occur without both economic growth and the promotion of human rights” (ibid., 48), it is in the interest of fulfilling their mandate that the IFIs increase their commitment to promote and protect human rights.

In order to support this argument, the paper will first explore the theory underpinning the interconnection of social and economic factors, followed by the consequences that a particular economic dogma, neoliberalism, has had on the stability of the global economy. Afterwards, the responsibility and legal obligations of the IFIs towards human rights will be scrutinized, as well as their actual commitment to human rights promotion and protection. The next section will analyse whether this is affected by private capture and study the IFI human rights record. Finally, recommendations for reform will be forwarded, with the goal of enhancing the efforts of IFIs towards the promotion and protection of human rights, of prevention of private capture, and to

increase their capacity to fulfil their mandate.

3. Theory

3.1 The Interrelatedness of Human Right and Social Realities

Human rights are the highest social good. Every human is entitled to a set of inalienable rights contained in the Universal Declaration of Human Rights of 1948, the International Covenant on Economic, Social and Cultural Rights, and the International Covenant on Civil and Political Rights (the latter two adopted by the UN General Assembly in 1966). All three constitute the International Bill of Human Rights, which took on the force of international law as of 1976 (Council on Foreign Relations). As noted in the 1993 Vienna Declaration on Human Rights, “all human rights are universal, indivisible and interdependent and interrelated” (Article I 5.) It thus recognizes that human rights are affected by the economic, social and cultural context of each society.

Sen takes this argument further when he says that development is not just about economic progress, but about the expansion of freedoms and capabilities of people (Sen 2009, 234). Economic growth is thus not merely an end in itself, but a means to new freedoms that were previously unattainable. For example, higher income might make it possible to gain access to (better) education or health care. In that sense, freedoms are defined as the capability to choose between different ways of living your life within your reach (*ibid.*, 237). However, economic progress does not only preclude an expansion of freedoms, but it is rather a process in which both factors go hand in hand and reinforce each other. Human rights are the most basic set of freedoms every person should enjoy (*ibid.*, 366). For example, Article 5 of the Universal Declaration of Human Rights states that “no one shall be subjected to torture or to cruel, inhuman or degrading treatment or punishment”. In other words, every person has the right to freedom from torture.

From this follows that economic factors alter the social reality. Second, development-oriented economic interventions should not be measured merely by its impact on economic growth. Since the Bill of Human Rights is universally accepted, development should enhance the freedoms and capabilities of any given society. Conversely, if e.g. development aid in the form of purely monetary transactions fails to achieve an increase in capabilities of the persons in need in the recipient area, then this transaction can be seen as irrelevant. “Development is fundamentally an empowering process” (*ibid.*, 249) that “cannot occur without both economic growth and the promotion of human rights” (Bradlow 1996, 48).

Through their economic operations the IFIs impact human rights in recipient countries. This became obvious with the global financial and economic crisis that erupted in 2008, and to which the IFIs have contributed by advancing an economic doctrine that has misaligned private and social returns.

3.2 Market Failures and Regulation: The Current State of the Global Economy as a Misalignment of Private Profits and Social Returns

The decade before the outbreak of the financial crisis was characterized by steady global economic growth (Joyce 2013, 155). This growth was driven by trade liberalization, the global integration of financial markets, and deregulation. Yet today we find that most profits from this era of economic bonanza were produced by a strong financial system that redistributed wealth to the top income percentiles and significantly increased the volatility of the global economy (Stiglitz 2012, 6). This is the result of the predominant economic doctrine since the 1980s: neoliberalism.

According to Stiglitz, a stable economy is one in which private profits and social returns are aligned (ibid., 33). A stable economy is beneficial and prosperous because it “creates a more favourable environment for savers and investors to make intertemporal contracts, enhances the efficiency of financial intermediation, and helps improve allocation of real resources” (Crockett 1997, in Joyce 2013). Yet markets are not inherently stable, they do not provide this balance by themselves. On the contrary, they are beset by market failures, such as imperfect competition and information asymmetries, that prevent markets from being efficient (Stiglitz 2012, 34). Neoliberalism simply ignores these market failures.

The theory underlying neoliberalism is the neoclassical school, which establishes a specific set of conditions under which markets are efficient (Stiglitz 2010, 242-248): that market actors make decisions based on all information available; that they act in an environment of perfect competition; that there is no unemployment, for the demand for labour equals its supply; and that workers get paid according to their marginal contribution to society. Under these conditions, markets are efficient and thus require only minimum government intervention. Neoliberalism takes these conditions as a given. It trumpets the benefits of free markets, who are taken to be, in and of themselves, efficient, self-correcting and thus welfare-enhancing. “Neoliberalism embraced the ideas of classical liberal economics that emphasise market capitalism and free trade, but added a social and moral aspect, which included the reification of the market, a focus on private property, and decreasing government regulation with zeal” (Mueller 2011, 389-390).

