Public International Law in the International Monetary System

Joseph Gold

Follow this and additional works at: https://scholar.smu.edu/smulr

Recommended Citation
https://scholar.smu.edu/smulr/vol38/iss3/2

This Article is brought to you for free and open access by the Law Journals at SMU Scholar. It has been accepted for inclusion in SMU Law Review by an authorized administrator of SMU Scholar. For more information, please visit http://digitalrepository.smu.edu.
PUBLIC INTERNATIONAL LAW IN THE INTERNATIONAL MONETARY SYSTEM

by

Sir Joseph Gold*

I. AN APPROACH TO DEFINITION OF THE INTERNATIONAL MONETARY SYSTEM

This paper, as a contribution to the symposium entitled Public International Law and the Future World Order conducted under the auspices of the Southern Methodist University School of Law in March 1984, considers a special but enormously important segment of the relations among states and the prospects for greater order in those relations. The subject matter of these relations is monetary in character and can be distinguished, therefore, from all other relations, although the word "monetary" is not free from ambiguity.

A question that arises immediately is whether monetary relations among states are conducted according to rules, principles, or practices that constitute an international monetary system. It might be objected that the question as formulated in this way is tendentious because even in the absence of rules there will be practices, and, further, because the absence of rules implies a principle, even if it is a principle of freedom from constraint.

The question has to be discussed because the expression "international monetary system" is now a term of art in legal provisions. Within the International Monetary Fund (IMF), the first important legal instrument in which the term was incorporated was the decision of the IMF called the General Arrangements to Borrow (GAB).1 The decision was adopted by the IMF on January 5, 1962, and became effective on October 24, 1962, as an agreement between the IMF and ten participants, of which eight were leading industrial members of the IMF and two were the central banks of two other such members. The ten participants agreed to consider requests by the IMF to borrow from them to supplement its resources to forestall or cope with an impairment of the international monetary system in what

were then the new conditions of the convertibility of currencies and greater freedom for exchange markets.

The expression "the international monetary system" received greater legal importance when it was included in the Articles of Agreement of the IMF for the first time by the Second Amendment, which became effective on April 1, 1978. The term, which appears in various provisions, is not defined by the Articles or in any decision of the IMF. The principal function of the expression is to refer to the relations among states that are within the IMF's field of interest under its power to supervise the management and supervision of the international monetary system.2

The status of the expression as a term of art led me, in lectures delivered at the Academy of International Law at The Hague in 1982, to consider the interrelationships among the concept of the international monetary system, the IMF, and international monetary law.3 Some of the ideas advanced in those lectures are summarized in the next paragraphs, with some additional reflections, as an introduction to the present paper.

Some writers, usually economists, have attempted to define, or to demarcate the terrain of, the international monetary system. One tendency has been to list the normative elements, but this approach does not arrive at a principle that unifies the elements or distinguishes the category of international relations that are the subject matter of a system composed of these elements from other international relations. Moreover, a list of the normative elements is unsatisfactory as a definition because the elements change from time to time. The changes can be the inclusion or exclusion of elements or modifications in them. An example of the inclusion of a new element in the system is the power conferred on the IMF by the First Amendment of the Articles, which took effect on July 28, 1969, to create reserve assets in the form of SDRs (special drawing rights) for allocation to members. An example of exclusion is the elimination of gold from the role of primary reserve asset in the system by the Second Amendment. The radical changes in the norms relating to exchange rates are an example of change in a continuing element of the system, namely, international concern with exchange rates.

Some authors have concentrated on the objectives or qualities of the international monetary system, or on the problems that it should solve. These authors make useful contributions to clarification, but these efforts also are open to the criticism that they do not provide a principle by which to isolate the relations among countries that are the subject matter of the system.

2. Articles of Agreement of the International Monetary Fund, Sched. D, para. 2(a) (unless otherwise stated, all references to provisions are to the present Articles of Agreement of the IMF) [hereinafter cited as Articles of Agreement]. See also Resolution No. 29-8 of the IMF's Board of Governors, Oct. 2, 1974, para. 3, reprinted in 10 SELECTED DECISIONS OF THE INTERNATIONAL MONETARY FUND AND SELECTED DOCUMENTS 346-47 (1983) [hereinafter cited as SELECTED DECISIONS].

A better approach to a definition focuses on relations through national balances of payments and holds that the system is composed of the rules governing these relations. The monetary authorities, which consist of the Treasury, central bank, stabilization fund, or other fiscal agency, are normally in charge of the relations. Each of these agencies may have authority under its national law to conduct part of or all the international monetary relations of its country.

An alternative but similar approach to a definition is that the international monetary system consists of the rules that relate to the adjustment or financing of the balances of payments. The rules include those that monetary authorities are legally bound, or consider themselves morally bound, to observe to prevent or eliminate a condition of the balance of payments that cannot be sustained without undesirable consequences.

