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Many companies have found it useful to define their main objective in a mission statement. To the outsiders the mission statement projects a clear and preferably positive image of the company. To the insiders it provides a sense of common purpose.

When the Articles of Agreement (Articles)[1] of the International Monetary Fund (Fund) were adopted at the Bretton Woods conference in 1944, the concept of mission statement did not exist. However, the drafters of the Articles found it useful to set forth the purposes of the Fund in Article I and to state that the Fund would be guided in all its decisions by these purposes. These purposes clearly demonstrated the monetary character of the Fund: it was established to promote the stability of exchange rates, the financing of balance of payment deficits, and the liberalization of payments for current international transactions. In contrast, the Fund's sister organization, the International Bank for Reconstruction and Development (World Bank), was established as a development agency.

The successive amendments of the Fund's Articles in 1969, 1978 and 1990 did not change the monetary character of the Fund. Actually, the first two amendments strengthened the role of the Fund as the central monetary institution. The first amendment (1969) gave the Fund the power to supplement existing reserve assets through allocations of special drawing rights in order to meet "the long-term global need, as and when it arises, for additional liquidity in the world."[2]

The second amendment (1978), drawing on the failed experience of the par value system, recognized the freedom of Fund members to adopt exchange arrangements of their choice, which legalized the practice of floating currencies. The same amendment, however, gave the Fund two new mandates, both of which expanded its role as a monetary institution. One was to oversee the international monetary system to ensure its effective operation. The other was to oversee the compliance by members with their newly defined obligation to cooperate together and with the Fund in the conduct of their economic, financial, and

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1. Articles of Agreement of the International Monetary Fund, *available at* http://www.imf.org/external/pubs/ft/aa/ [hereinafter Articles of Agreement].

2. First Amendment to Articles of Agreement, July 28, 1969.

exchange rate policies "to assure orderly exchange arrangements and to promote a stable system of exchange rates."[3] More specifically, the Fund was required to exercise "firm surveillance" over its members' exchange rate policies, with a view in particular to avoiding competitive exchange rate depreciation for fear of a return to the pre-World War II "beggar thy neighbor" policy of some countries.

Although the monetary character of the Fund is still enshrined in its Articles, a profound evolution has taken place gradually, which now results in sharply contrasting views as to what should be the role of the Fund. This evolution has affected both the jurisdiction of the Fund as a regulatory agency and its balance of payments assistance as a financial agency. In both cases, there has been a substitution of broad judgment-based powers for rigid and objective rules. The replacement of the par value system by the exercise of surveillance has given great latitude to the Fund to define the scope of its involvement in its members' external and domestic policies. The invention of conditionality in the early years of the Fund, followed by the implicit, and later explicit recognition of the Fund's authority to adopt different policies on the terms and conditions of its financial assistance (including the possibility of specifying different rates and maturities for different policies), in order to address different balance of payments problems, have given the Fund the power to withhold or grant assistance on a case-by-case basis and to determine the cost and duration of its assistance with a large degree of flexibility. This power was even strengthened by allowing the Fund, at the time of the second amendment, to provide concessional assistance (including grants) to developing countries, this assistance being funded from the profits on the sale of gold held by the Fund at the time of the second amendment.

Consequently, it is not surprising that the existence of such powers should lead to attempts to steer the course of the Fund's activities in new directions. National governments or groups of governments (such as the Group of Seven: Canada, France, Germany, Italy, Japan, United Kingdom, and United States, also known as the G-7), international organizations (such as the U.N.), and nongovernmental organizations (NGOs) hold and express views (sometimes conflicting) about the actions the Fund should take or refrain from taking. For instance, should the Fund refrain from providing assistance to countries blacklisted by the U.N. General Assembly, the U.S. Government, or the Financial Action Task Force, because these countries violate human rights, harbor terrorists or war criminals, or do not cooperate in the fight against drug trafficking or money laundering? Vice-versa, should countries that cooperate in the fight against terrorism, drug trafficking, or money laundering be rewarded with generous Fund financing? Should the Fund engage in debt forgiveness in a systematic fashion as proposed by some countries and NGOs? Should the Fund use its leverage to liberalize trade and capital movements? Should the Fund ensure compliance with the core labor standards adopted by the International Labour Organization?

All these attempts, successful or unsuccessful, to use the Fund for different objectives have led to a blurring of its image as a monetary institution. Another factor is the simplification inherent in any form of communication through the mass media. Thus, in press communiqués issued at the end of international meetings, the Fund, the World Bank, and regional development banks are usually referred to as the "international financial institutions" (IFI), as if they were as fungible as the money they provide. Partly for the same reason, the terminology used for development banks' operations is used to describe the

3. Second Amendment to Articles of Agreement, Apr. 1, 1978.

Fund's financial transactions with its members. These transactions, which are the vehicle for Fund assistance from its General Resources Account, take the form of exchanges of currencies. Technically, the Fund sells foreign exchange against the purchasing member's currency. These exchanges of currencies (called "transactions") were designed to follow the model of currency swaps, for monetary intervention, between central banks. However, they are commonly described as loans, even in some Fund publications, which make them appear to be commercial bank loans. Similarly, while the objective of the Fund's assistance is very specific, in that it is intended to help the recipient country overcome a balance of payments problem, governments often find it politically preferable to present this assistance as a source of financing for domestic expenditure (budget deficit, sectoral lending), a clearly more understandable and attractive objective for the local populace.

Another reason for the present confusion between the respective roles of the Fund and development banks is that, instead of referring to the immediate purpose of the Fund's assistance (i.e., the resolution of a member's balance of payments problem), this assistance is presented in terms of the country's ultimate objectives, which are the resumption of economic growth and, for poorer countries, the reduction of poverty. At this level of generality, all international financial institutions appear interchangeable. In particular, the separation between the Fund and the World Bank seems rather artificial, and their merger may seem to be an inescapable consequence of this evolution. The common initiatives of the Fund and the World Bank for Poverty Reduction and Growth and for Heavily Indebted Poor Countries illustrate this trend. There is no doubt, however, that a movement in the opposite direction has found some support. Efforts have been made to better define the respective roles of the Fund and the World Bank. There have also been proposals to circumscribe the role of the Fund, not unlike that of a central bank, to short-term financing for external liquidity problems and systemic risks.

There is a play by Luigi Pirandello about six characters in search of an author. The Fund is more like a single character with many playwrights, being asked to play the jack-of-all-trades and to be available for any objective that needs to be achieved through the exercise of its powers.

The evolution that has taken place since the inception of the Fund has affected the two main aspects of the Fund's mandate: the exercise of its jurisdiction and the provision of its financial assistance. In addition, it has affected the Fund as an institution, both internally (powers and structure of its organs) and externally (relations with the membership and with other organizations). Those three aspects (jurisdictional, financial, and institutional) will be examined in turn.

## I. Jurisdictional Aspects

As a regulatory agency, the Fund oversees the compliance of its members with those obligations under the Articles that constitute the Fund's code of conduct. These obligations fall into two categories and are listed in two different Articles. Article VIII, sections 2(a) and 3 prohibit restrictions on current payments, multiple currency practices and discriminatory currency arrangements, except in certain circumstances. Article IV requires members to collaborate with the Fund and other members to assure orderly exchange arrangements and to promote a stable system of exchange rates.

The first category of obligations has remained unchanged since the original Articles, while the second was introduced by the second amendment, which may explain the sharp contrast in their respective formulations. The obligations in Article VIII are obligations to

refrain from taking certain actions in the area of exchange controls and exchange rates. Therefore, once the meaning of these terms is understood, the scope of these obligations is clearly delineated.

In contrast, the obligations set forth in Article IV are defined in terms of the objectives to be pursued rather than in terms of actions to be taken or avoided; they are broadly but loosely formulated, and reassuringly take into account the capacity of each member to comply. This means that, if there is a dispute on the scope of a member's obligations under Article IV, an interpretation of this provision will be required, and the Fund itself will be the final interpreter.[4] Therefore, the loose formulation of Article IV—with a proliferation of adjectives such as "sound," "orderly," or "reasonable," all of which denote subjective criteria—also gives ample room to the Fund, when implementing this provision, to define the obligations of its members either in general terms or on a case-by-case basis. In some countries, had it been part of their national legislation, Article IV might have failed to pass the constitutional requirement of sufficient precision to ensure predictability of result and uniform treatment. This is only one of the odd features of this provision which, after twenty years of application, remains in many respects unclear and, probably for that reason, has become a key element of the Fund's expanding role. Napoleon said that a constitution must be short and obscure. Article IV is not short but it is indeed obscure.

## A. Liberalization of International Payments (Article VIII)

This aspect of the Fund's regulatory powers is often referred to as the Fund's approval jurisdiction: three types of measures (exchange restrictions on current payments, multiple currency practices, and discriminatory currency arrangements) are prohibited unless they are approved by the Fund. The Fund's approval is granted on the basis of criteria that are formulated in general decisions of the Fund. For instance, an exchange restriction may be approved only if it is temporary, justified by balance of payments reasons and nondiscriminatory (i.e., no discrimination among Fund members). An exception is made for restrictions imposed for reasons of national or international security, which are not subject to those conditions.

The rules governing the Fund's approval jurisdiction have remained remarkably stable since the inception of the Fund. Yet, in recent years, two related issues have attracted the attention of Fund members. The first one is really not new at all: it is whether Article VIII, section 2(b) should be revived, through interpretation and/or amendment, to help countries facing a major debt crisis. The second one is whether the Fund's approval jurisdiction should be extended to cover capital movements.

### 1. *Article VIII, Section 2(b)*

When a company becomes unable to meet its liabilities, it files for bankruptcy. This has two consequences: first, it imposes a stay on creditors' actions, which gives time to decide whether the company can be rehabilitated or should be liquidated; and second, it gives jurisdiction to a court, which will monitor the negotiations between debtor and creditor and rule on disputes between them.

There is no similar procedure for states. The traditional justification is that a state does not become insolvent because it can always levy taxes. However, insolvency is not the rele-

4. Articles of Agreement, *supra* note 1, art. XXIX.

vant test for the initiation of bankruptcy proceedings. The test is illiquidity and a state may be as illiquid as a private debtor, particularly when it is indebted to foreign creditors whose claims are payable in foreign exchange. For those payments, the ability to print local currency does not help if there is not enough foreign exchange in the country's economy. Foreign exchange has to be earned or borrowed ahead and, in the meantime, the state's foreign debt cannot be serviced. Exchange controls and surrender requirements may be imposed but they have a negative impact on the country's economy.

From time to time, and particularly when a major crisis strikes, suggestions are made for the creation of an international bankruptcy court or at least for an equivalent mechanism, but usually the interest generated by those suggestions wanes as soon as the crisis that prompted them is over.

In 1995–96, both the Fund and the Group of Ten studied the feasibility of creating an international bankruptcy court. The conclusion was that this creation would raise many difficulties and the world community was not ready for it. More recently (2001), however, the First Deputy Managing Director of the Fund has proposed the creation of a sovereign debt restructuring mechanism for states whose external debt has become unsustainable.