Private market actors do not seek to enhance social returns, but to increase their own profits. Market regulations decrease their profits, because regulations are restrictions. “[...] profits where firms are restricted in what they can do will appear to be less than they would be if they were not restricted” (Stiglitz 2010, 265). More so, private actors thrive on the imperfections of the market. “[...] Private financial firms work to ensure that markets don't work well. [...] Their objective is simply to make markets work for them, to make them more profitable” (Stiglitz 2012, 35). They exploit the market failures to their advantage and they try to make sure these are not corrected. It is mainly financial actors that have pushed for deregulated markets. With an increased focus on capital due to cheaper labour costs in the emerging economies and rising productivity due to technological innovations, the US became increasingly reliant on their financial sector. In order to maximize their competitive advantage, the government actively supported and subsidized it (ibid., 82). Neoliberalism plays squarely into the hands of the financial industry because it underplays the role of labour (since unemployment is non-existent) and argues for a market that is most welfare-enhancing if left to its own devices. Furthermore, capital knows no national boundaries. By benefiting special interests, neoliberalism became the driving force of a globalized world economy based on the maxims of privatization, free trade and free capital movements.

Deregulated financial markets increase the volatility of the global economy. They encourage decision-making focused on short-term gains and place a large bonus on risk. The rewards for this behaviour are immense. Financial markets only benefit a small minority. In the United States, the principal advocate of neoliberalism, the top 0.1% has an income “220 times larger than the average of the bottom 90%” (ibid., 2). While the compensation of executives and managers has exponentially increased, income of the average full-time male worker has stagnated in the last 30 years (ibid., 3). As inequality increases at the expense of the working middle class, so does the volatility of the economy because it comes to rely increasingly on debt to fuel consumer demand (ibid., xii). Internationally, reliance on capital flows and lack of regulating mechanisms has made countries vulnerable to negative externalities. An economic shock originating in a foreign country can rapidly expand to other countries, creating a so called “contagion effect” (ibid., 60). Capital movements are mostly pro-cyclical, meaning that while investments abound during economic booms, the opposite occurs during crises. Countries are then hit by retrenchment of private capital, exacerbating economic downturns (Ocampo 2011, 321). These are just some of the reasons why capital market liberalization “does not lead to economic growth; it does, however, lead to increased

instability and inequality” (Stiglitz 2012, 140).

The volatility of today's economy can, on the one hand, be ascribed to the zeal of private financial actors to maximize their profits. The other side of the coin is the failure of public regulatory institutions to provide limits to that zeal. Private actors always seek to circumvent existing regulations and exploit unregulated niches to maximize their profits. Public institutions are tasked with designing policies that balance private profits with social returns and limit socially damaging behaviour. They shape market forces by “setting the rules of the game” and by altering the distribution of wealth and the distribution of financial and human capital (ibid., 30-31). Markets by themselves do not lead to an alignment of private profits and social benefits, but it is up to regulatory bodies to correct the “market failures” (ibid., 34).

The financial and economic crisis from which the world is still recovering is proof that these institutions failed to harness and regulate the destructive forces of unfettered financial markets. By infiltrating the economics profession and public regulatory institutions, neoliberalism rose to be the undisputed economic dogma of the past decades and hugely benefited a small financial elite to the detriment of the rest. At the heart of international finance are the IMF and the World Bank. These international financial institutions (IFIs) were created to assure global economic and financial stability and to foster economic development. The IFIs have been permeated by the same neoliberal agenda that brought about the crisis and have long actively promoted deregulation, privatization, and trade liberalization (Stiglitz 2010, 220). This has come at the expense of human rights.

4. The International Financial Institutions and their Responsibility towards Human Rights

The IFIs impact the human rights situation of its member countries by providing credit to and financing projects in developing countries and those with balance of payment deficits. As established before, the economy and societal factors are intertwined. Both institutions recognize this interrelation and promote institutional and policy reforms in recipient countries by attaching conditionalities to their loans. The quality of the impact of IFI loans on human rights is hotly debated. Yet what stands out is that, despite the recognition by both institutions that their operations affect the human rights situation in recipient countries, they lack any formal commitment to the promotion or protection of human rights. The following section will assess the responsibilities of the IFIs regarding human rights, as derived from their mandate, lending operations and legal status.

4.1 IMF: Mandate and Lending Operations

The IMF has the mandate “to assure global financial and economic stability” (Joyce 2013, 22). It oversees the exchange rate policies of its member countries¹, who have the obligation to provide the Fund with the information necessary to promote a stable system of exchange rates (IMF Articles of Agreement, Article IV Section 3). Furthermore, it provides liquidity to members with a maladjusted balance of payments, thus functioning as a sort of lender of last resort (ibid., Article I (v)). Its primary mechanism for monitoring member states' exchange rate and balance of payment policies are regular consultations with the state.

During crises, troubled countries often have difficulties in accessing private capital markets because they cannot pay the high interest rates charged to offset increased investment risks. This capital is vital for troubled countries in order to prevent default on their debt obligations. In addition, a restructuring of the economy in order to correct their balance of payment is often inevitable. To this end, governments can borrow IMF resources in order to keep fronting their obligations while implementing the proper adjustment policies to address the crisis (Joyce 2013, 10).

To mitigate the risk of these loans and ensure that the recipient country engages in the correction of its balance of payment deficit, IMF loans are disbursed under certain conditions. As stated in the Articles of Agreement (AA), “the Fund shall adopt policies on the use of its general resources, [...] and may adopt special policies for special balance of payment problems, that will assist members to solve their balance of payments problems [...]” (ibid., Article V Section 3). These policies are discussed in Article IV consultations between the IMF and the recipient government and laid out in a letter of intent (Bradlow 1996, 69). The IMF disburses the credit depending on the fulfilment of the performance criteria established in that letter.