Either of the approaches as described above represents an intermediate position between two extreme views. At one extreme is the view that the international monetary system consists of all the rules and practices that apply to the transactions of both monetary authorities and private parties that affect the balance of payments. At the other extreme is the view that the international monetary system consists solely of those rules affecting the balance of payments that monetary authorities have undertaken to observe by international agreement in the strict sense.

The view that is intermediate between these two extremes is cogent because it is inconceivable that the IMF could exercise supervision over the management and adaptation of the rules and practices according to which monetary authorities and private parties conduct their multitudinous activities across national boundaries. The other extreme view would lead to equally impractical results. It would exclude, for example, agreements between central banks, which, according to some theories of international law, are not international agreements in the same sense as treaties. Yet, agreements between central banks have profound effects on international monetary relations and sometimes are entered into by the central banks because they have the authority to do so under existing legal provisions. The decisions that they should enter into agreements may be taken, however, by the Treasury on behalf of the national Executive. Furthermore, the extreme view considered here would cast doubt, again according to some conceptions, on whether agreements by countries to collaborate, consider, or consult on monetary matters are part of the international monetary system because of the imprecision or subjectivity of these obligations.

The intermediate view means that the international monetary system consists of a complex of relationships among countries on matters affecting the adjustment or financing of the balance of payments that are governed by rules and understandings that are more extensive than international monetary law as a branch of public international law. Nevertheless, public international law, principally in the treaty form, is now at the heart of the

---

5. J. Gold, supra note 1, at 446-68.
international monetary system. An implication of the intermediate view is that the rules and understandings are taken seriously by countries, and that if countries fail to observe the rules and understandings there will be some response even if it consists only of censure. Another implication may be that an international organization at the center of the system is necessary to administer the main rules. There is such an organization, the IMF. It is itself part of the system. Its law and the law governing the monetary functions of other international organizations are part of international monetary law.

II. AN APPROACH TO THE IDEA OF ORDER IN THE SYSTEM

If the Future World Order means the future of order in the world, how shall order in the international monetary system be understood? Order can be taken to mean the realization—or at least a close approximation to it—of the purposes to which most countries have subscribed by becoming members of the IMF. Article I of the IMF's Articles is the most elaborate formulation of these purposes. The provision was the product of intensive negotiation before and at the Bretton Woods Conference in July 1944 at which the Articles were drafted. Article I has remained intact, with only slight modifications that did not affect substance on the occasion of the First Amendment. The longevity of Article I is remarkable in view of the profound changes that have occurred in the international monetary system.

The purposes of the IMF refer to an international monetary organization, the expansion and growth of international trade, stability and equity in the exchanges, the convertibility of currencies, the availability of resources to give members the opportunity to correct maladjustments in their balances of payments, and limitation of the period and intensity of disequilibria in balances of payments. No paraphrase can give an adequate impression of Article I, in which the purposes are formulated as follows:

(i) To promote international monetary cooperation through a permanent institution which provides the machinery for consultation and collaboration on international monetary problems.

(ii) 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.

(iii) To promote exchange stability, to maintain orderly exchange arrangements among members, and to avoid competitive exchange depreciation.

(iv) To assist in the establishment of a multilateral system of payments in respect of current transactions between members and in the elimination of foreign exchange restrictions which hamper the growth of world trade.

(v) To give confidence to members by making the general resources of the Fund temporarily available to them under adequate safe-
guards, thus providing them with opportunity to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity.

(vi) In accordance with the above, to shorten the duration and lessen the degree of disequilibrium in the international balances of payments of members.\(^6\)

When the original proposals for a currency plan that ultimately took the form of the Articles was under discussion, the British experts led by John Maynard Keynes advocated a plan, Proposals for an International Clearing Union, under which the international organization to be created would have issued an international monetary reserve asset ("bancor") to participating countries.\(^7\) The U.S. experts feared that the United States, as the country most likely to be in surplus in its balance of payments, would have to accept an unduly large proportion of bancor in settlement for the real resources it would be providing. The United States, preferring a limited and certain exposure, was successful in achieving this aim in the form of an obligation to make a defined subscription.\(^8\)

In the Sixties a widespread conviction developed that the international monetary system was threatened by a dilemma in which one horn was the continued addition of a surfeit of U.S. dollars to the monetary reserves of other countries as a result of deficits in the balance of payments of the United States and the other horn was a shortage of monetary reserves with which to ensure growth in international activity if the deficits were curbed or ceased. The world returned to the idea of a monetary reserve asset, the SDR, that could be allocated by the IMF to its members. This development was the most important one that had occurred since Bretton Woods, but the objectives that were to be served were not included among the purposes in Article I. The difficulty with which that provision had been negotiated originally discouraged the amendment of it. In addition, the

---

\(^6\) Articles of Agreement, Art. I.