As an alternative and more modest proposal, various proposals were made in the midnineties and use Article VIII, section 2(b) as a proxy for a stay on foreign creditors' actions. Assuming that a government imposes a moratorium on payments by resident debtors to their foreign creditors, this measure would constitute an exchange control regulation. This restriction, to the extent that it affected current payments, would have to be approved by the Fund; if it affected capital movements, it would not require Fund approval. Under Article VIII, section 2(b), once an exchange control regulation is found to be consistent with the Fund's Articles of Agreement, which would be the case here, exchange contracts contrary to that regulation cannot be enforced in the courts of other countries. Therefore, in the case of a moratorium, other countries would have to cooperate with the country imposing the moratorium by refusing to enforce the creditors' claims in their courts.

If Article VIII, section 2(b) could be used to suspend enforcement of exchange contracts against private debtors, why not use it to suspend their actions against sovereign debtors?

This was a very attractive suggestion, but it raised some difficulties. The first problem was that, in order for a moratorium to constitute an exchange control regulation, it has to apply to persons other than the government imposing the moratorium. It is well established in the law of the Fund that a government's default on its own debt is not an exchange restriction. Therefore, it is outside the scope of Article VIII, section 2(b). This would seriously limit the usefulness of resorting to that provision.

The second problem was that Article VIII, section 2(b) had already been interpreted rather restrictively by the courts of some major countries. In the United Kingdom and the United States, courts have taken the view that Article VIII, section 2(b) applies only to a very limited type of debts: those that arise from a contract for the exchange of currencies. This interpretation is based on the reference to "exchange contract" in Article VIII, section 2(b), a somewhat ambiguous concept, which has been interpreted more broadly by the courts of other countries. Moreover, in Germany, the courts have decided that Article VIII, section 2(b) does not apply to restrictions on capital movements, in part because it is inserted in a provision, of which the first section deals exclusively with restrictions on current payments.

As it is not easy to amend the Fund's Articles or to adopt an interpretation that would contradict the judicial interpretation that prevails in some major countries, there has been no further attempt in either of those directions. However, the possibility of an amendment

or an authoritative interpretation of Article VIII, section 2(b) by the Fund has not been ruled out and is raised from time to time in discussions among Fund members.

The current emphasis on the need to cooperate against financial crime, in general, and money laundering, in particular, creates a new perspective. Since a payment or transfer in violation of exchange controls is a crime, countries that have undertaken to cooperate against all forms of financial crime should take action against the laundering of the proceeds of this crime in their territories and, in particular, against laundering through their banking system. It is not clear, however, whether this cooperation should include a duty to impose a stay on creditors' actions in their courts. If it did not, however, the courts would be allowed to order a payment that would constitute the commission of a crime against the laws of the country imposing the moratorium.

2. *Capital Movements*

The drafters of the Fund's Articles were ambitious but they were also realistic. After the end of World War II, an immediate priority was the resumption of multilateral trade, which required a liberalization of current payments, but a premature liberalization of capital movements could have undermined the fragile post-war economies. Therefore, the sovereignty of members with respect to exchange controls on capital movements was preserved; restrictions on capital movements could be imposed without Fund approval.[5] However, while Fund members could have access to the Fund's financial assistance for their current account deficits, they could not use the Fund's resources to meet a large or sustained outflow of capital, and the Fund could request a member to exercise controls to prevent such use of the Fund's resources.[6]

Since Bretton Woods, the situation has changed radically. Capital markets have become a major source of financing both for private and sovereign debtors. A number of bilateral or regional agreements liberalizing capital movements have been entered into (e.g., European Economic Community, NAFTA, and OECD) and the General Agreement on Trade in Services (GATS) contains provisions on the liberalization of service-related investments. Economists generally recognize the beneficial effect of a liberalization of capital movements as it allows investors to make the best possible use of their savings and entrepreneurs to expand their activities. There is also an indirect benefit for the governments of both parties as they are able to collect more taxes, not to mention other benefits for the recipient country such as economic growth and, with the creation of new enterprises through direct investment, the transfer of knowledge.

However, this rosy picture must be nuanced. The freedom of capital movements increases the risk of sudden outflows of capital when there is a loss of confidence in a country's ability to service its external debt. There may also be political reasons for preventing foreigners from acquiring dominant positions in strategically important sectors of a country's economy (e.g., armaments, telecommunications). Finally, many countries require local savings to be invested locally in order to provide public and private borrowers with inexpensive resources, while the cost to them would be greater if they had to compete for the same resources with foreign borrowers.

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5. *Id.* art. VI, § 3.
6. *Id.* art. VI, § 1.

For all these reasons, a liberalization of capital movements will usually be a gradual process. It must be accompanied with adequate macroeconomic and structural policies that will generate confidence in the country's economy and build up a domestic financial system able to prevent or withstand possible shocks.

When the suggestion of an amendment of the Articles was put forward by some members a few years ago in the Fund, the initial reaction was rather favorable. At the 1997 Annual Meeting of the Board of Governors, the Interim Committee of the Board of Governors on the International Monetary System (generally known as the Interim Committee and now replaced by the International Monetary and Financial Committee) endorsed the principle of an amendment that would make the liberalization of capital movements one of the purposes of the Fund and give the Fund jurisdiction over such movements.

Soon thereafter, however, in the wake of the Asian crisis, the process began to unravel. In some developed countries, trade unions denounced capital liberalization as a ploy to transfer investments to countries where labor was cheap and unregulated. Some NGOs claimed that the globalization of the economy was a threat to the environment. A number of developing countries were concerned that capital liberalization would undermine their weak economies and generate instability. Some developed countries were concerned that their laws against foreign investment in strategic sectors would have to be repealed.

A counter-proposal was put forward by one member. Instead of expanding the Fund's jurisdiction by creating obligations for all members, why not rather use the Fund's conditionality and make capital liberalization a condition for the Fund's financial assistance? Thus, users of Fund resources would have to open their territories to foreign investments, which would be highly beneficial for them since they were mostly developing countries. In contrast, developed countries, which do not use the Fund's resources, would not be subject to this liberalization. However, this proposal had very little support because it implied that capital liberalization would be forced by the Fund upon reluctant countries that had no choice but to submit to the Fund's yoke. Not only would it give capital liberalization a negative connotation, but also this liberalization would probably be short-lived, as countries, once free from Fund conditionality, would probably revert to their earlier practices.

A compromise proposal, prepared by the staff, was to liberalize capital movements in two stages. The first stage would liberalize all payments and transfers for capital transactions once the transactions themselves had been liberalized. The process would be very similar to the liberalization of current payments. Under the Fund's Articles, payments for trade transactions may not be restricted if the trade transactions themselves are permitted. There is no obligation to authorize payments for illegal trade transactions. Therefore, by analogy, assuming that a particular investment is permitted, all payments and transfers relating to the investment would have to be permitted. If a disinvestment was permitted, the repatriation of the proceeds could be made.

The second stage would be a gradual liberalization by each member of capital transactions. There would be no timetable, no obligation to liberalize but, once a type of transaction had been liberalized, no restriction could be imposed without Fund approval. The main incentive for liberalizing would be investor confidence. The Fund would not force countries to liberalize, including through the use of its conditionality. This would be a purely voluntary, "à la carte" process.

This proposal has not been discussed by the Executive Board and, for the time being, capital liberalization is no longer on the Fund's agenda.

B. Surveillance (Article IV)

The present Article IV is a product of the second amendment (1978) of the Fund's Articles of Agreement and it can only be understood in light of what was called the collapse of the "par value" or "gold exchange" system that had been in place since the inception of the Fund.

The original Article IV, as adopted at the Bretton Woods Conference, required Fund members to establish a par value either in terms of gold or in terms of the 1944 (gold) U.S. dollar and to maintain exchange rates within a margin of 1 percent above or below parity. The parity was calculated on the basis of the respective par values of the currencies of Fund members. The obligation to maintain exchange rates based on parities could be performed by imposing fixed exchange rates or through market intervention. An alternative way was for a country to stand ready to exchange its currency for gold. In practice, all countries but the United States adopted the former approach while the United States adopted the latter. Therefore, the dollar rather than gold was seen as the anchor of the system as most countries effectively maintained exchange rates in terms of the U.S. dollar as the dollar was deemed to be as good as gold.

Under the par value system, changes in par value could take place but—beyond an initial threshold—only with the consent of the Fund and to correct a fundamental disequilibrium. In reality, however, some unauthorized practices developed: some devaluations took place without the consent of the Fund and some countries let their currencies "float" outside the permitted margins. More importantly, the decision of the United States in 1971 to suspend the convertibility of the U.S. dollar into gold marked the end of the par value system, if not *de jure* at least *de facto*.

During the following years, an intense debate pitted the supporters of fixed exchange rates against those of floating rates. The outcome was the new Article IV as adopted at the time of the second amendment.

The new provision was a political compromise with the necessary calculated ambiguities to allow both sides to claim victory. The general idea was that, instead of either requiring the maintenance of fixed exchange rates or giving full freedom to members, there would be a general obligation for all members "to collaborate with the Fund and other members to assure orderly exchange arrangements and to promote a stable system of exchange rates."[7] Therefore, instead of the former obligation to achieve a certain result, there is now an obligation to cooperate toward common goals.

In order to give more concrete substance to this rather vague obligation, Article IV lists specific obligations, which do not exhaust the scope of the obligation to cooperate but provide guidance to the Fund and its members in the implementation of Article IV. Moreover, in order to make these obligations effective, the Fund was given the mandate to oversee the compliance of each member with these obligations.

These principles were reflected in Sections 1 and 3 of Article IV.

Section 1. *General obligations of members*

Recognizing that the essential purpose of the international monetary system is to provide a framework that facilitates the exchange of goods, services, and capital among countries, and

7. *Id.* art. IV.

that sustains sound economic growth, and that a principal objective is the continuing development of the orderly underlying conditions that are necessary for financial and economic stability, each member undertakes to collaborate with the Fund and other members to assure orderly exchange arrangements and to promote a stable system of exchange rates. In particular, each member shall:

(i) endeavor to direct its economic and financial policies toward the objective of fostering orderly economic growth with reasonable price stability, with due regard to its circumstances;
(ii) seek to promote stability by fostering orderly underlying economic and financial conditions and a monetary system that does not tend to produce erratic disruptions;
(iii) avoid manipulating exchange rates or the international monetary system in order to prevent effective balance of payments adjustment or to gain an unfair competitive advantage over other members; and
(iv) follow exchange policies compatible with the undertakings under this Section.