At first sight, the IMF fulfils a purely macroeconomic function. While it is certainly the case that the IMF touches on human rights more indirectly, the IMF has over the years interpreted its mandate more broadly to include poverty reduction and the promotion of growth. This entailed a greater involvement with developing countries. Moreover, under the floating exchange rate regime that characterizes today's global economy, social variables such as labour, health and education all affect the value of a country's currency and are themselves affected by adjustments in the balance of payments (ibid., 70). Consequently, the IMF needs to take all these factors into account when prescribing policy conditionalities. The macroeconomic prescriptions of the IMF invariably alter the

¹ The IMF has 188 member countries.

social fabric of the recipient countries.

4.2 World Bank: Mandate and Lending Operations

While the IMF has gradually expanded its role towards poverty alleviation, the World Bank has the express mandate to promote sustainable development and inclusive growth. It does this by providing concessional loans and technical assistance to middle income and low income countries². The Bank defines poverty reduction as an increase of capabilities, echoing Amartya Sen: “Poverty encompasses lack of opportunities (including capabilities), lack of voice and representation, and vulnerability to shocks. The Bank's support for poverty reduction is focused on actions, consistent with its mandate, to increase opportunity, enhance empowerment, and strengthen security” (World Bank 2014). The Bank thus takes a broad-based approach to development, using as a roadmap the Millennium Development Goals (MDGs) (McGroarty 2011, 52). Loans are made to finance projects and institutional reforms that aim to reduce poverty as defined by progress made in these areas.

As happens with the IMF, conditionalities are attached to the loans in order to make sure that they fulfil their intended purpose. They are decided upon in a collaborative process between the Bank and the borrowing government. When applying for a loan, the borrower has to submit to the Bank's Board a Poverty Reduction and Strategy Paper (PRSP) that contains a clear strategy on the use of resources, priorities and poverty reduction targets. The Bank, taking into account the PRSP and their own research, then issues a Country Assistance Strategy (CAS) to the borrower for approval. The CAS contains verifiable targets and benchmarks, on whose attainment depends the continued disbursement of the loan (McGroarty 2011, 88-89). It is the borrower that implements the program, while the Bank evaluates and assesses its progress. If the former does not comply with its contractual obligations, the Bank has the right to cancel the funding (World Bank Program-for-Results Financing).

Regarding the themes and issues that guide World Bank spending, it is pretty clear that they are directly linked to human rights. Some of the Bank's areas of concern, such as a health, education and adequate labour, are specifically mentioned rights in the “Universal Declaration of Human Rights” and the “International Covenant on Economic, Social, and Cultural Rights”. Also, good governance reforms influence the relationship between government and society, relating, among others, to the right to freedom of expression and thought. Similarly, large infrastructure projects

² Defined as GNP/Capita of \$996-\$12,195 and >\$996-\$6,885 respectively, as of April 2011 (McGroarty 2011, 14, 16).

funded by the Bank have implications for a large number of people. However, the Bank's mandate does not mention a specific commitment towards human rights. Neither does the mandate of the IMF. So are the IFIs at all obliged to promote or protect human rights?

4.3 The Obligation of the IFIs towards Human Rights

The AA of the IFIs bear no mention to human rights. As Skogly argues, this forecloses any positive obligation to promote human rights or to fulfil international human rights standards (Darrow 2003, 134). More to the point, the AA specifically mention that only economic considerations should be taken into account in the decision-making processes of the IFIs. Article IV section 10 of the IBRD³'s AA posits that “the Bank and its officers shall not interfere in the political affairs of any member; nor shall they be influenced in their decisions by the political character of the member or members concerned. Only economic considerations shall be relevant to their decisions” (International Bank for Reconstruction and Development Articles of Agreement). The same is mentioned in the IDA's AA under Article V. The IMF is to make its decisions respecting the “the domestic social and political policies of members” (IMF Articles of Agreement, Article IV Section 3 (b)).

Nevertheless, the IFIs are legal entities and subject to international law, consequently obliged to act in conformity with it (Bradlow 1996, 82). However, from that derives no obligation to comply with human rights conventions. For one, because the IFIs are not signatories to them. Second, it is very difficult to make the IFIs directly responsible for human rights violations. They do not engage in systematic human rights violations. Rather, if violations occur, they are indirect consequences of their operations. IFIs would only be directly responsible if they would coerce member states to violate human rights, if the conditionalities would be framed in such a way that it would leave the recipient State no choice but to commit those acts (De Sena 2010, 255). IFIs affect policies through conditionality clauses, “which are unlikely to imply international responsibility on the part of the IMF or the World Bank for human rights violations committed by the [receiving] States” (ibid., 253).

It is with them that the primary responsibility lies concerning human rights. International organizations such as the IFIs are bodies made up by their member states, and it is them who ultimately control the IFIs through their representatives in its highest governing bodies, the Boards of Governors. As signatories to human rights conventions and “as a matter of international law,

³ The World Bank consists of two lending arms: the “International Bank for Reconstruction and Development” (IBRD) and the “International Development Association” (IDA).

governments retain all their human rights obligations when they become members of an international organization and therefore cannot abandon them in their capacity as governing members of the Bank. In that capacity, governments are obliged to exercise due diligence with respect to their human rights obligations” (Human Rights Watch 2013a, 28). For example, member states signatories to the “International Covenant on Economic, Social, and Cultural Rights” have the obligation to prevent negative repercussions of IFI financing operations and general actions on the rights established by the Covenant (De Sena 2010, 259). Avoidance of action would constitute a violation of the Covenant. However, it is very difficult to establish a link between an organizations' action and a member state's failure to prevent it (ibid., 261).