\(^7\) (a) We need an instrument of international currency having general acceptability between nations, so that blocked balances and bilateral clearings are unnecessary; that is to say, an instrument of currency used by each nation in its transactions with other nations, operating through whatever national organ, such as a Treasury or a Central Bank, is most appropriate, private individuals, businesses and banks other than Central Banks, each continuing to use their own national currency as heretofore.

\(^8\) Furthermore, a member's quota could be adjusted—subscription was equal to quota—only with the consent of the member, and the provision requiring consent could be amended only with the acceptance of all members. These provisions of the original Articles remain in the present Articles as Article III, § 2(d) and Article XXVIII(b).
provisions relating to the SDR were included in what was really a new and
discrete chapter added to the Articles so as to disturb the original provi-
sions as little as possible. The statement of a new purpose could not be
avoided, but it was included, in the following form, in the new chapter:

In all its decisions with respect to the allocation and cancellation of
special drawing rights the Fund shall seek to meet the long-term
global need, as and when it arises, to supplement existing reserve as-
sets in such manner as will promote the attainment of its purposes and
will avoid economic stagnation and deflation as well as excess de-
mand and inflation in the world.

This provision is drafted in both teleological and normative language.

The Seventies saw the collapse of the par value system that had been
established by the original Articles and the adoption of the Second
Amendment as a consequence. The revised Articles contain language that
formulates a purpose of the international monetary system. The purpose is
not drafted as a purpose of the IMF, so to avoid a normative principle
from which the Fund could draw regulatory jurisdiction over members,
in contrast to the provision of the First Amendment, quoted above, which
was drafted as a normative direction. Once again, the new provision was
not included in Article I. The pertinent language of the Second Amend-
ment is as follows:

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 that sustains sound
economic growth, and that a principal objective is the continuing de-
development of the orderly underlying conditions that are necessary for
financial and economic stability.

By avoiding a normative formulation, the drafters were able to express a
purpose of great breadth. It embraces, for example, the exchange of goods,
services, and capital, over which the IMF does not have regulatory jurisdic-
tion. The argument for considering the language as indicative of a pur-
pose of the IMF is that the provision sets forth an "essential purpose of the
international monetary system" and the IMF is charged with the duty to
"oversee the international monetary system in order to ensure its effective
operation," in addition to the function of supervising the management
and adaptation of the international monetary system. The duty to over-
see the system so as to ensure its effective operation is strong language, but
as of the date of this paper no attempt has been made to explore what
authority this duty confers on the IMF.

9. J. Gold, supra note 1, at 128-47.
10. Articles of Agreement, Art. XVIII, § 1.
11. See generally Gold, Strengthening the Soft International Law of Exchange Arrange-
13. Id. Art. IV, § 3(a).
14. See supra note 2 and accompanying text.
15. Although the duty is set forth in Article IV, § 3(a), and Article IV is headed "Obli-
gations Regarding Exchange Arrangements," Article IV, § 3(a) is formulated so as to
III. Regulation of the International Monetary System

The original Articles of Agreement of the IMF, which were drafted at the Bretton Woods Conference in July 1944 and became effective on December 27, 1945, were the first multilateral charter for the regulation of the international monetary system. The Agreement is a treaty among countries that provides for their membership in the IMF. The Articles were not the first treaty on monetary matters. For example, during the First World War, the U.S. Congress, in the exercise of its banking and currency power, passed the Second Liberty Bond Act to authorize the U.S. Administration to make arrangements with foreign countries during a limited period to stabilize foreign exchange and to obtain foreign currencies. Under the same congressional power, the U.S. Administration was authorized by the Gold Reserve Act to deal in gold and foreign exchange for the purpose of stabilizing the exchange value of the U.S. dollar, without limitation on the period during which agreements might be entered into under this authority.

The latter statute was the authority under which the United States exe-
cut the Tripartite Currency Stabilization Agreement of 1936 by means of bilateral agreements with France and the United Kingdom. Later, the Netherlands and Switzerland adhered to the principles of the agreement. The importance of the stabilization agreements, and particularly the Tripartite Agreement, is that they were in the mind of Harry Dexter White of the U.S. Treasury, the official who, with colleagues, in the early Forties produced the Preliminary Draft Outline of a Proposal for an International Stabilization Fund of the United and Associated Nations.

Both Keynes and White were aware that their plans, if accepted, would introduce innovations of radical importance in international law. Published records show how concerned Keynes was with such questions as the degree of sovereignty that states should be willing to forgo in monetary matters. The tradition of centuries had been that these matters were exclusively within the jurisdiction of each state, and that states were entitled to act unilaterally whatever the impact might be on others. It is not surprising, therefore, that Keynes paid much attention to the division between the authority that each member should retain and the authority that all members should concede to a new international organization. Both Keynes and White discussed the justification for surrendering authority...
to an external entity.