Section 3. *Surveillance over exchange arrangements*

(a) The Fund shall oversee the international monetary system in order to ensure its effective operation, and shall oversee the compliance of each member with its obligations under Section 1 of this Article.
(b) In order to fulfill its functions under (a) above, the Fund shall exercise firm surveillance over the exchange rate policies of members, and shall adopt specific principles for the guidance of all members with respect to those policies. Each member shall provide the Fund with the information necessary for such surveillance, and, when requested by the Fund, shall consult with it on the member's exchange rate policies. The principles adopted by the Fund shall be consistent with cooperative arrangements by which members maintain the value of their currencies in relation to the value of the currency or currencies of other members, as well as with other exchange arrangements of a member's choice consistent with the purposes of the Fund and Section 1 of this Article. These principles shall respect the domestic social and political policies of members, and in applying these principles the Fund shall pay due regard to the circumstances of members.[8]

1. *Ambiguities of Article IV (Sections 1 and 3)*

(a) Article IV, section 1 is the only provision of the Articles that begins with a preamble. Whether this preamble was necessary and what it was intended to achieve has not been explained and, absent any legislative history that could shed light on the reasons for its inclusion, the interpreter is reduced to conjectures.

The most probable explanation is that the drafters did not want the end of the par value system to be seen as the end of the international monetary system. There was still such a system, albeit a new one and the Fund would oversee its effective operation.[9] However, this system could not be defined in terms of obligations of members (except for the brief and obscure prohibition in Section 1(iii) against "manipulating . . . the international monetary system"[10]). It could only be described in terms of what it was supposed to achieve, i.e., to provide the "framework that facilitates the exchange of goods, services and capital among countries, and that sustains sound economic growth."[11]

8. *Id.*
9. *Id.* art. IV, § 3(a).
10. Articles of Agreement, *supra* note 1, art. IV, § 1(iii).
11. *Id.* art. VI, § 1.

Because the word "purpose" is used both in the preamble of Article IV, section 1, and in Article I (which lists the purposes of the Fund), a hasty reading of the preamble could lead to the conclusion that the purpose in that provision has been added to the purposes of the Fund. The consequence would be that the Fund would have in all its activities, and in particular in the provision of its financial assistance, to facilitate trade and capital liberalization and sustain sound economic growth. Also, the verb "to facilitate" is sometimes read as a synonym for "to achieve," which would mean that the Fund should make trade and capital liberalization a condition of its financial assistance.

This is clearly a mistaken interpretation of the preamble. The purpose of the international monetary system is not a purpose of the Fund and making trade and capital liberalization possible through monetary stability is not the same thing as liberalizing them.

(b) After the preamble and the general obligation to collaborate in assuring orderly exchange arrangements and promoting a stable system of exchange rates, Article IV, section 1 lists four specific obligations of members as corollaries of the general obligation. Two of these obligations relate to economic and financial policies or underlying economic and financial conditions of members. The other two obligations relate to exchange rates or exchange policies.

With great logic, Article IV, section 3(a) requires the Fund to oversee the compliance of each member with its obligations under Section 1. Then comes the unexpected. Article IV, section 3(b) states: "In order to fulfill its functions under (a) above, the Fund shall exercise firm surveillance over the exchange rate policies of members, and shall adopt specific policies for the guidance of all members with respect to those policies."[12] There are two possible readings of this provision, neither of which is fully satisfactory. The first one is to deem all the obligations listed in Section 1 to be exchange rate policies, which would require the Fund to exercise firm surveillance and adopt specific principles not only on the last two specific obligations in Section 1 (exchange rates and exchange policies), but also on the first two (economic and financial policies or conditions). Then, the Fund would really fulfill its functions of overseeing compliance with all the obligations in Section 1. The objection, however, is that the first two obligations in Section 1 have nothing to do with exchange rate policies and are not easily dealt with in specific principles.

The second reading of Section 3(b) focuses on the words "exchange rate policies" understood literally, i.e., to the exclusion of economic and financial policies or conditions. The objection is that, if firm surveillance and specific principles are limited to exchange rate policies strictly defined, the Fund will not be fulfilling all its functions under Section 3(a). This point was conceded by the Fund in 1977, when it approved the staff document entitled "Surveillance over Exchange Rate Policies," which adopts the second of the two meanings mentioned above. The document recognizes that exchange rate policies are only one of the two types of policies governed by Article IV, section 1. It also recognizes not only "that there is a close relationship between domestic and international economic policies,"[13] a distinction that refers to the two groups of obligations in Article IV, section 1, but also that the appraisal of a member's exchange rate policies "shall be made within the framework of a comprehensive analysis of the general economic situation and economic policy strategy of the member, and shall recognize that domestic as well as external policies

12. *Id.* art. IV, § 3(b).
13. *Id.*

can contribute to timely adjustment of the balance of payments. The appraisal shall take into account the extent to which the policies of the member, including its exchange rate policies, serve the objectives of the continuing development of the orderly underlying conditions that are necessary for financial stability, the promotion of sustained sound economic growth, and reasonable levels of employment."[14] Therefore, although the principles and procedures set forth in the document deal only with exchange rate policies understood literally (e.g., avoidance of unfair competitive depreciation or manipulation of exchange rates, market interventions to counter disorderly conditions), the Fund's appraisal takes into account both exchange rate and domestic (economic and financial) policies.

This question of interpretation seems now settled but an interesting development is taking place. While it would have been premature at the time of the second amendment for the Fund to adopt specific principles for the guidance of members in their economic and financial policies, there is now a momentum in that direction through the adoption of standards and codes of best practices.

It may be noted in passing that neither the principles for surveillance over exchange rate policies nor the standards and codes that may be used in surveillance over domestic policies constitute obligations for members. The Fund can provide guidance but the obligations of members can only be prescribed by the Articles.

(c) According to the document "Surveillance over Exchange Rate Policies" mentioned above, the international economic policies governed by Article IV, section 1 are exchange rate policies; the other policies governed by that provision are "domestic." Does it mean that surveillance does not apply to international policies in areas such as trade and investment, although both are mentioned in the preamble? The Principles set forth in the document recognize the relevance of trade and investment policies, but only as an element to assess exchange rate policies: the introduction or intensification, for balance of payments reasons, of restrictions on trade or investments may denote the existence of inadequate exchange rate policies; the same is true of incentives for capital inflows or outflows or if there are unsustainable flows of private capital.

Therefore, trade liberalization as such is not an obligation under Article IV, which is understandable since it is supposed to be achieved under the auspices of the World Trade Organization. Nevertheless, the Fund does discuss trade issues. And when these issues are discussed in a general or regional context, or if they are substantial with respect to a particular member, a representative of the WTO may attend the meeting as an observer.

Similarly, the liberalization of capital movements is not an obligation under Article IV, and Article VI, section 3 explicitly recognizes the right of members to regulate capital movements. However, the use of restrictions on capital inflows to prevent the appreciation of the local currency could be seen as an attempt to manipulate exchange rates in order to gain a competitive advantage.

(d) Perhaps the most difficult, and as yet unresolved, question of interpretation of Article IV is whether the obligation to cooperate includes an obligation to sacrifice a country's self interest to those of others. With respect to exchange rate policies, Article IV, section 1 provides an answer to this question: a member may not manipulate its exchange rates to gain an unfair competitive advantage over other members. In practice, this intention may be difficult to prove, but at least the prohibition is expressly formulated.

14. *Id.*

In other cases, absent an equally explicit prohibition, the principle should be that countries are free to compete with each other. The clearest example would be competition to attract foreign investments through tax incentives. In the trade area, the rules of the GATT or GATS may prevent the granting of subsidies or other means of unfair competition, but these prohibitions are outside the scope of the Fund's Articles.

Issues of deliberate international competition do not arise very often within the Fund. For example, a country passes legislation that appears to give sanctuary to foreign criminals if they deposit a large amount of money in the country's banks; the Fund postpones the conclusion of the Article IV consultation until the country gives the necessary appeasements. Some countries, in order to encourage exports, accept the tax deductibility of bribes paid by their residents to foreign public officials in connection with the negotiation of procurement contracts; an OECD Convention prohibiting such practices (1997 Convention on Combating Bribery of Foreign Public Officials in International Business Transactions) is adopted and, in the Fund, the staff will "recommend that such practices be stopped."[15] It may be noted that a recommendation by the staff does not imply the existence of an obligation under the Articles.

In other cases, the competitive advantage may be simply the result of domestic policy choices. Nevertheless, a country's refusal to align itself with the laws and practices of other countries may be seen by those countries as a failure to cooperate against what they regard as criminal activities that are harmful to their economic or financial interests. The issue, therefore, is whether Article IV imposes an obligation to cooperate for the success of other countries' policies. For example, is there an obligation for a Fund member to amend its banking secrecy laws and to inform other countries about banking or other transactions that violate the tax laws, exchange controls, or criminal laws (money laundering, financing of terrorism, or other illegal activities) of those countries and to take action against such practices? The recognition of such an obligation would have far-reaching consequences, as it would indirectly lead to an enforcement of foreign public laws, which normally requires explicit treaty or statutory provisions. For instance, it is an established principle that countries do not collect the taxes of other countries. Nor do they enforce foreign criminal laws in their courts; at most, the accused will be either tried under the local law if that law so provides or extradited in accordance with the local law or international treaties. Similarly, the refusal of courts in some countries to accept a broad interpretation of Article VIII, section 2(b), as mentioned above, illustrates this reluctance to give effect to foreign public laws, even when this effect is limited to civil remedies between private parties.

The traditional objections to the application of foreign public laws are that (1) there may be, and often is, a conflict of interest between the foreign state enacting the law and the local state (e.g., collecting taxes for the foreign state reduces the tax base for the local state) and (2) foreign laws may be repugnant to the ethical principles of the local state (e.g., persecution of religious or racial minorities or of political opponents through criminal laws, confiscatory tax laws, discriminatory exchange controls, etc.).

To overcome these obstacles, various means of achieving international cooperation against international financial crime have been developed. The most common is the ne-

15. Guidance Note of July 2, 1997 on the Role of the Fund in Governance Issues, *in Selected Decisions and Selected Documents of the International Monetary Fund*, Twenty-Fifth Issue, Washington, DC, Dec. 31, 2000 [hereinafter *Selected Decisions*], at 31, 37.

gotiation of international treaties, on a bilateral or multilateral basis (e.g., the OECD Convention mentioned above on bribery of foreign public officials and the 1999 U.N. Convention for the Suppression of the Financing of Terrorism). Exceptionally, in the exercise of its peace-keeping powers, the U.N. Security Council may require the imposition of financial sanctions against countries or individuals (e.g., Resolution 1373 (28 September 2001) of the Security Council requiring all States to "[c]riminalize the wilful provision or collection, by any means, directly or indirectly, of funds by their nationals or in their territories with the intention that the funds should be used, or in the knowledge that they are to be used, in order to carry out terrorist acts"[16]).