So are IFIs completely absolved of promoting and/or protecting human rights? Not entirely. The IFIs are UN specialized agencies. The charter of the UN tasks all UN-organizations, including its specialized agencies (Article 57, 1.), with the promotion of the universal respect and observance of human rights (ibid., Article 55 c.). This is echoed by the 1993 Vienna Declaration, which calls on the responsibility of the entire UN system in promoting the universal respect for human rights (Article I 6.). While no legal obligations for the IFIs can be derived from this (De Sena 2010, 250-251), Skogly argues that “the Bank and Fund are under a baseline obligation to ‘respect’ human rights as expressed through the UN Charter [...]” (Darrow 2003, 133). Furthermore, Skogly identifies a negative obligation not to violate human rights. He follows that this obligation entails not making human rights situations worse than they already are through their own actions (ibid., 134).

Failing to protect human rights could have consequences for the IFIs. While not of legal nature, it can affect their credibility as UN specialized agencies and impair their ability to fulfil their mandate. The IFIs have the function of providing the public goods economic stability and poverty reduction, yet in order for them to provide it they need the trust of their members that they can actually provide these goods. However, if IFI operations worsen human rights situations of recipient countries, either indirectly through purely economic operations or directly through policy reforms and projects, states could doubt the commitment of the IFIs to fulfil their mandate and thus refrain from asking them for help. The same would be true in the opposite case, in which a positive IFI human rights record could increase their ability to fulfil their mandate. This argument hinges on the commitment of the borrowers to human rights and their willingness to implement the conditions put forward by the IFIs. However, this does not clear the latter from their obligation to do what is in their power to

comply with international human rights standards and prevent human rights violations. As argued by Amartya Sen, “[The recognition of human rights] is, rather, an acknowledgement that if one is in a position to do something effective in preventing the violation of such a right, then one does have a good reason to do just that [...]” (Sen 2009, 373).

4.4 Commitment of the IFIs towards Human Rights

The World Bank has voiced its commitment to human rights in statements and publications: “the World Bank believes that creating the conditions for the attainment of human rights is a central and irreducible goal of development” (IBRD 1998, 2)”. The Bank seeks to limit negative effects of their operations, declaring that “activities that are judged to be likely to have significant adverse impacts that are sensitive, diverse, or unprecedented on the environment and/or affected people [...] are not eligible for Program-for-Results financing, and are excluded from the Program” (World Bank Program-for-Result Financing).

The Bank is guided in its decision-making process by its operations manual that contains social and environmental safeguard policies. However, they include no provisions on human rights. Only once, in the section concerning indigenous peoples, are human rights specifically mentioned. (World Bank 2005). The lack of clear guidelines and safeguard policies on human rights is problematic because it leaves the Bank's staff without guidance on how they should approach human rights concerns (Human Rights Watch 2013b).

Human Rights Watch has criticised that the World Bank is increasingly lagging behind in its human rights commitment, showing that most UN agencies and development organizations, including the Multilateral Development Banks, have adopted human rights policies (Human Rights Watch 2013a, 21-22). It goes on criticising the Bank's few policies that directly refer on to rights: “The Bank has policies on involuntary resettlement and indigenous peoples, but even these policies fall short of international human rights standards” (Human Rights Watch 2013b).

The IMF has a similar issues, although its responsibility towards human rights is more limited due to its focus on macroeconomic issues. As with the World Bank, the IMF only takes into account economic considerations in its decision making. However, its role has expanded into poverty reduction and growth promotion, to the extent where it provides special credit facilities for low income countries with balance of payment problems. The Extended Credit Facility, for example, specifically mentions poverty reduction as a goal, and it comes with policy conditions to safeguard

social objectives (IMF Factsheet Extended Credit Facility). The pillars of IMF's approach to poverty reduction are “implementing sound policies, strengthening institutions, and improving governance” (Krockow and Ramlogan 2007, 44). The IMF does not impose human rights conditions, for it argues that it is outside its area of expertise. Instead, it focuses on its core areas of expertise, the pursuit of macroeconomic stability and macro-relevant structural reforms, leaving the more directly socially relevant aspects to the World Bank (*ibid.*, 44). However, the IMF itself has recognized that economic policies influence human rights (Pereira Leite 2001).

The IMF's primary mechanism for monitoring the balance of payments and exchange rate policies of its members are regular consultations with them (Bradlow 1996, 68). Its AA urges it to “respect the domestic social and political policies of members”, yet this does not equal a prohibition on a voice and opinion on political and social matters (*ibid.*, 81). While human rights promotion should not become a central function of the IMF, the establishment of guidelines concerning human rights could make the IMF more aware of the human rights implications of its macroeconomic operations. As recognized by Péreira Leite, “clearly, the pursuit of economic, social, and cultural rights is an integral part of sound economic policies. Respect for human rights contributes to increased economic and social stability [...]” (2001). A greater responsibility towards human rights protection would thus contribute to the IMF's mandate. It would be a step towards the realignment of private profits and social returns, towards a more stable economy. The IFIs have failed to provide the public good of macroeconomic stability and lost a lot of credibility and legitimacy in the eyes of developing and emerging economies. One of the main reasons for their failure is their capture by private financial interests.