Keynes discussed other issues of interest to international lawyers then and now. For example, how much of the authority of the new international organization should be the subject of precise rules and how much should be left to its discretion? What was the value of the right of withdrawal by a member from the organization?

IV. Original Articles

The Articles of Agreement that emerged from the Bretton Woods Conference were largely in accordance with the preferences of the United States. The U.S. and the British prenatal plans agreed that a code of obligations to govern international monetary relations should be instituted, and that the countries that became members of the IMF should contribute to a pool of resources on which members facing balance of payments difficulties could draw. Balance of payments difficulties could be overcome within the short to medium term and were said to be "temporary." Longer-term difficulties were problems of reconstruction and development and were to fall within the competence of the World Bank. The resources of the IMF were to be available to enable a member to solve its balance of payments problem without following policies or adopting measures that were inconsistent with the obligations in the code of conduct. This combination of regulatory authority and financial resources is still unique among multilateral international organizations.

Keynes and White agreed that a central monetary organization must have authority over exchange rates. The appropriate exchange rate for a member's currency was crucial if disequilibrium in the member's balance of payments was to be avoided or eliminated. Regulatory authority over exchange rates raised the issue of the surrender of sovereignty that concerned them both. White supported somewhat more authority for the organization than Keynes was willing to concede. The provisions of the Articles on par values on which agreement was reached included compromises that in some important aspects favored the view of Keynes that a member should retain substantial authority over the external value of its currency.

Keynes and White differed more sharply on the resources that were to be available to facilitate observance of the code of conduct. As noted above, Keynes wanted the organization to be able to create resources, while White wished to limit the resources to those that would be subscribed by members. White wanted the organization to be able to borrow if it needed to augment its subscribed resources, but the organization would have to find a willing lender. The concurrence of the member that

---

24. See infra Appendix B.
25. 3 J. Horsefield, supra note 7, at 20; see also Gold, Keynes on Legal Problems of International Organization, 14 Conn. L. Rev. 1 (1981) (discussing Keynes's views on the problems of establishing of an international economic system).
issued the currency to be borrowed would have to be obtained if the member itself was not the lender. The U.S. approach on subscribed and borrowed resources prevailed. The power to borrow has had an increasingly important function in the IMF's activities, partly because quotas have been too low. The power has given Managing Directors the legal basis on which to rely in proposing new departures in the IMF's activities to meet new problems.

Even after the Bretton Woods Conference there remained a difference of opinion on the use of the IMF's resources that was related to considerations of sovereignty. According to the British view, a member should be able to use the IMF's resources automatically, which meant without challenge by the IMF, unless the member wanted to draw from the pool an abnormal amount in proportion to its quota. The U.S. view was that a member's right to use the IMF's resources was always subject to scrutiny and could be challenged for good cause. The U.S. position prevailed and led in time to the doctrine of conditionality, which requires a member to satisfy the IMF that the use of its resources will be in accordance with its purposes.

The par value system, which was at the heart of the IMF's regulatory jurisdiction, recognized that exchange rates were matters of international concern. Therefore, exchange rates should be subjected to international examination and should carry international endorsement. Each member had to establish a par value for its currency in terms of gold, or in terms of a U.S. dollar of fixed gold content, which had the same effect. The option existed because, under the laws of some countries, the external value of the currency was defined in relation to the U.S. dollar. Gold was the common denominator of the par value system because of the traditional acceptability of gold and its function as a monetary reserve asset. The agreement of the IMF was necessary for the initial par value that was established under the Articles, and the concurrence of the IMF had to be obtained for a change of par value. The word "concurrence" was intended to imply that the IMF would lean in favor of a proposed change. To promote exchange stability, a change was justified only if it was necessary to correct a fundamental disequilibrium.

In accordance with the underlying legal principle that each member is responsible for its own currency under the Articles, each member was required to maintain the effectiveness of the par value of its currency as established under the Articles. This obligation was expressed in operational terms by requiring each member to take appropriate measures consistent with the Articles to ensure that spot exchange transactions in the member's territories were carried out at exchange rates within the narrow margins defined by the Articles. These margins were around the "parity," i.e. the ratio derived from the par values of the two currencies that were the subject of the exchange transaction.26 The IMF had no authority to approve a

26. A member’s obligation was based on an apparent territorial view of jurisdiction, but the provision raised the question of the territory or territories in which exchange transactions
member's withdrawal of support for the par value of its currency. Floating was a heinous retreat to disorder. A member had only the option of changing an unsupportable par value to one that it could maintain, and even an interval of floating was illegal.