In recent years, a soft law approach to international cooperation against international financial crime has been used. In various organizations (e.g., the OECD) or working groups (e.g., the Financial Action Task Force (FATF) and the Financial Stability Forum (FSF), both created at the initiative of the G-7), principles are developed, which are presented as recommendations not only for the members of the organization or of the working group but also for other countries. For example, recommendations have been made by the FSF on offshore financial centers and by the FATF on money laundering. Offshore financial centers are subjected to particular scrutiny as their legislation or their administrative framework does not always adequately prevent or detect financial transactions that are linked to international financial crime. Money laundering is criminalized and prosecuted as a means of preventing criminals from enjoying the fruit of their crimes by making them appear legitimate; those crimes (called "predicate offenses") may have been committed within the country where the laundering takes place or abroad. In some countries, money laundering applies not only to illegal earnings but also to illegal savings (tax evasion).

In order to make these recommendations more effective, various types of pressure may be envisaged. Thus, jurisdictions (countries or dependencies) that refuse to cooperate and comply with the recommendations of the FATF are publicly blacklisted ("name and shame") by the FATF and economic "countermeasures" may be imposed against them. When the noncooperative jurisdiction is a dependency, the blacklisting and the countermeasures apply only to that territory. This is in contrast to the Fund's surveillance where each member is responsible for the actions of its dependent territories.

In order to further strengthen the effectiveness of these recommendations, the Fund may be asked by the countries supporting the recommendations to propagate them through its various activities. In the case of offshore financial centers and money laundering, the Fund has agreed to provide technical assistance to countries that wish to have their legislation and administrative arrangements reviewed and, if necessary, adjusted. This assistance is provided by Fund staff under the Fund's Financial Sector Assessment Program.

It has also been suggested that the Fund should give even greater effect to the recommendations of the FATF on money laundering by including these recommendations in the scope of its surveillance under Article IV and refusing to provide financial assistance to members that do not comply with the recommendations.

These issues were discussed by the Fund's Executive Board in April 2001. According to the summing up by the Acting Chairman (April 17, 2001), it was "agreed that the Fund has an important role to play in protecting the integrity of the international financial system, including through efforts to combat money laundering."[17] The term "integrity" is worth

16. S.C. Res. 1373, U.N. SCOR, 56th Sess., 4385th mtg., U.N. Doc. S/RES/1373 (2001).

17. Available at http://www.imf.org/external/np/sec/pn/2001/pn0141.htm.

noting as it has two possible meanings. It may refer to the moral integrity of the financial system (i.e., avoiding its use for the benefit of criminals, which would include not only the laundering of money illegally acquired or saved (tax evasion) but also the financing with legally acquired money of criminal activities, such as terrorism). Alternatively, it may refer to its financial integrity (i.e., avoiding its use for transactions that may have a destabilizing effect on the system itself). Also worth noting is the absence of a definition of money laundering, probably because there are different definitions in different countries. (N.B. The same is true for the definition of terrorism.)

With respect to activities other than technical assistance, it was "generally agreed that the Fund should . . . include anti-money laundering concerns in its surveillance and other operational activities when macroeconomic relevant."[18] However, with respect to the adoption of anti-money laundering measures for the benefit of other countries, there was no consensus: "A number of Directors considered that the cross-border implications of money laundering should be raised during Article IV consultations, even if it is not macroeconomic relevant for the member but when it had significant externalities for other countries."[19] On the extent of the Fund's contribution to money laundering, it was "confirmed that it would not be appropriate for the Fund to become involved in law enforcement activities."[20]

The approach taken by the Fund in this decision is that money laundering by itself has negative economic effects. Another approach would be to recognize the even more harmful economic effects of large-scale crime, and particularly organized crime, and that the proceeds of those activities can be used not only to expand their scope but also to corrupt a country's governance structures, thus undermining its capacity to implement sound economic and financial policies.

Perhaps the most interesting aspect of this discussion is that conclusions are reached on the scope of surveillance without referring to the provisions of Article IV. In the Acting Chairman's summing up, the word obligation does not even appear at all. This avoidance of legal terminology in a discussion on surveillance reflects the ambiguity of its legal nature, not in the Articles of Agreement, but in the practice of the Fund.

### 2. *The Legal Nature of Surveillance*

There is sometimes confusion between soft obligations and soft law. A soft obligation is an obligation that does not require the achievement of a particular objective or even the exercise of best efforts or due diligence, but only a reasonable effort in light of all relevant circumstances. In contrast, soft law means that there is no obligation at all.

Article IV, section 1 offers a good example of different types of obligations. The first two specific obligations (economic and financial policies or conditions) are undeniably soft: a member must "endeavor to direct its economic and financial policies toward the objective of fostering orderly economic growth with reasonable price stability, with due regard to its circumstances;"[21] it must also "seek to promote stability by fostering orderly underlying economic and financial conditions and a monetary system that does not produce erratic disruptions."[22] The other two obligations (exchange rates and exchange policies) are hard

18. *Id.*
19. *Id.*
20. *Id.*
21. Articles of Agreement, *supra* note 1, art. IV, § 1(i).
22. *Id.* art. IV, § 1(ii).

obligations: a member must "avoid manipulating exchange rates or the international monetary system in order to prevent effective balance of payments adjustment or to gain an unfair competitive advantage over other members;"[23] it must also "follow exchange policies compatible with the undertakings under this Section."[24] The last obligation is formulated in terms that give great latitude to the Fund, which does not change the nature of the obligation but makes its scope rather uncertain.

Where there is an obligation, there can be a sanction. The sanctions listed in Article XXVI could apply to a member that fails to meet any of its obligations under Article IV. Even if no sanction is applied, the Managing Director is required to report to the Executive Board any case in which it appears to him that a member is not fulfilling its obligations under the Articles.[25]

In fact, there has not been a single instance in which sanctions have been applied or a report has been made for breach of obligation under Article IV.

This de facto transformation of Article IV, section 1 into a soft law provision is reflected in the description of Article IV consultations with members as "policy advice" provided by the Fund to each member or "policy dialogue" between each member and the Fund. More and more, surveillance and technical assistance are seen as two closely related activities, even though surveillance is mandatory for the Fund and its members while technical assistance is optional for both. For instance, it has been suggested that compliance with some standards should be an optional element of the surveillance process at the discretion of each member. This mixture of technical assistance and surveillance would have the advantage of securing gradual acceptance of standards by all members, but would also blur the distinction between the two activities.

In some cases, Article IV consultations offer an opportunity to exercise peer pressure without asserting the existence of an obligation under Article IV. This is particularly true when the policies of a member are seen as harmful to the interests of others. The staff may then be instructed, on the occasion of its Article IV consultation discussions with the member's authorities, to raise those issues and elicit the authorities' intentions; the staff's findings are then reported to the Executive Board and discussed by the Executive Directors.

An even more interesting development is the reversal that is taking place between the two types of obligations under Article IV, section 1. The hard obligations on exchange rate policies were initially expected to take center stage in consultations with members while obligations relating to domestic policies were seen as less central to the process. In practice, the opposite has happened. Consultations focus on domestic (monetary, fiscal, structural) and usually trade policies, with only a broad appraisal by the Fund of exchange rate policies as such. In contrast, the exchange rate relationships among the currencies of G-7 countries are discussed regularly and sometimes extensively within that group.

One particular reason for this evolution is that, as the Fund becomes a larger institution, the confidentiality of discussions on exchange rate policies, which are by definition sensitive, can no longer be assured. Moreover, the demands for greater transparency from the Fund tend to relegate candid discussions on such topics to other more limited fora.

23. *Id.* art. IV, § 1(iii).

24. *Id.* art. IV, § 1(iv).

25. By-Laws, Rules and Regulations of the International Monetary Fund, Fifty-Eighth Issue, May 2001, Rule K-1, *available at* http://www.imf.org/external/pubs/ft/bl/blcon.htm.

With this change in focus, consultations on domestic policies tend to expand and cover more and more ground. For instance, the principles adopted by the Fund for the guidance of its members must respect their political and social policies,[26] but labor policies have an impact on economic performance and the 1977 document "Surveillance Over Exchange Rate Policies" (quoted above) mentions "reasonable levels of employment" as relevant to the Fund's surveillance. In practice, labor policies are now included in Article IV discussions. Another example is the emphasis on good governance in domestic policies, with particular attention being given to corruption. More recently, the scope of Fund surveillance has been extended to money laundering, at least when it is "macroeconomic relevant."

As the nature of surveillance is perceived less as compliance with obligations than the exercise of peer pressure, the perception of surveillance as an element of Fund jurisdiction tends to fade. If surveillance is not related to obligations under the Articles, why not expand it to cover standards developed outside the Fund (e.g., by other intergovernmental organizations, such as the OECD, or working groups of national officials, such as the Financial Action Task Force and the Financial Stability Forum, or private associations)? A lot of good work is being done outside the Fund and the Fund would simply have to assess each member's observance of those standards. Similarly, why should surveillance be a privilege of the Fund? Why not involve the World Bank and its vast staff and expertise in the consultation process?

The difficulty with this approach is that it is no longer surveillance. Members have an obligation under the Fund's Articles to cooperate with the Fund, to provide information to the Fund, and to perform the other obligations specified in the Fund's Articles. This does not include an obligation to cooperate with other organizations or private associations, to provide them with information, or to comply with standards set by them. All this can only be done on a voluntary basis (perhaps reluctantly and under the threat of being blacklisted or subjected to retaliatory measures by other countries) and failure to comply cannot give rise to sanctions under the Articles. However, as Article IV is seen as soft law, the difference with other forms of peer pressure is less and less perceptible and this penumbra facilitates both an expansion and a dilution of Fund surveillance.

In order to bridge the gap between technical assistance and surveillance while maintaining the distinction, a new instrument has been developed by the Fund. The Reports on Observance of Standards and Codes (ROSC) are prepared by Fund and World Bank staff at the request of a member to assess its compliance with standards and codes. The results are reflected in the Article IV consultation report concerning the member.

## II. Financial Aspects

Since the second amendment of the Fund's Articles (1978), a major distinction—not always fully understood—has been made between two types of financing by the Fund.

(a) The general resources (held in the General Resources Account (GRA)) of the Fund are available to assist all members, on a uniform basis, under policies adopted by the Fund, to help them resolve their balance of payments problems in accordance with the provisions, and in particular the purposes, of the Fund. There are different policies for different types of balance of payments problems, but no other distinction among members (e.g., between developing and developed countries) is permitted.

26. Articles of Agreement, *supra* note 1, art. IV, § 3(b).

This financial assistance takes the form of bilateral exchange transactions between the Fund, which provides foreign exchange or special drawing rights, and a member, which provides an equivalent amount of its currency. This sale of foreign exchange must be reversed by the member within a specified period, which may vary depending on the policy under which the assistance was granted (e.g., three to five years). The member pays a transaction charge at the time of the transaction and a periodic charge until the transaction is reversed.

A recent review of the Fund's policies on the use of its general resources has reduced the number of policies, adjusted their respective costs for users of Fund resources, and generalized the system of repurchase expectations, which tends to accelerate the reversal of transactions without making it mandatory. Long-term financing by the Fund had been criticized by some governments as making the Fund less a monetary than a development agency. A shortening of repurchase obligations would have required an 85 percent majority of the total voting power, which could not be obtained. The adoption of a repurchase expectation, by a majority of the votes cast, was the final compromise.