5. Private Capture

Joseph E. Stiglitz names private capture as one of the prime causes of the 2008 crisis (2012). He exposes how the financial industry undertook huge efforts in order to lobby U.S. rule-makers to create legislation advantageous to them (*ibid.*, 48). Even after the financial crisis, continued lobbying has persisted in order to prevent strong regulation of financial activities (The Economist May 17th 2014, 65). Also the IFIs have been captured by private interests to promote neoliberal economic policies. This capture was less the result of direct lobbying efforts, but of a close working relationship between IFIs and banks. The following chapter will examine the channels through which IFIs have been captured, and how this was mirrored in IFI operations increasingly biased

towards the financial industry and to the detriment of macroeconomic stability and human rights.

5.1 Channels of Capture: Lobbying

The capture of regulatory institutions is defined by Young as “the idea that the content of regulation is actively designed by, and in the interest of, the regulated industry itself” (2012, 664). Young, Underhill and Zhang argue that, in comparison to national organizations, international ones are more susceptible to capture. They rely more on technocratic expertise, which is more abundant and specialized in private institutions (ibid., 668). Second, there is a greater distinction between rule-makers and rule abiders. Third, the communities which international organizations are supposed to serve, and to which they are accountable to, are very far away (Underhill and Zhang 2008, 538). As the wider public good they are supposed to provide fades into the background, the checks to the output they produce are weaker. There are several channels through which the financial industry can influence IFI decision-making: via lobbying, “revolving doors”, intellectual capture, and structural power.

Lobbying involves a direct, consistent and systematic effort from organized private sector groups aimed expressively at influencing a regulatory agency's decision-making process (Young 2012, 666). They seek to actively design the content of regulation in their interests (ibid., 664). Indeed, private sector groups organize themselves transnationally in associations and club-like organizations so as to promote their interests (ibid.; Underhill and Zhang 2008; Tsingou 2014). Examples include the Institute of International Finance (IIF), a transnational association of large banks, and the International Swaps and Derivatives Association (ISDA) (Young 2012, 672). Underhill and Zhang detail how the IIF and the ISDA spared no efforts in lobbying the Basel Committee on Banking Supervision (BCBS) in order to influence the drafting process of the BASEL II Accords⁴. Young uses the same example and he affirms that lobbyists indeed had broad access to the decision-making process. However, he opposes Underhill and Zhang in recognizing a causal relationship between the resulting lax regulatory regime and the access enjoyed by lobbyists. That the results match the preferences of the lobbyists does not mean that they have been enacted at their behest. The BCBS was open to consultation with financial sector groups but, “when it comes to making actual decisions on the basis of such consultation, a different picture seems to emerge – one of discretion available to regulators” (ibid., 681). He convincingly argues that “access does not necessarily equal

⁴ The Basel II Accords is an international, non-binding framework aimed at strengthening the banking system via, amongst others, higher minimum capital requirements (Bank for International Settlements 2006).

influence” (ibid., 668). On the contrary, pressure from lobbyists sometimes had the opposite reaction from regulators, hardening their positions. Little evidence can be found of successful lobbying of IFIs, and judging from the evidence presented by Young, one can assume that regulators in the IFIs enjoy the same discretion in their decision-making. Nevertheless, since their preferences have merged and aligned with that of the financial industry, more remote causal factors seem to be at play. Remote factors allude to the context in which actors operate. This is what Tsingou refers to when arguing that “non-state authority in global finance rests primarily on three sets of sources: expertise, material resources and the power of ideas” (2014, 4).

5.2 Channels of Capture: Intellectual Capture, Revolving Doors, and the Structural Power of the Financial Industry

The alignment of preferences between IFIs and the financial industry occurred less through lobbying efforts, but because the ideas prevalent in the private sector spread out into the transnational arena. Gradually, the IFIs became imbued by the neoliberal belief in the efficiency and self-correcting nature of markets. This ideational convergence was promoted by a close connection between bankers and regulators.

For one, both groups have a similar educational background. The IFIs were founded on Keynesian-based economics of market regulation and capital controls. This economic foundation became less and less prevalent as the US started advocating expansionary monetary policies in the 1960s and asserted their central position in financial markets after the collapse of the Bretton Woods system in 1971. This shift was reflected in educational institutions, which, spearheaded by the Chicago School, emphasized the benefits of self-correcting and efficient markets. As regulators still educated in Keynesian economics retired during the 1970s and 1980s, they were replaced by a new cohort of graduates whose education had been centred on the benefits of neoliberal ideas (Joyce 2013, 84). As the prime educational institutions are US and British universities, receiving a Western education is almost a requirement for employment in the IFIs. “[...] In 2001, around 90% of IMF staff with PhDs obtained them from North American or British universities [...]” (Wade 2006, 398). Regardless of nationality, regulators are socialized into a western and neoliberal worldview, contributing to an ideational monoculture within the IFIs.

Not only does the educational background of bankers and regulators overlap, but so do their professional careers. “Examples abound of influential people who spent their careers moving

seamlessly between the private sector, academia, national policy making, and the IMF” (Mueller 2011, 392). Prominent examples are James Wolfensohn, investment banker come President of the World Bank Group, and Timothy Geithner, former Secretary of the US Treasury and now working for a Wall Street private equity firm. The IMF and banks established a close working relationship during the debt crisis of the 1980s. In order to help debt-ridden developing countries attain access to private capital markets, the IMF acted as a mediator between them and the banks. It certified their creditworthiness towards the banks, facilitating private investment, and stepped in with loans so that they could keep fronting their debt obligations (Chorev and Babb 2009, 468). The IMF acted as a sort of Gatekeeper to private resources. However, strict conditionalities were attached to mitigate risk. Because the goal of those IMF programs was to facilitate private funding, the banks could control the conditionalities imposed on the debtor countries, giving “the banks a virtual veto over the approval and financing of adjustment programs” (Joyce 2013, 70). Conditionalities included financial liberalization and privatization of state enterprises.