The United States did not wish to police its exchange markets to make sure that exchange rates for the U.S. dollar were within the defined margins. It negotiated a provision at the Bretton Woods Conference that entitled, but did not compel, a member to follow a particular practice that was deemed to be an appropriate measure on exchange rates. The practice was the readiness of a member to buy and sell gold for its own currency in transactions requested by the monetary authorities of other members, at prices compatible with the par value of the currency. The theory of the provision was that a member following the practice was taking reasonable action to maintain the external value of its currency in terms of gold as the common denominator of the par value system. If exchange transactions involving the currency occurred at exchange rates outside the margins for exchange transactions imposed by the Articles, the responsibility could be attributed to the failure of other members to engage in gold transactions with the member that was prepared to enter into them. These transactions would enable a member that requested them to intervene in its exchange market to support the exchange rate for its currency in relation to the currency convertible into gold. The member supported its currency by buying or selling the gold-convertible currency in exchange for its own currency. The gold-convertible currency could be obtained or disposed of for gold in transactions with the issuer of that currency.

It was apparent at Bretton Woods that only the United States would have the resources to engage in gold transactions under the provision it had negotiated. The United States may have assumed that the strength of its prospective balance of payments would not result in substantial outflows of gold. The only member that did purport to engage in gold transactions in support of its currency under the provision was the United States.

Certain consequences followed from the declaration by the United States that it was prepared to follow the practice. First, this undertaking by the United States became the foundation of the par value system in fact, because the undertaking enabled other members to refrain from engaging in gold transactions. Instead, members could retain their holdings of U.S. dollars for investment, using them to intervene in exchange mar-

---

27. Articles of Agreement, Art. IV, § 4(b) (original Articles); J. GOLD, supra note 1, at 547-49.

---
kets when necessary to manage exchange rates. Members could earn interest by investment with the assurance that gold was available on demand if they wished to add gold to their reserves. Moreover, members could be confident that the U.S. economy would be so well managed and so strong that there would be no prospect of a devaluation of the dollar and, therefore, no risk of loss as a result of holding dollars. This confidence was based not entirely on faith because the privilege of members to call for gold could have a disciplinary influence on the United States.

Second, the undertaking assured members of symmetry in the international monetary system. Symmetry in the treatment of groups of countries perceived to be in different situations in the international monetary system was a principle of the system even if the principle was not made explicit until more recent times. The United States was obviously different from all other members in the international monetary system because of the way in which the par value system operated and for other reasons. Symmetry existed in the structure of the par value system in theory because other members intervened in the exchange markets with their holdings of U.S. dollars, or currencies convertible into dollars, while the United States would provide gold to other members, on demand, in the comprehensive settlement of international transactions. Both the United States and other members would use reserve assets in support of the exchange rates for their currencies.

For lawyers, it may seem remarkable that the par value system rested in reality on a voluntary undertaking by the United States. The situation recalls the philosophical theory that a legal system rests on a norm that is outside the system in the sense that it is not prescribed by the system. The undertaking became the fundamental norm of the international monetary system because of the assumption that the strength and stability of the U.S. economy would be maintained.

A second consequence of the par value system in operation was the passivity of the U.S. monetary authorities in the exchange markets. This passivity was authorized by the provision on gold transactions, but Keynes


29. In time, the United States would object that the system did not assure it of symmetry for various reasons. For example, when the United States was in deficit in its balance of payments, it would lose gold to other members, but they did not provide gold to the United States when they were in deficit. Instead, they transferred dollars to the United States, or, in other words, cancelled its currency liabilities, which did not provide it with additions to its monetary reserves. Second, the United States could be called on for gold, even though it was not in deficit in its balance of payments, because the member tendering dollar balances for conversion with gold was in surplus with other members. To cure these flaws, the concept of "asset settlement," in lieu of the former convertibility, evolved during the attempt to reform the international monetary system after the collapse of the par value system. INTERNATIONAL MONETARY FUND, REFORM OF THE INTERNATIONAL MONETARY SYSTEM: A REPORT BY THE EXECUTIVE DIRECTORS TO THE BOARD OF GOVERNORS 31-40 (1972); COMMITTEE ON REFORM OF THE INTERNATIONAL MONETARY SYSTEM AND RELATED ISSUES, INTERNATIONAL MONETARY REFORM: DOCUMENTS OF THE COMMITTEE OF TWENTY (1974) [hereinafter cited as DOCUMENTS OF COMMITTEE OF TWENTY].
was distressed immediately after the Bretton Woods Conference at the prospect that the United States would not take other action to prevent the depreciation of sterling in the U.S. exchange market. Keynes exhorted the U.S. authorities, without success, to adopt legislation that would make exchange rates outside the prescribed margins illegal in the United States.\footnote{26 The Collected Writings of John Maynard Keynes: Activities 1941-1946, Shaping the Post-War World, Bretton Woods and Reparations 142-43 (D. Moggridge ed. 1980) [hereinafter cited as 26 Keynes].}

An irony of international monetary history is that the provision Keynes found objectionable because it permitted passivity by the United States was the basis of the complaint by the United States almost three decades later that it suffered fundamental disadvantages in the system.