(b) Before the second amendment, the Fund had been receiving gold from most Fund members in payment of their quota subscriptions. This gold, which was the property of the Fund, had been received and accounted for at the official price (SDR 35 per ounce), but market prices were much higher. Therefore, it was agreed that except for an amount of gold to be sold to members at the official price, the Fund would be allowed to sell gold at market prices and could decide to use the profits to assist developing countries. Accordingly, profits on sales of gold that was held by the Fund at the time of the second amendment may be transferred to the Special Disbursement Account (SDA) and used to provide balance of payments assistance consistent with the purposes of the Fund to developing countries, taking into account their per capita incomes. One difference between general and SDA resources is that the concept of balance of payments problem is broader in the context of the SDA because it takes into account the external deficit that may be created by the recipient country's development strategy. Another difference is that the Special Disbursement Account does not engage in reversible exchange transactions but may extend either loans or grants. These resources, combined with voluntary contributions made by a number of Fund members, are now being used in the context of two facilities for developing countries: the Poverty Reduction and Growth Facility, which extends long-term concessional loans, and the Heavily Indebted Poor Countries Initiative, which provides grants to help recipient countries discharge all or part of their indebtedness to the Fund.

Although the technique, the cost and the beneficiaries of the two types of assistance differ, both types of assistance must be consistent with the Fund's purposes, which implies that the assistance is of a monetary rather than developmental nature. Also, both types of assistance are subject to conditions, though the nature and scope of Fund conditionality may vary because the problems to be addressed are not necessarily the same.

## A. The Purposes of the Fund's Financial Assistance

### 1. *Existence of a Balance of Payments Problem*

The purposes of the Fund's financial assistance are derived from the purposes of the Fund, as set forth in Article I. The most direct connection is found in the fifth purpose, which is "[to] give confidence to members by making the general resources of the Fund temporarily available to them under adequate safeguards, thus providing them with op-

portunity to cover maladjustments in their balance of payments, without resorting to measures destructive of national or international prosperity."[27] (N.B. the references to "general resources" and "adequate safeguards" mean that the general resources may not be used in grants; this limitation does not apply to resources in the Special Disbursement Account.)

To give effect to this purpose, Article V, section 3(a) requires the Fund to adopt policies on the use of its general resources for balance of payments problems: "The Fund shall adopt policies on the use of its general resources, including policies on stand-by or similar arrangements, and may adopt special policies for special balance of payments problems, that will assist members to solve their balance of payments problems in a manner consistent with the provisions of this Agreement and that will establish adequate safeguards for the temporary use of the general resources of the Fund."[28]

A balance of payments problem may have different causes but will manifest itself through a balance of payments deficit and/or low reserves (foreign exchange, gold, special drawing rights, reserve position in the Fund). The Fund's assistance will be used to finance the deficit and/or strengthen the country's reserves.

Therefore, when requesting a purchase, a member must represent "that it has a need to make the purchase because of its balance of payments or its reserve position or developments in its reserves."[29] This means that a balance of payments deficit may not be the cause of the member's need for assistance; low reserves could also justify a request, but it is still the sign of a weak external position, and it is included in the broad concept of "balance of payments problem."

From these provisions it is clear that Fund resources cannot be used for purposes other than corrections in members' balances of payments; they cannot be used to finance a budget deficit or development projects. An interpretation of the Articles adopted by the Fund in the first year of its existence was very explicit on this point: "authority to use the resources of the Fund is limited to use in accordance with its purposes to give temporary assistance in financing balance of payments deficit on current account for monetary stabilization."[30] A few years later it was clarified that this interpretation did not preclude the use of the Fund's resources for capital transfers to the limited extent provided in Article VI, but the principle remained that Fund resources were available only for balance of payments assistance. Similarly, when the second amendment recognized that financing by the Fund would be available not only for a balance of payments deficit but also to strengthen reserves, this was still regarded as balance of payments assistance because reserves are needed to meet a potential external deficit.

### 2. *Growth as a Purpose of Fund Assistance*

Since corrections in a country's balance of payments will allow the resumption of growth-oriented policies, it is sometimes said that growth is one of the purposes of the Fund's financial assistance. This would mean that the Fund should make growth a condition of its assistance and provide the necessary financing. The justifications for asserting that growth is one of the Fund's purposes are usually not offered, probably because growth is seen as

27. *Id.* art. I(v).

28. *Id.* art. V, § 3(a).

29. *Id.* art. V, § 3(b)(ii) (N.B. The third concept, "developments in reserves," does not correspond to a balance of payments problem but to an inadequacy in the composition of reserves.).

30. Decision No. 71-2, Sept. 26, 1946, *in Selected Decisions*, *supra* note 15, at 128.

such a desirable objective that it need not be made explicit in a legal provision. Sometimes, a justification is provided by pointing out that growth is mentioned both in Article I(ii) and in Article IV, section 1. Neither of these references, however, is relevant.

The growth mentioned in Article I(ii) is the growth of international trade, not the domestic economic growth of recipients of Fund resources. The whole sentence reads as follows: "To facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income and to the development of the productive resources of all members as primary objectives of economic policy."[31] The expression "to contribute thereby" shows that high levels of employment, real income, etc. are a mediate effect of the achievement of the Fund's second purpose, which is "to facilitate" trade expansion, but it is not part of the purposes of the Fund.

The term "growth" appears twice in Article IV, section 1, but this provision deals with surveillance, not with the Fund's financial assistance. Moreover, growth is not mentioned in the preamble of section 1 as a purpose of the Fund itself. Nor is there a direct relationship between growth and the international monetary system. The "essential purpose" of the international monetary system is only to provide a "framework" that sustains economic growth.

In section 1(i), growth is mentioned again, but only in the definition of members' obligations and with a number of qualifications, and in any case not as a purpose of the Fund. What Article I(ii) and Article IV, section 1(i) have in common is that "the development of the productive resources" and "orderly economic growth" are really the objectives of the members' own policies.[32] Under Article I(ii), it is for the members to decide whether and how they want their economies to grow and in Article IV, section 1(i) it is for the members to pursue "the objective of fostering orderly economic growth with reasonable price stability."[33]

Although legally incorrect, the reference to growth as a purpose of the Fund's financial assistance is understandable for political reasons. Correcting maladjustments is not glamorous and is often associated with austerity and unemployment. Growth as a final objective of adjustment policies has greater appeal and may signal the desire to resume growth as soon as possible. The legal and the political uses of the term are not completely incompatible. A railroad engineer would say that the purpose of a railroad line is to transport passengers and goods from one place to another. A minister may prefer to say that the purpose is to create jobs and develop the country's economy. The word purpose has different meanings in different contexts.

3. *The Fund as Lender of Last Resort*

In recent discussions on the financial role of the Fund, various suggestions were made to make the Fund less a primary lender to countries than a lender of last resort.

In a national system, the lender of last resort is the central bank. Its function is to provide liquidity to primary lenders (commercial banks) but not to rescue them when they are insolvent, unless there is a systemic risk (failure of the banking system).

One suggestion was to limit each member's access to Fund resources to a low level in terms of quota and to create a special facility, with no specified access limit, for cases of systemic crises. A systemic crisis is not defined by its impact on the country requesting

31. Articles of Agreement, *supra* note 1, art. I(ii).
32. *Id.* arts. I(ii) and IV, § 1(i).
33. *Id.* art. IV, § 1(i).

financial assistance but by its impact on other countries. Therefore, a country creating a systemic risk would receive more financing to stem the risk of contagion to other countries. This raises a legal issue. Since access to Fund resources is determined by a country's own balance of payments problem, the impact of a crisis on other countries is not a relevant consideration for assessing the member's need for assistance. As systemic crises would only originate in major countries, other countries facing a problem of the same magnitude (in terms of their quotas) would not qualify for the same level of assistance. This would be contrary to the principle of uniform treatment. The proposal was not pursued.

Another proposal was that countries that have access to capital markets should not have access to Fund resources. The argument was that, since they can finance their own external deficit, they have no balance of payments problem. Two objections were made to this proposal. The first one was that it was based on a misunderstanding of what constitutes a balance of payments problem. Under the Fund's definition, external borrowing, by a government or a central bank, to finance external payments or increase reserves does not eliminate but usually confirms the existence of a balance of payments problem. Such a problem exists whenever official action is needed to acquire foreign exchange. The second objection was that access to capital markets would not necessarily allow the recipient country to resolve its balance of payments problem in a manner consistent with the purposes of the Fund: the amount, cost, and duration of the loans might not allow the country to avoid imposing exchange or trade restrictions or other harmful measures, which Fund financing would enable it not to take. This proposal also was abandoned.

4. *The Moral Hazard Issue*

One of the concerns about the bailout of commercial banks by central banks is the risk of moral hazard; a bailout may create an incentive for lax management by other banks. More generally, any systematic use of public money to rescue private debtors creates a moral hazard for other debtors and their creditors as imprudent lending becomes risk-free.

The same argument has been used in the Fund, probably because of the analogy with national lenders of last resort. However, the Fund is not a central bank. Its function is to help countries facing a balance of payments problem. The moral hazard argument, if carried to its full logic, would put the Fund in the situation of a hospital turning down incoming patients, including those with contagious diseases, to encourage recourse to preventive medicine. Not only would the Fund fail in its duty to assist members in difficulties, but also this failure would adversely affect other countries, as the ailing member would probably resort to measures "destructive of national or international prosperity."[34] At least between the Fund and the debtor country, the moral hazard argument has no place.

Between the Fund and the country's creditors the moral hazard argument is relevant. The problem, however, is that limiting access to Fund resources in order to avoid bailing out irresponsible lenders would first hurt the country itself.

5. *Safeguard of Fund Resources*

There is no doubt that the Fund's resources are limited and must be safeguarded. Nor is there any doubt that the Fund is not allowed to use its resources to finance large or sustained outflows of capital. Therefore, a degree of participation of public and private creditors in the

34. *Id.* art. I(v).

financing of Fund-supported programs is necessary. The contribution of official creditors through rescheduling and refinancing of their claims takes place under the auspices of the Paris Club. There is a similar process for commercial creditor banks in the London Club. There is no equivalent process, except on a case-by-case basis, for bondholders.

Initially, the Fund's policy was not to "lend into arrears": no financing was made available until the debtor country had reached agreement with its public and private creditors. The present practice is for the Fund to provide financing even before an agreement is reached with private creditors if prompt Fund support is considered essential for the successful implementation of the member's adjustment program and the member is making a good faith effort toward a collaborative agreement with the creditors. During the interim period, a participation of the private sector in the financing of the program—through rollovers or reductions in the service of the debt—may be necessary for the program to succeed. In contrast with other (public or private) creditors, the Fund is regarded as a preferred creditor, whose claims are not subject to rescheduling. This special status finds its origin in the practice of the Paris Club not to include the Fund and the World Bank in their negotiations with debtor countries, thus allowing them to stay out of the rescheduling process.