With financial innovation picking up speed and financial markets growing ever more complex, the IFIs sought out the technical expertise held by professionals in private markets and came to rely on it (Seabrooke and Tsingou 2009, 2). Regulation requires expertise and the IFIs prize the knowledge and expertise that people from the private sector bring to the table. Because of the prevalence of neoliberal economic theories in western education, the complexity of financial markets and a booming global economy, there was little reason to oppose advice from the financial industry. Today “regulators and supervisors [...] tend to have significant numbers of recruits from the [financial] industry” (Admati and Hellwig 2013, 204). Similarly, it is common for regulators to switch over into the private sector (Seabrooke and Tsingou 2009, 3).

This phenomenon, called “revolving doors”, not only promotes the convergence of ideas, but also a convergence of interests. “When regulators are aware that they are likely to become the regulated, for example, they might be more receptive to a particular type of market-friendly regulatory standard [...]” (ibid., 22). Lines between the private and the public become blurred as public officials become detached from their roles of public officials and more receptive towards the interests of the financial industry (ibid., 19).

The prevalence of neoliberal economic theories in educational facilities, the structural power achieved by the financial industry and the reliance of IFIs on private technical expertise has created a mutually reinforcing system that has elevated neoliberalism to an orthodoxy and drowned

opposing ideas. The alliance of these professional ecologies has created an ideational monoculture in the IFIs that dominates its decisions and outcomes. This is what Tsingou refers when speaking of intellectual capture as the isolation of knowledge production and assimilation of interpretative options caused by ideological homogeneity (Tsingou 2014, 4).

6. Impact of IFI Operations on Human Rights

IFI operations, following neoliberal principles, have impacted human rights situations in recipient countries. The World Bank poverty reduction approach lends high importance to the strengthening of private markets in developing countries to develop the conditions needed to attract and retain private investment. This is reflected in its spending. The largest share of World Bank lending in 2010, with 30%, accrued to “Financial and Private Sector Development”. In comparison, very little attention is given to industrial and technological development, with “Industry and Trade” receiving just 2% of the loans (McGroarty 2011, 56).

The IDA, the World Bank lending arm for low income countries, ranks its members on the country's economic management, economic policies, social inclusion, and governance. The ratings determine the size of IDA loans a country has access to. As is to be expected, the ideal country modelled by the Bank follows a very neoliberal and Western model (Wade 2010, 58-59).

The IMF is criticised for serving the interests of its, predominantly Western, creditors. Stiglitz argues that IMF interventions are “designed more to help Western creditors recoup more of their money than they otherwise would have been able to, than to help the afflicted country maintain its economic strength” (Stiglitz 2010, 215). Similarly, Mueller argues that the concessional loans through the Extended Credit Facility (ECF) benefit a financial elite (Mueller 2011, 394). The conditions include the familiar battery of “reducing government spending through privatisation of state enterprises, reduction of the civil service and cutting spending for social services; devaluing currency to make exports cheaper and raising interest rates to encourage foreign investment; and removing trade barriers by ending price controls and establishing tax-free zones for foreign corporations” (Mueller 2011, 394). In so doing, Stiglitz finds that IMF-lending has often exacerbated economic downturns (2010, 215).

The IFIs have not always paid much attention to the social consequences of their economic policies. By promoting the aforementioned neoliberal policies, they have effectively restricted the freedoms and capabilities of a large number of people in the developing countries. Through privatization of

state enterprises, drivers of economic activity in many of the poorest countries, they have lowered the standard of living of many to the benefit of a few. Their weakening of trade unions and insufficient attention to social protection can be seen as direct violations of the International Covenant on Economic, Social and Cultural Rights. The promotion of austerity measures have a direct effect on a government's capacity to ensure basic health services, provide education and social protection to its citizens. Reliance on foreign capital leaves developing countries with no political space to engage in counter-cyclical measures and without leverage to withstand IMF conditionalities.

Abouharb and Cingranelli studied the effects of IFI lending on physical integrity rights between 1981 and 2003. They present evidence that the respect for physical integrity rights in recipient countries worsened while countries were under IMF or World Bank programs (2009). “The more years a developing country government spent under IMF programs between 1981 and 2003, the greater the use of torture and extra-judicial killing and the worse its score on the Political Terror Scale” (ibid., 49). Their hypotheses as to presumed causal links are speculative in nature, however. They argue that, as IFI programs lead to cutting of social programs, these result in protests and riots by the poor (ibid., 50). Similarly, opposing political forces might oppose policy changes and take to the streets. Governments then answer with increased repression. Another possible explanation is that weakening of state power due to market-enhancing reforms lead to worse human rights situations. Promotion, protection and monitoring of human rights require large investments that the state might no longer be able to support (ibid.).