Later, the principle was expounded that in any orderly system of exchange rates in which there were $n$ currencies, there would be $n-1$ exchange rates. The theory justified passivity, because if the United States pursued an active exchange rate policy, the result might be conflict between that policy and the exchange rate policies of other members. It was possible, however, as practice demonstrated from time to time, to coordinate intervention by the United States and other members in exchange markets in support of a common policy. The argument in support of passivity supposes that there would be circumstances in which exchange rate policies were inconsistent and could not be reconciled.

The par value system operated successfully in producing an environment in which international economic activity flourished, but there were flaws that contributed to a faltering and then a collapse of the system. Repeated deficits in the U.S. balance of payments shook confidence in the dollar. Members did not propose the prompt changes in the par values of their currencies that would avoid maladjustment in their balances of payments. The IMF had no legal authority to propose a change. Many other flaws, some but not all of which were inherent in the legal structure of the par value system, can be added to the roster of weaknesses that led to collapse.

For some years before the fall of the par value system, however, symmetry had ceased to exist. As confidence in the dollar ebbed and the U.S. stock of gold was reduced progressively by conversions of dollar balances, the United States adopted one technique after another to offer other benefits that would discourage conversions. The realization grew that conversions were economically inopportune because they might shatter the structure of the par value system and were politically inopportune because they might arouse the ire of the United States. The undertaking of the United States to engage in official gold transactions was not challenged as the fundamental norm by the IMF or by other members, even though the undertaking had become a legal fiction. The experience demonstrated that an international monetary system can be created on the basis of a legal fiction, unless that fiction is repudiated by the actors in the system. The Smithsonian Agreement was a further demonstration of this possibility be-
cause the understandings on new par values for the currencies of the parties were accompanied by no promise of the United States to convert official holdings of dollars or to intervene in the exchange market. On August 15, 1971, it was the United States that implicitly repudiated the legal fiction.

An objective of the par value system was fixed and stable, but not rigid, exchange rates. Among the other objectives of the provisions on exchange rates were the avoidance of multiple currency practices, discriminatory currency arrangements, and competitive exchange alterations. These provisions were of particular interest to the United States. The order that would be achieved if the purposes of the IMF were realized would benefit all members, including the United States, but that country saw itself as the most likely victim if disorderly practices, such as discrimination and competitive devaluation, were resorted to in the disturbed conditions that would follow the Second World War. The role of the IMF in eliminating and preventing these practices was a special benefit for the United States. Self-interest does not preclude altruism: the mixture is often called enlightened self-interest. The United States agreed, for example, that members would be able to maintain existing discriminatory practices, and to adapt them, under transitional arrangements. Moreover, the United States even proposed the so-called “scarce currency clause” that would enable other members to introduce discrimination against a member if the IMF found that the member’s currency was scarce.

Roy Harrod’s biography of Keynes should be read if the impact of the U.S. proposal on British officials is to be grasped. Here is a brief extract that recalls Harrod’s reaction as he first read the draft in the dim light and crowded conditions of a wartime train in February 1943:

I could not believe my eyes or my brain. I read it again and again. . . . I was transfixed. This, then, was the big thing. For years we had complained of the United States’ attitude as a creditor. For months we had struggled in vain to find some formula which would pin them down to a share of responsibility. Now they had come forward and offered a solution of their own, gratuitously. This was certainly a great event. For it was the first time that they had said in a document, unofficial, it was true, and non-committal, but still in a considered Treasury document, that they would come in and accept their full share of responsibility when there was a fundamental disequilibrium of trade.

Even so, the final version of the clause was strengthened, and again the initiative was taken by the United States.

The importance for the British was not the expectation that the clause

---

31. Articles of Agreement, Art. VIII, § 3 (original Articles).
32. Id. Art. I(iii); Id. Art. IV, § 4(a) (original Articles).
33. Id. Art. VII, § 3 (original Articles).
34. R. Harrod, The Life of John Maynard Keynes, 544-45 (1951). For the full account, see id. at 543-48.
35. Id. at 565, 571-72.
would be invoked against the United States, but that the principle noted by Harrod was acknowledged. The expectation was that the United States would take steps to avoid a severe “dollar shortage.” This expectation was realized: the clause has never been applied even though it has remained in the Articles throughout the three versions. U.S. policies were those of a good creditor, so that there was no justification for relying on a clause that authorized an action considered to be a sanction. It is true, however, that the transitional arrangements reduced any disposition to apply the clause, because they authorized the maintenance and adaptation of restrictions, including discriminatory restrictions.