### B. Fund Conditionality

The expression Fund conditionality is more often used than defined. In one sense, Fund conditionality began with the Fund itself because the original Articles of Agreement set forth a number of conditions for access to Fund resources. However, what may be regarded as the beginning of conditionality by the Fund as the term is now understood was the decision of 1948 recognizing the power of the Fund to add conditions to those set forth in the Articles. Since then, the techniques of Fund conditionality have evolved considerably, with a constant tension between the need for users of Fund resources to know their rights with reasonable certainty and the desire of the Fund's organs to retain as much discretion as possible; this evolution may even be described as a pendulum oscillating between certainty and discretion. Another aspect of Fund conditionality has been the gradual expansion of its scope from macroeconomic to structural adjustment.

#### 1. *The Origin of Conditionality*

Under the original Articles of Agreement, a member was entitled to use the Fund's resources if it met the conditions specified in the Articles.[35] If these conditions were not met, the member had no entitlement, but the Fund could waive the conditions prescribed by the Articles.

One of the conditions under the former Article V, section 3 was that the member "represent" that the currency it wanted to purchase was "presently needed for making in that currency payments which are consistent with the provisions of this Agreement."[36] Since the rate of charge paid to the Fund was rather low, there was a risk that some members would purchase currencies from the Fund and invest them for profit. Moreover, after a few years it became clear that most requests were for purchases of U.S. dollars, which created a different risk, namely, that the Fund, acting under Article VII, section 3, would declare the

35. Former art. V, § 3(a).
36. *Id.* art. V, § 3.

U.S. dollar a scarce currency, which would have allowed other members to restrict exchange operations in U.S. dollars in their territories.

On March 10, 1948, the Fund adopted an interpretation of Article V, section 3(a), which clarified and substantially limited the right of members to purchase currencies from the Fund. It was decided that the word "represents" means "declares." In the same decision, however, the Fund took the view that it had the power, for good reason, to challenge the correctness of a member's declaration, for instance, because in the judgment of the Fund the currency was not "presently needed" or not needed for payment "in that currency" or the payment was not "consistent with the provisions of this Agreement."[37] In such cases, the member's request could be postponed, rejected or made subject to conditions. This was the first assertion of the Fund's power to add conditions to those set forth in the Articles.

This interpretation created great uncertainty. Members were reluctant to request purchases without the assurance that the request would be met. A new instrument was therefore invented to combine conditionality and certainty. In 1953, a policy of the Fund on stand-by arrangements provided that "a member having a stand-by arrangement will have the right to engage in transactions without further review by the Fund."[38] This meant that requests for purchases would be met to the extent and subject to the conditions specified in the stand-by arrangement.

The stand-by arrangement is a creation of the Fund's practice. Later, other types of arrangements have been developed for special policies (extended arrangements and PRGF arrangements) but they are based on the same model.

The invention of the stand-by arrangement was designed to give greater confidence to members, not to preclude the possibility of requests for purchases outside an arrangement ("outright purchases"). Gradually, however, arrangements have tended to become the preferred instrument for access to Fund resources. Under the credit tranche policies, both outright purchases and stand-by arrangements can be used, but in practice access beyond the first credit tranche is under an arrangement. In the Extended Fund Facility, the Supplemental Reserve Facility and the Contingent Credit Lines, assistance is provided under a stand-by arrangement or (except for the CCL) an extended arrangement. In the Compensatory Financing Facility, outright purchases are used, but higher access is possible if there is a parallel stand-by or extended arrangement. In the Emergency Assistance Facility, outright purchases are used. In the Poverty Reduction and Growth Facility, loans are extended under arrangements.

The existence of stand-by and similar arrangements and their role in Fund conditionality are now explicitly acknowledged in the new Article V, section 3(a), as modified by the second amendment. The concept of stand-by arrangement is now defined in Article XXX(b): "Stand-by arrangement means a decision of the Fund by which a member is assured that it will be able to make purchases from the General Resources Account in accordance with the terms of the decision during a specified period and up to a specified amount." In addition, the 1979 Guidelines on Fund conditionality clarify the legal nature of stand-by arrangements: they "are not international agreements and therefore language having a contractual connotation will be avoided in stand-by arrangements and letters of intent."[39]

37. Decision No. 284-4, Mar. 10, 1948, *in Selected Decisions*, *supra* note 15, at 129.

38. Decision No. 270-(53/95), Dec. 23, 1953, para. 4, *in Selected Decisions*, *supra* note 15, at 146, 147.

39. Decision No. 6056-(79/38), Mar. 2, 1979, para. 3, *in Selected Decisions*, *supra* note 15, at 149.

Extended arrangements are not defined in the Articles but they are regarded as "similar" to stand-by arrangements for purposes of Article V, section 3(a). There are certain differences between the two instruments because they are used under different policies, but the source and nature of the commitment are the same as for stand-by arrangements. Therefore, the same definition applies to them and their legal nature is identical.

The same can be said of arrangements under the Poverty Reduction and Growth Facility (formerly the Enhanced Structural Adjustment Facility, which itself followed the Structured Adjustment Facility). The only difference is that financing under a stand-by or extended arrangement takes the form of a sale of currency because this is the technique in the General Resources Account, while financing under a PRGF (or ESAF or SAF) arrangement takes the form of loans because this is the technique in administered accounts (or in the Special Disbursement Account).

Because of this difference, some have argued that SAF/ESAF (or now PRGF) arrangements are of a contractual nature. The implicit reason seems to be that a stand-by arrangement is a unilateral decision of the Fund because it is a commitment to sell currency, while a PRGF arrangement is a contract because it is a commitment to lend currency. This analysis has no merit. If a commitment to sell may be unilateral, the same is true of a commitment to lend. In any case, the commitment itself is neither a sale nor a loan.

2. *Techniques of Conditionality*

Broadly understood, Fund conditionality consists of three layers of conditions.

(a) The first layer is found in the Articles of Agreement and the policies adopted by the Fund under the Articles. In the GRA, Article V, section 3(a) requires the adoption of general policies applicable to all types of balance of payments problems (the credit tranche policies) and authorizes the adoption of special policies for special balances of payments problems (e.g., the Extended Fund Facility). These special policies may specify not only different conditions but also different levels of access, maturities and charges. Both general and special policies must "assist members to solve their balance of payments problems in a manner consistent with the provisions of this Agreement and . . . will establish adequate safeguards for the temporary use of the general resources of the Fund."[40]

(b) The second layer is found in stand-by and other arrangements. Each arrangement is a self-contained document. All the conditions, but only the conditions specified in the arrangement, apply to the assistance provided under that arrangement. There are essentially two types of conditions: performance criteria and reviews.

Performance criteria are specified in the arrangement when approved or reviewed by the Executive Board. They are objectively defined and their implementation is monitored by the staff. If the relevant criteria are met and no review is required for a particular purchase, the purchase may be made without having to request Executive Board approval; the request for the purchase could not even be denied on the grounds that the member has no balance of payments need and that its representation of need (required for the purchase) is demonstrably false. The Fund could only take action after the fact by requesting a reversal of the transaction.[41] If a performance criterion is not met, the purchase may not be made unless the Executive Board grants a waiver of applicability or for nonobservance of the performance criterion. Sometimes, however, a performance criterion appears to have been met

40. Articles of Agreement, *supra* note 1, art. V, § 3(a).
41. *Id.* art. V, § 5.

but the information provided by the member turns out to be incorrect; in such cases of misreporting, the member will be called upon to reverse the transaction unless the Fund grants a waiver.

Performance criteria are conditions, not obligations. Failure to meet a performance criterion by a member is not a breach of obligation and does not give rise to sanctions under the Fund's Articles. The only exception would be when the performance criterion is nothing but the observance of an obligation under the Articles (e.g., non-imposition of restrictions on current payments). As they are specified by the Fund pursuant to the Articles and policies of the Fund, performance criteria must be consistent with the Articles and the relevant policies.

Reviews are conducted by the Executive Board. For a long period, their sole purpose was to set performance criteria for the period not covered by the performance criteria specified at an earlier date. Now, reviews are part of Fund conditionality. Non-completion of a review for performance regarded as unsatisfactory by the Executive Board suspends further access to Fund assistance under the arrangement. In some arrangements, monthly reviews are required, which substantially limits the effectiveness of the assurance the arrangement is supposed to provide to the member.

In addition to performance criteria and reviews, there may be conditions relating to the occurrence of particular events. For instance, under the Contingent Credit Lines, the Fund's commitment under the arrangement can only be activated in the event of contagion ("adverse developments in international capital markets consequent upon developments in other countries"[42]).

(c) The third layer of Fund conditionality is based on the role played by the Managing Director and the staff in conducting discussions with members requesting access to Fund resources and in making recommendations to the Executive Board for the approval of an arrangement or the completion of a review. These recommendations are based on the taking of prior actions or the meeting of benchmarks, which have been communicated to the member by the staff as conditions or relevant considerations for the Managing Director's recommendations to the Executive Board. These prior actions and benchmarks are not conditions in the same sense as performance criteria since they are not formulated by the Executive Board in the arrangement, and failure to meet them does not automatically suspend the Fund's assistance or require a waiver. They may, however, affect the member's access to Fund resources because the Managing Director's recommendations carry particular weight with the Executive Board. As they are formulated by staff and management in the performance of their duties as Fund officials, these prior actions and benchmarks must, like performance criteria, be consistent with the Articles of Agreement and the relevant policies of the Fund.

It may be noted that, in addition to the conditions specified in the arrangement and the prior actions and benchmarks specified by the staff, a member may state its intention to take other measures that will be part of the economic and financial program for which Fund support is requested. These measures are not part of Fund conditionality.

42. Decision No. 11627-(97/123) SRF, as amended on Apr. 23, 1999, para. 15, *in Selected Decisions*, *supra* note 15, at 233, 237.

3. *Scope of Conditionality*

When conditionality under stand-by arrangements was invented, the scope of Fund conditionality was limited essentially to macroeconomic policies (budget, credit, external debt, and reserves) and compliance with obligations under the Articles (avoidance of exchange restrictions). The 1979 guidelines on stand-by arrangements (in the credit tranches) still stated:

> Performance criteria will normally be confined to (i) macroeconomic variables, and (ii) those necessary to implement specific provisions of the Articles on policies adopted under them. Performance criteria may relate to other variables only in exceptional cases when they are essential for the effectiveness of the member's program because of their macroeconomic impact.[43]

In contrast, the 1974 decision on extended arrangements (under the Extended Fund Facility) emphasized the need for comprehensive programs "to correct structural imbalances in production, trade, and prices," which corresponded to a longer-term commitment of resources by the Fund to help correct structural maladjustment in production and trade.[44]

Therefore, different conditionalities for different types of balance of payments problems characterize the practice of the Fund. In fact, each special policy on the use of Fund resources requires its own type of conditionality. For instance, the Supplemental Reserve Facility and the Contingent Credit Lines, although they share some common provisions, are subject to very different types of conditionality because they correspond to different balance of payments problems.