Their evidence is contradicted by Eriksen and De Soysa (2009). In their own words, “receiving loans from the IFIs has positive effects on government respect for physical integrity rights [...]” (ibid., 486). They justify their finding with the argument that neoliberal conditions are unlikely to be the cause for HR violations, because the loans are gradually disbursed depending on the fulfilment of the terms set by the IFIs (ibid., 487). Also, signing a conditionality agreement does not mean it is actually implemented (ibid., 490). This is contradicted by Abouharb and Cingranelli, who argue that mere loan negotiations between IFIs and borrowers are enough to spark riots and cause repression (2009, 51). Also Eriksen and De Soysa's argument comes with caveat: government respect for human rights turns negative when loan payback exceeds new IFI disbursements (2009, 487).

Quantitatively, the direct implications of IFI operations on physical integrity rights are unclear. However, these studies do not account for social, cultural and economic rights. This gap can be

filled by looking at case studies, which also prove the occurrence of abuse of physical integrity rights. Only recently, Human Rights Watch submitted a report deploring the lack of commitment from the World Bank to the protection of human rights (2013a). World Bank projects in Ethiopia have forced the relocation of 1,5 million people under conditions “marred by intimidation and violence, with state security forces repeatedly threatening, assaulting, and arbitrarily arresting villagers who resist transfer” (ibid., 2). Several deaths were reported and the area of relocation provided for a worse living than before. Another case study reports World Bank funding of drug detention centres where severe human rights abuses were well documented and regularly committed (ibid., 39-40). Both the IMF and the World Bank have been severely criticised for their use of structural adjustment policies in developing countries during the 80s and 90s, leading to a “lost decade” for the debtor countries (Joyce 2013, 69). Similarly, the IMF has been widely criticised for its handling of the 1997-1998 East Asian crisis, in which it imposed a large amount of conditionalities on the debtor countries that only worsened the economic downturn (ibid., 116-117). These cases show that, even though the overall impact of IFI operations on human rights is disputed, human rights abuses or worsening of human rights situations certainly do occur through IFI interventions. And these are not exceptions to the rule. These cases justify the call for the recognition of responsibility concerning human rights on the part of the IFIs. Furthermore, the protection of human rights goes hand in hand with ensuring macroeconomic stability and poverty reduction. By contributing to a volatile economy and a crisis that has worsened the living situations of many, the IFIs have failed their mandate. This has cost them in terms of legitimacy and credibility in the eyes of developing countries, who “would have to be on [their] death bed[s] before turning to the IMF” (Stiglitz 2010, 215). Increasingly, countries have looked for alternatives to the IFIs. Emerging and developing countries have built up large currency reserves of their own, or entering in regional arrangements to pool resources, in order to protect themselves from crises. “[...] the emerging market economies effectively decided that the cost of acquiring and holding reserves were less than those of entering an IMF program. The accumulation of reserves for the purpose of self-insurance, therefore, represented a sign of “no confidence” by the emerging markets in the IMF” (Joyce 2013, 150). The mentioned “cost” refers not only to the economic, but also to the social costs. This contributes to economic volatility by adding to global current account imbalances. As occurred in the run-up to the 2008 crisis, the accumulation of reserves meant large capital inflows to the US, which kept interest rates low and fuelled its financial bubble (Helleiner 2011a, 570). The

ultimate manifestation of the lack of confidence in the IFIs was the establishment by the BRICS of their very own New Development Bank on July 15th 2014. This bank is meant to function both as lender of last resort and a development bank (BBC News Business).

Economic policies have social consequences that need to be accounted for. By succumbing to private capture, the IFIs have benefited special interests and not exclusively served the public good. Reforms to prevent private capture and increase accountability towards human rights could restore some of their legitimacy.

7. Reforms

The first thing to acknowledge is the urgent need for clear guidelines and operational policies on human rights that comply with internationally recognized standards. The positive consequence of the adoption of such guidelines would be numerous. For one, it would increase the transparency of its decision-making processes. The AA of the World Bank forbid it to consider non-economic influences, and it defines economic factors as everything that has a direct and obvious economic effect (Bradlow 1996, 60). Since many social factors can have “economic effects”, the Bank's interpretation of it varies from case to case and makes the consideration of social factors arbitrary (except the ones contained in its social safeguards policies). A clear commitment to human rights would help the Bank's staff to assess the human rights risks of their projects. It would help borrowers in devising the Poverty Reduction Strategy Papers, because the requirements for Bank funding are more clearly defined. And it would increase the accountability of the Bank towards human rights abuses.

To a lesser degree, this applies also to the IMF. The IMF's mandate is concerned with macroeconomic factors, and the IMF rightly refers to that when asked about the social implications of its programs. However, its increased interventionism and expansion into the field of poverty reduction warrant clearer guidelines on human rights. The IMF should concern itself mostly with human rights protection. Both the Bank and the IMF should devise human rights impact assessments, to be taken into account when designing operations (Human Rights Watch 2013a, 24). As this is not the field of expertise of the IMF, these assessments could be carried out by the World Bank or in cooperation with public experts. The IMF is not forbidden to voice concerns over the domestic social and political affairs of its members (Bradlow 1996, 81). It could raise its efforts in addressing such issues during Article IV consultations. Furthermore, the IMF can actively play a

role in limiting negative human rights impacts of its operations through conditionalities. Already it seeks to prevent cuts in social protection spending while borrowing countries undergo austerity programs. However, despite increased IMF commitment in this area, due to overall budget-cut requirements the spending of recipient governments on social protection is still reduced (Rowden 2009, 4). The IMF can do more in this regard, for “there was a tendency of the IMF and finance ministries to continue to view public sector spending and public sector workers only as “costs” and not as providing benefits to the economy or society” (ibid., 23). Some of the explanations forwarded by Abouharb and Cingranelli concerning negative human rights consequences of IMF programs relate to social unrest caused by actual or attributed negative social effects of imposed austerity programs (2009). Greater concern by the IMF towards protection of social spending could over time better its image and cause fewer riots that trigger government repression.