The multilateral system, or market convertibility as it has been called sometimes, was another major feature of the regulatory jurisdiction of the IMF under the original Articles. Members not availing themselves of the transitional arrangements were to avoid restrictions on the making of payments and transfers for current international transactions, so that what was earned in these transactions in one country could be used in payments for transactions in other countries. The Articles recognized that members retained the authority to control capital movements. The damaging effects of movements of “hot money” in the period between the two World Wars were among the reasons why members would not give up any part of their authority over capital transfers.

The drafters of the original Articles expected many members to centralize the foreign exchange earned by their residents. One purpose of the surrender of foreign exchange was to prevent capital flight. Surrender requirements were not prohibited, because surrender was not in itself an impediment to the making of payments. It did not follow that a member would refuse to provide its residents with the foreign exchange they needed to make payments for current international transactions, or that the member would refuse to provide nonresidents with the means to transfer into their own currency their earnings in current transactions with residents.

The IMF’s resources were available to assist a member that found it difficult to provide the foreign exchange for either purpose. If there was a deficit in the member’s balance of payments, the member could turn to the IMF for resources. If as a result of a deficit in the balance of payments of

36. Articles of Agreement, Art. I(iv); Id. Art. VIII, § 2(a) (original Articles).
37. Id. Art. VI, § 3 (original Articles).
38. When it became clear that the U.S. did not share his (Keynes’s) view on this issue [the suggestion that central control of inward and outward capital movements should be a permanent feature of the post-war world], he insisted that strict capital controls be permitted in the new international monetary order in those countries which chose to adopt them. Keynes argued here, as he had in the 1930s, that the free flow of capital among countries would make successful domestic planning for full employment in any country impossible.

Terra, Patria, which imposed exchange surrender requirements on its residents, held the currency of Terra, Patria could require Terra to buy the balances of Terra's currency held by Patria. This was a form of official convertibility, because it operated only between monetary authorities. The obligation was subject to a number of limitations, among which two were most important. First, official convertibility was designed to be in support of market convertibility. Patria could demand the conversion of the balances it held only if they had been recently acquired as the result of current international transactions, or, if the balances did not meet this criterion, conversion was needed for making payments for current transactions. Second, the obligation had to be performed only if Terra was in a position to use the IMF's resources. This limitation did not mean that Terra had to use the IMF's resources in making the conversion, but only that it was able to use them if it wished.

Official convertibility through the mechanism of the IMF as explained above never became a feature of the international monetary system. The provision requiring official conversion was inspired in part by the prospect that the volume of foreign exchange necessary for payments and transfers for current international transactions might be too great for the exchange markets. In time, however, exchange markets developed sufficient capacity for this purpose. They were allowed to operate without the hindrance of surrender requirements. If a deficit developed in a member's balance of payments, the member could turn to the IMF not for the resources with which to convert foreign official holdings, but to put resources into the exchange market in support of the member's currency. Few currencies were used in international payments, and only these currencies were accumulated in the monetary reserves of members. In any event, therefore, few members would have been called on for official convertibility even if the obligation had been invoked. Moreover, the leading reserve currency by far was the U.S. dollar, and members could request gold for their holdings of dollars, if they wished, in accordance with the separate undertaking of the United States.

The neglect of official convertibility is an illustration of the radical misjudgments about future developments that the drafters of treaties can make. There was an elegance about the obligation of official convertibility that helped to complete a system based on par values and the multilateral system of payments and transfers for current international transactions. The wonder is not that the future was unforeseeable, but that the Articles could work effectively for so long, without legal strain, in conditions radically different from those that had been foreseen at Bretton Woods.

The theory that justified the contribution of resources to the IMF was that they could be made available to a member in balance of payments difficulty to enable it to support its currency either by performing the obligation of official convertibility or by maintaining market convertibility.
The resources helped a member to preserve the order that was the objective of the international monetary system under the original Articles. A member would not be forced by circumstances to withdraw support from the par value for its currency or to resort to restrictions, discriminatory currency arrangements, multiple currency practices, or competitive devaluation.

V. First Amendment

In 1969 the First Amendment of the IMF's Articles became effective, two years before the collapse of the par value system. The First Amendment was intended to reinforce the international monetary system as it then existed. Members were to be provided with monetary reserves, in the form of the SDR as a new reserve asset, if the IMF decided that there was a long-term global need to supplement existing reserve assets. Allocations were to be made, or SDRs cancelled, in such manner as would promote attainment of the purposes of the IMF and would avoid economic stagnation and deflation as well as excess demand and inflation in the world.40 The IMF would be able to manage the global volume of reserves in a rational manner if, as was hoped, the United States would eliminate the deficits in its balance of payments.