When designing its conditionality, the Fund is guided by two main considerations. The first one is that the conditions must help the member to resolve its balance of payments problem in a manner consistent with the purposes of the Fund while safeguarding the Fund's resources. The other one is that the conditions are only those necessary to achieve those objectives. As conditions affect a member's exercise of its sovereign powers, they must be kept to the minimum necessary to achieve the objectives states by the Articles.

An example of this self-restraint may be found in the conclusions of a discussion in 1991 at the Executive Board on the treatment of military expenditure in Fund conditionality: although a number of Executive Directors deplored the unproductive nature of military expenditures, it was "agreed that data on military expenditures should not serve as the basis for establishing performance criteria or similar conditions associated with Fund-supported programs."[45]

Self-restraint is not easy to exercise in the face of a major financial crisis, particularly when other Fund members see the crisis as a unique opportunity to impose the reforms they have been advocating. In these circumstances, the member requesting Fund assistance may wonder whether the reforms demanded by the Fund are really necessary for the resolution of its own problem or rather intended to satisfy the objectives of other countries.

Self-restraint is easier to observe when another organization takes responsibility for certain aspects of a program. For instance, when the same country turns to both the Fund and the World Bank for assistance, it is possible to limit the scope of Fund conditionality to

43. Decision No. 6056-(79/38), Mar. 2, 1979, para. 9, *in Selected Decisions*, *supra* note 15, at 149, 150.

44. Decision No. 4377-(74/114), Sept. 13, 1974, Part II, para. 1, *in Selected Decisions*, *supra* note 15, at 165, 166.

45. Concluding Remarks by the Acting Chairman, Military Expenditure and the Role of the Fund, Executive Board Meeting 91/138, Oct. 2, 1991, *in Selected Decisions*, *supra* note 15, at 447, 448.

macroeconomic measures and a few structural measures, leaving the major part of the structural adjustment to the World Bank.

From a legal standpoint, the most difficult question is not whether a particular measure is necessary or not, but rather whether it may be imposed without exceeding the limits set by the Articles. In practice, the main criterion is consistency with the purposes of the Fund. Those purposes are economic and financial; they are not political, which would exclude political conditionality. These purposes include the facilitation of international trade, which would authorize trade liberalization, or at least the avoidance of trade restrictions for balance of payments reasons, as part of Fund conditionality. The Fund's purposes also include the preservation of productive resources, which would include human resources (safety nets, health, and education) and natural resources (environment). What is absent from the Fund's purposes is the liberalization of capital movements, which is explicitly excluded from the mandate of the Fund in Article VI. Therefore, this liberalization is outside of the Fund's conditionality.

The duty to exercise self-restraint in the formulation of Fund conditionality and to observe the requirements of the Articles when deciding whether or not a particular condition is within the Fund's mandate applies to the organs of the Fund. It does not apply to members of the Fund. They are free to advocate changes in Fund conditionality as a vehicle for the attainment of their own objectives. An example can be found in the U.S. legislation as incorporated in Title 22 of the U.S. Code; these provisions often direct the Secretary of the Treasury to instruct the U.S. Executive Director in the Fund to oppose Fund financing for countries that do not meet specified conditions and to promote the inclusion in Fund conditionality of certain objectives. (For a comprehensive review of the legislation and its implementation, see the report of January 2001 of the U.S. General Accounting Office to Congressional Committees on "Efforts to Advance U.S. Policies at the Fund," GAO 01–214.) Although the U.S. Executive Director is an official of the Fund who is not legally under the authority of the Secretary of the Treasury, the fact that the Secretary may terminate the U.S. Executive Director's appointment at any time is a strong incentive for complying with those instructions. Other Executive Directors also receive instructions relating to Fund conditionality, usually from the executive branch rather than the legislature of their constituents.

## III. Institutional Aspects

### A. Internal Aspects

#### 1. *Structure*

Since the creation of the Fund, its internal structure has remained remarkably stable. The Fund is an international financial institution whose members are independent states. Each member is assigned a quota, which determines its voting rights (in addition to 250 basic votes allotted to each member), the size of its contribution to the Fund, and the extent of its entitlement to use the Fund's resources. Uniformity of treatment in the Fund does not mean equal access in absolute amounts to the Fund's resources but access in proportion to quotas.

Each member appoints one Governor and the Board of Governors is the supreme organ of the Fund. The members also appoint or elect Executive Directors. The members with the five largest quotas elect one Executive Director each (United States, Japan, Germany, United Kingdom, France). The other members elect the other Executive Directors who at

present number nineteen. Given the large number of members not appointing Executive Directors (178), those members organize themselves into groups, each of which forms a constituency to elect an Executive Director. However, three members have enough votes to form single-country constituencies and elect three Executive Directors (China, Russia, Saudi Arabia). The present total number of Executive Directors is twenty-four, but the number of elected Directors is not fixed. The standard number of elected Directors under the Articles is fifteen, but it may be increased or decreased by the Board of Governors; that decision is made every two years, at the time of the election of Executive Directors and requires an 85 percent majority of the total voting power. The Executive Board exercises the powers delegated by the Board of Governors and those conferred directly by the Articles of Agreement.

The Executive Directors elect a Managing Director who is the head of the staff. Therefore, the staff is under the authority of the Managing Director, not of the Executive Board.

The Board of Governors may create committees with advisory functions. In 1974, an Interim Committee of the Board of Governors on the International Monetary System had been established; it had the same number of members as the Executive Board and was designated by the same constituencies as those that appoint or elect the Executive Directors. In 1999, the Interim Committee was replaced by the International Monetary and Financial Committee (IMFC) with the same composition as the Interim Committee but an expanded mandate. It is supposed to supervise the adaptation and management not only of the international monetary system, which is referred to in the Fund's Articles, but also of the international financial system. Although this concept does not appear in the Fund's Articles and is not defined in the resolution of the Board of Governors, its mention reflects the growing interest of Fund members in ensuring an orderly conduct of international financial relations. Financial markets are a major source of liquidity both for governments and for the private sector. Hence, the emphasis that is now given in the work of the Fund on standards and the prevention of financial abuse.

Consideration had been given to establishing the Council, a decision-making organ of limited membership whose creation is authorized by the Fund's Articles, but this proposal did not succeed. Instead, the IMFC, with advisory powers, was established.

2. *Membership*

Membership in the Fund is open to "countries." By countries the Fund understands sovereign states. In order to be a member, a country need not have its own currency.

Some countries do not issue their own currency; this does not preclude them from being members of the Fund. In that case they select another member's currency and use it as their own in transactions with the Fund. The Fund's holdings acquired as a result of such transactions are accounted for separately from those acquired in transactions with the issuer of the currency. Although a number of Fund members have joined monetary unions and share common currencies, they do not share a common membership in the Fund. Each member of a monetary union may join the Fund and is treated like any other member. For instance, the members of the West African Economic and Monetary Union are all members of the Fund. The Union is not a member of the Fund because it is not a country. The members of a monetary union remain subject to all their obligations under the Articles, including those relating to exchange rates.

This issue came up recently after the creation of the European Monetary Union (EMU) with a common single currency and a common central bank. The view was taken by some

that the Union should replace its members in the Fund. This view was not accepted by the Fund. Instead, the European Central Bank was allowed to become an observer at meetings of the Fund's Executive Board on issues within its competence.

It is, of course, possible for members of a monetary union to form a constituency and elect the same Executive Director to the Executive Board, but only if they are not among the countries that have the five largest quotas because those countries have to appoint an Executive Director. For instance, France and Germany have to appoint their own Executive Directors. Other members of EMU could form one or more EMU constituencies to elect one or more Executive Directors but so far they have chosen to remain in constituencies with non-EMU members.

It is rather superficial to believe that membership in the Fund should be based on the issuance of a separate currency. The Fund is a monetary institution but its surveillance applies to economic and financial policies, including fiscal policies, which are outside the scope of a monetary union. Fund conditionality also covers a broad range of issues, again far beyond monetary policies. Moreover, a country that does not issue its own currency or participates in a monetary union may face a balance of payments problem; its membership in a monetary union would not deprive it of its access to Fund resources.

3. *Voting Powers*

The Fund was established as a cooperative in which each member may, in case of need, receive assistance from the Fund. Therefore, all members are supposed to share a common interest in the design of Fund conditionality and other activities of the Fund. However, reality is more complex. During the first years of the Fund, it became clear that certain countries (the United States at first) were mainly providers of assistance through the Fund while others were mainly recipients of this assistance. Once countries see themselves as creditors or debtors, they tend to have a polarized view of financial assistance. As developed countries have "graduated" from Fund assistance, this assistance is seen now as benefiting mostly developing or middle-income countries. In discussions on the design of Fund facilities, "creditor countries" may argue for higher costs and shorter maturities of Fund assistance against "debtor countries," which want to preserve the status quo. The size of Fund assistance is also a controversial issue, as well as the extent of Fund conditionality, where "creditor" and "debtor" countries often take opposite views. Although this polarization is somewhat mitigated by the existence of mixed constituencies in which developed and developing countries elect the same Executive Directors, positions taken in the Executive Board tend to reflect a division between supporters of the views of developed countries versus those of developing countries.

Some developing countries have proposed a reallocation of voting powers that would strengthen their role in the Fund's decision making-process. Various factors could be considered: more basic votes for each member; additional votes based on the size of a country's population; and more votes for poorer countries (in terms of per capita income). No decision has been taken. Such changes would require an amendment of the Articles.

Another issue is the requirement in the Fund's Articles of a special majority for many decisions: 70 or 85 percent of the total voting power. Those majorities give a de facto veto to countries with large quotas; for instance, with more than 15 percent of the total voting power, the United States can veto a number of major decisions. Conversely, groups of smaller countries may unite to veto those decisions. These special majorities explain the need in many cases for reaching a consensus on a compromise between conflicting views.

4. *Transparency and Accountability*

(a) There have been complaints about the lack of transparency of the Fund's activities, particularly in the context of its financial assistance and surveillance. Decisions of the Fund either of a general or of a country-specific nature may be published and the Fund has adopted policies to expand the scope of such publications. In addition, the Executive Board often authorizes the publication of papers prepared by the staff for consideration by the Board. A decision of January 4, 2001, has codified the Fund's publication policies. For country-specific documents, the consent of the member is required.