Stricter standards should be applied to the World Bank. In order to ensure that its operations do not exacerbate human rights situations, the Bank should follow procedures similar to the ones applied to Indigenous Peoples and Involuntary Resettlement: full assessment of potential human rights impact; prior consultation with affected individuals; design measures to avoid adverse impacts, or, when avoidance is not feasible, to minimize or compensate for such effects; include a framework for continued consultation with the affected communities during project implementation; and close monitoring of the project (World Bank 2005). The Bank could involve specialized human rights organizations to assist in these matters.

The World Bank has political room to not only increase their efforts in human rights protection, but also in its promotion. The maximization of positive human rights impacts is consistent with its mandate of poverty reduction (Human Rights Watch 2013a, 6). Between 2001 and 2009, the overall percentage of IDA lending operations aimed at “social development and protection” and “human development” was extremely low, with just about 5% and 13% respectively (De Sena 2010, 266). In 2010, the IBRD and IDA together invested only 2% of its disbursed loans in “social development, gender & inclusion” and 14% in “human development”, compared to 30% loan share in “financial and private sector development” (McGroarty 2011, 56). Only 2% was spent on “industry and trade” (ibid., 56). By funnelling more funds into human and social development, the Bank would have a much more positive human rights impact. In fact, it would help the Bank concentrate more on poverty alleviation in a stricter sense instead of overlapping with the IMF in strengthening markets and promoting private sector development. Furthermore, the Bank could promote human rights by

requiring that recipient governments take human rights into account when devising and implementing their PRSP. Bank funding would then be conditional on human rights improvements as defined by the benchmarks set in the PRSP.

Measures against private capture could facilitate human rights reforms. Baker proposes to combat the problem of “revolving doors” by “enforcing legally defined time periods during which a former regulator could not move into the regulated industry, or someone from a regulated industry into a regulatory position” (Baker 2010, 657). Helleiner argues for mandatory public disclosure of all past and present industry ties of individuals of regulatory bodies (2011a, 570). While these measures would certainly help prevent private capture, measures of this kind could impair the ability of IFIs to attract the expertise they need. Having demonstrated that private capture is mainly about the predominance of a certain set of ideas, in the end the question of private capture prevention becomes one of increasing the variety of ideas present in the organization. The problem is thus a structural one. To solve it demands increasing the voice and voting shares of underrepresented countries and recruit staff with more diverse educational backgrounds. This would ensure that a wider array of interests are adequately represented, providing a stronger check to the predominant interests and ideas, and offering more alternatives when it comes to policy prescriptions.

The IFIs cannot be expected to be the leading international organizations in the promotion of human rights. However, as UN specialized agencies and subjects to international law they have the responsibility to at least not exacerbate human right situations. Furthermore, greater attention to the social conditions of recipient governments could help restore some of their lost legitimacy in the eyes of developing countries. Human rights epitomizing public goods, the IFIs would be perceived less subject to special interests. Furthermore, the proposed reforms would provide checks against private capture. Closer involvement of stakeholders would increase ownership of the public in the IFIs. By increasing the transparency of their decision-making processes, special interests might find it more difficult to circumvent the established operating standards to their advantage. By increasing the accountability of the IFIs towards human rights, management and staff are incentivized to comply with the regulations. All in all, these measures would contribute to readjust the balance of private profits and social returns the IFIs are meant to safeguard in order to stabilize the global economy.

8. Conclusion

The 2008 crisis has largely delegitimized the neoliberal principles that have guided the work of the IFIs. The intellectual tide is turning and there is now increased political salience for financial regulation (Baker 2010, 656). In responding to the crisis, the IMF softened its stance on pro-cyclical austerity measures, promoting the need for fiscal stimuli. Both IFIs stepped up their loan commitments and helped prevent the bankruptcies of member countries. Where they previously promoted financial deregulation, the IFIs now recognize that certain kinds of capital controls can increase macroeconomic stability (Joyce 2013, 171).

The G-20, in an effort to maintain the relevance of the IFIs, have pledged to make them more inclusive. In 2011, the emerging and developing countries saw their voting power in the IMF increase by 5,3%. So has their number of executive directors (Ocampo 2011, 325). Also, the G-20 promised that the head of the IMF would be chosen openly and transparently without regard for nationality (Stiglitz 2010, 216). However, the issues human rights and private capture were kept off the reform agenda (Helleiner 2011a, 570). Decisive action on these topics is essential. Neoliberalism may presently be disfavoured, but when the economy recovers there will be less urgency and incentives for reform. Private capture is pro-cyclical in nature precisely because the wider public is less interested in matters of regulation during financial booms (Baker 2010, 648). That is why structural reforms are needed now.

The question about the responsibility of the IFIs towards human rights is ultimately a question about their legitimacy in being able to work for the common good. The decisive actions of the IFIs during the crisis demonstrated that they are still relevant organizations. The volatility of today's economy makes organizations that allow for the international coordination of economic policies indispensable. Economic and social factors are closely intertwined. Committing to the promotion and protection of human rights will help regain some of that trust in the IFIs and enhance their capacity to provide for macroeconomic stability and development.

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