The Fund's latitude in adopting publication policies is limited by three considerations. The first one is of a legal nature. A member's letter of intent requesting financial assistance and describing its program is a document of the member and can only be published by the member or with its consent. The same is true of any documents or information communicated to the Fund on a confidential basis. Therefore, the Fund can only encourage but cannot require the publication of those documents or data. The trend is toward more transparency in that respect. The second consideration is also of a legal nature. Under Article XII, section 8, the Fund's (i.e., the Executive Board's) assessment of a member's situation and policies—particularly in the context of surveillance—may be communicated informally to the member but may not be published by the Fund without the consent of the member. (N.B. This condition would not apply if the Fund found that the member's policies tended "to produce a serious disequilibrium in the balance of payments of members" but such a finding has never been made.) More and more this consent is granted by the member concerned. The third consideration is of a policy nature. A report by Fund staff on a member's situation and policies, though not expressing the official views of the organization, may be mistakenly seen as an informal expression of such views. Therefore, the Fund will not publish the report without the consent of the member.

(b) The Fund is accountable to its members and the Executive Board is accountable to the Board of Governors. However, accountability of the Fund to the public is not required by the Articles. Some organizations have created a system of independent evaluation whose results are made public. The World Bank has created an Inspection Panel. In the Fund, it has now been decided to establish an Independent Evaluation Office. Its director has been appointed by the Executive Board. The Evaluation Office will conduct assessments of the Fund's activities. These assessments can be made public.

### B. Relations with Other Organizations

1. *Principles*

The Fund is required by its Articles to cooperate within the terms of its Articles with any general international organization (i.e., the United Nations) and with public international organizations having specialized responsibilities in related fields.[46] This requirement is qualified: the Fund can only cooperate within its mandate; it may not undertake to perform functions not authorized by its Articles, unless the necessary amendments of the Articles are first adopted by its membership. Demands on the Fund to give effect to recommendations of other organizations can only be met if the actions to be taken are consistent with the Articles.

46. Articles of Agreement, *supra* note 1, art. X.

The condition of consistency with the Articles is essential. The Fund has not been established and endowed with resources to become an agent of other organizations. It is incumbent upon the organs of the Fund to make sure, regardless of the pressures exercised by governments, that this condition is observed. The fact that there is often support for using the Fund as an enforcer of other treaties, does not make those treaties part of the Fund's Articles.

For instance, it is sometimes stated that the Fund is bound by the provisions of the Covenant on Economic, Social and Cultural Rights adopted in 1966 under the auspices of the United Nations and entered into force in 1976. There is no doubt that, in the exercise of its mandate, considerations that led to the adoption of the Covenant should also guide the Fund. Specifically, the reference in Article I(v) to the Fund's financial assistance being made available to provide its members "with opportunity to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity"[47] means that the economic and social welfare of its members must be a key consideration in the Fund's decision. However, this does not mean that only the welfare of the recipient country should be considered. Otherwise, international prosperity could suffer. Nor does it mean that the Fund can ignore the various limitations imposed by its Articles of Agreement. For example, the Fund can only provide financial assistance for balance of payments problems. On the more fundamental issue, which is whether the Fund is legally bound by the provisions of the Covenant on Economic, Social and Cultural Rights, the answer is that the Covenant does not apply to the Fund for three reasons. First, the Fund is not a party to the Covenant. Second, the obligations imposed by the Covenant apply only to states, not to international organizations. Third, the Covenant itself explicitly recognizes, in its Article 24, that "[n]othing in the present Covenant shall be interpreted as impairing the provisions . . . of the constitutions of the specialized agencies which define the respective responsibilities . . . of the specialized agencies in regard to the matters dealt with in the present Covenant."[48]

2. *Bilateral Agreements*

A number of cooperation agreements have been entered into by the Fund with other international organizations.

A 1947 agreement with the United Nations (U.N.) governs the relations between the Fund and the U.N.[49] This agreement recognizes the Fund as a specialized agency within the meaning of the U.N. Charter (Article 57). That does not mean that the Fund has become an agency of the United Nations; the term agency does not connote any subordination of the Fund to the U.N. Article I.2 of the Agreement is quite clear on this point: "By reason of the nature of its international responsibilities and the terms of its Articles of Agreement, the Fund is, and is required to function as, an independent international organization."[50] The same Agreement recognizes that the Fund is not bound by the resolutions of the Security Council; the Fund only notes the obligatory effect on U.N. members

47. *Id.* art. I(v).

48. International Covenant on Economic, Social and Cultural Rights, G.A. Res. 2200A, 21st Sess., Agenda Item 62, U.N. Doc. A/RES/2200 (1966).

49. Agreement Between the United Nations and the International Monetary Fund, *in Selected Decisions*, *supra* note 15, at 651.

50. *Id.* at 651.

of Security Council resolutions adopted under Article 48, paragraph 2, of the U.N. Charter and undertakes to pay due regard to resolutions of the Security Council under Articles 41 and 42 of the U.N Charter.[51]

In 1996, the Fund entered into a cooperation agreement with the World Trade Organization (WTO).[52] One of the difficult issues during the negotiation of the agreement was whether the Fund could communicate its findings concerning the consistency or inconsistency of a particular exchange measure with the Fund's Articles to a dispute settlement panel of the WTO. This possibility was acknowledged in the agreement (paragraph 8). However, when approving the agreement, the General Council of the WTO decided that the Fund's communication would only be made to the Chairman of the Dispute Settlement Body, who would inform the chairman of the panel of the availability of the communication. This procedure created a risk that the panel would never see the Fund's communication, a result inconsistent with the terms of the agreement. On the other hand, it was probable that the panel would be informed by its chairman and would decide to see the Fund's communication. Only experience would tell. Therefore, the Fund's Executive Board, made aware of the General Council's decision, decided to approve the agreement "on the understanding that decisions taken by either party for the implementation of the Agreement will not prevent the effective application of this Agreement in accordance with its provisions."[53] The terms "either party" rather than "the WTO" were used to soften the message.

The President of the World Bank and the Managing Director of the Fund have adopted arrangements for cooperation at staff level between the two organizations. These arrangements have been communicated to the Executive Boards of both organizations. They delineate the areas of primary responsibility of the Fund and the Bank and recognize the existence of common areas where their responsibilities overlap.

It has been suggested that the Fund should enter into a cooperation agreement with the International Labour Organization for the exchange of information and with a view to giving effect to core labor standards through Fund conditionality and surveillance.

3. *Multilateral Cooperation*

A number of proposals have been made to increase multilateral cooperation among international organizations. Most of these proposals recognize the need to respect the mandate of each organization although, often implicit in the proposals, is the underlying assumption that closer cooperation will lead to a different reading of each organization's charter, more accommodating to the views of others. Some of these proposals give preeminence to the U.N. over specialized agencies for a number of reasons. The most important is that the U.N. has a general mandate while specialized agencies have a limited mandate. Another reason is of a legal nature: under Article 103 of the U.N. Charter, obligations of U.N. members under the Charter take precedence over their obligations under other treaties. A third reason is more political: it is that the one country-one vote system of the U.N. is claimed to be more democratic than the weighted voting system of international financial institutions. Other proposals tend to emphasize cooperation among the specialized agencies involved in trade, financial and labor issues. The U.N. has taken an initiative called

51. *See* art. VI, para. 1, of the Agreement Between the U.N. and the Fund, *in Selected Decisions*, *supra* note 15, at 653.

52. See the text of the Agreement *in Selected Decisions*, *supra* note 15, at 905.

53. Decision No. 11381-(96/105), Nov. 25, 1996, *in Selected Decisions*, *supra* note 15, at 901.

Financing for Development, which should result, in 2002, in concrete proposals for closer cooperation within the U.N. system.

## IV. Conclusion

What is the future of the Fund? Some suggestions have been made to revise its role as a financial institution, while others question its very existence.

1. The suggestions concerning the financial role of the Fund go in two opposite directions.

(a) In the current discussions on the future of the Fund, one of the most challenging suggestions is to return to a pre-1948 situation, before the invention of conditionality and the evolution of conditionality toward greater and greater involvement in structural policies of members. The Fund's assistance would be unconditional and of a short-term nature, essentially for monetary intervention purposes. This would obviously exclude all or most developing countries from Fund assistance, as the correction of their balance of payments usually requires structural adjustment. Even other countries would only qualify if the correction of their problem did not require any particular measures, which is rather unlikely. In fact, the only countries qualifying for Fund assistance would probably be those that need it least because the quality of their policies gives them easy access, at a low cost, to financial markets. The unsuccessful (so far) experience with the Contingent Credit Lines, a facility that has found no takers, is not a good omen for the usefulness of the Fund under this proposal.

(b) At the other end of the political spectrum, there are suggestions for using Fund resources for generalized debt forgiveness beyond the HIPC initiative. The problem with debt forgiveness is that, once it is recognized as a moral obligation of the international community, it is quickly perceived as an entitlement, which authorizes inappropriate policies among debtors and imprudent lending among creditors. Debt forgiveness tends to be addictive; it may also clear the way for renewed excessive borrowing and resource misallocation if there is an expectation of future debt forgiveness. There are clearly humane considerations in favor of debt forgiveness but, if it is financed with public money, it is the ultimate form of moral hazard and, if the burden falls on private lenders, it leads either to usury or to the suspension of all forms of credit.

2. The existence of the Fund has been questioned by its detractors in two different ways. Some would like to see it abolished. Others would like to have it merged with the World Bank.

(a) Those who see the Fund as a harmful institution fall into two groups. One group believes that balance of payments assistance should no longer be extended and debtor countries should have to fend for themselves. This seems to ignore the major risks that this nonassistance by the Fund would generate: either a need for bilateral assistance, on a case-by-case basis, or a return to a "beggar thy neighbor" policy. Moreover, the Fund is not only a provider of financial assistance. It performs a number of other functions and some other agency would have to be created to fill the gap created by the abolition of the Fund.

Another group blames the Fund for being too strict. However, this would militate for a relaxation of Fund conditionality, not for a termination of Fund assistance. Moreover, the same question as above about the Fund's other functions would arise.

(b) In light of the related and sometimes overlapping functions of the World Bank and the Fund, why not merge them? This would have at least one advantage: conflicting advice would not be given to the same country requesting financial assistance. The new organi-

zation would be endowed with the resources of both the Fund and the Bank, which could be used for balance of assistance and development purposes. However, two main issues would have to be resolved. The first one is whether the new organization would be a purely financial institution or would retain the other roles of the Fund, in particular, as a regulatory agency. The second issue arises from the differences in the financial structure of the two institutions: the Fund's resources come exclusively from its members and, while the Fund could under its Articles borrow from the private sector, this has not happened. The Fund sees itself as a non-profit making cooperative institution for the mutual benefit of its members; as such it should not be dependent upon the willingness of financial markets to provide the financing that may be needed for the Fund's rescue operations. In contrast, the World Bank's subscribed capital is mainly a guarantee of the Bank's solvency; only a small part of the capital is paid-up and most of the financing comes from financial markets. The reason is that the World Bank is supposed to make profitable investments, including in the private sector, which is not the case for the Fund. The differences between the two institutions may not be irreconcilable, but if the solution were a merger into one organization with two totally separate departments, it would be a complicated way of achieving nothing.