The original Articles gave the IMF regulatory functions to ensure stable exchange rates, a multilateral system of payments and transfers for current international transactions, and collaboration between members and the IMF on monetary problems. The task of the IMF was to preserve order not only by promoting these objectives, but also by acting as the organization to which other members were to address complaints that a member was failing to observe its obligations to maintain order. The Articles were based on a principle of reciprocity, qualified by certain limited derogations such as the transitional arrangements, but members were not permitted to resort to self-help if a breach of obligation occurred. If they could suspend their obligations by way of retaliation, disorder would be compounded. The IMF had the duty to see that a breach was repaired and full order restored.

The financial function of the IMF was to act, in effect, as a financial intermediary by providing the currencies of members in balance of payments surplus to members in balance of payments deficit. The First Amendment added a function that implied the management of official liquidity, including the form in which, to some extent, reserve assets should be held.

SDRs were a supplement to existing reserve assets, which meant, as one of the multiple connotations of this language, that neither currencies nor gold would be ostracized from reserves simply because of the arrival of the SDR.41 Some members were anxious to preserve the status of gold as a

40. Id. Art. XXIV, § 1(a) (First Amendment); Id. Art. XVIII, § 1(a).
reserve asset, while the United States wanted no suggestion of exile for the dollar. The allocation of SDRs, however, would enable members to receive additions to their reserves in the form of an internationalized asset instead of relying on a national asset, the U.S. dollar, the volume and quality of which depended on the policies of a single country. Furthermore, the vagaries of gold production and the destination of new gold need not give concern that gold was an unreliable source of reserves, even though gold remained in law the common denominator of the par value system and the subject of the U.S. undertaking as the fundamental norm of the system.

The benefits of the rational management of global reserves by means of the SDR scheme would accrue to all members, and the benefits were responsible for the vigorous support that the United States gave to the project that led to the First Amendment. The United States was interested in a more particular benefit for itself: the SDR could assist the United States to maintain the official convertibility of the dollar. As there was to be no frontal attack on the position of gold in the international monetary system, members were unwilling to forgo the privilege of obtaining gold from the United States in official settlements in accordance with the undertaking it had given under the original Articles. Faced with this resolve of other members, the United States wanted some assurance that it would be able to use its holdings of SDRs as well as its gold, when called upon to convert official holdings of dollars. The best that the United States could negotiate was a provision under which it could convert dollar balances with SDRs by agreement with the member that was tendering the balances for conversion.42

Whatever the future of the SDR may be, the agreement to create it was an extraordinary development in international organization, the international monetary system, and international law. As an imaginative and adventurous attempt to respond to international monetary problems it is second only to the agreement represented by the original Articles.

VI. COLLAPSE OF PAR VALUE SYSTEM

On August 15, 1971, the President announced that the monetary authorities of the United States would no longer convert foreign official holdings of dollars with gold or other reserve assets, and that no steps would be taken to see that exchange rates for the U.S. dollar were kept within defined margins. The United States had concluded that it was locked into an intolerable position in which it would not be able to achieve an effective devaluation of the dollar, and, therefore, the United States saw no point in proposing a change in par value. The United States had no hope of curing the disequilibrium in its balance of payments and restoring its lost competitiveness in international trade except by the drastic action it took. The

42. Articles of Agreement, Art. XXV, § 2(b)(i) (First Amendment); see id. Art. XIX, § 2(b).
country that was the chief architect of the international monetary system was aware that it was bringing about the collapse of the system. Although it did not justify its action by reference to anything like the plea of *rebus sic stantibus*, the assumption of persistent surplus in the balance of payments on the basis of which the United States had negotiated the Articles had been proved to be unfounded in the face of persistent deficits.

The action by the United States was in breach of its obligations under the Articles, but not by the withdrawal of the undertaking to engage in official gold transactions for dollars. That undertaking was not mandatory under the Articles. The breach was the failure to apply other appropriate measures that would restrain exchange rates in transactions involving the dollar and the currencies of other members within the margins around parities consistent with the Articles. The United States was responsible for taking other measures to ensure observance of the legal margins, because the abandonment of its undertaking had produced the neglect of parities for the dollar. A principle of the Articles, it has been seen, is that each member is responsible for its own currency, and that this responsibility cannot be thrust onto other members. The refusal of the United States to perform the obligation of official convertibility in support of the multilateral system of payments as discussed above was a further violation of the Articles.

VII. Second Amendment

From 1972 to 1974 strenuous efforts were made to reform the international monetary system. No direction was given to the discussions until the United States advanced a plan for a par value system that would have operated more symmetrically to compel adjustment by members whether in deficit or in surplus in their balances of payments. The United States had come to the view that its persistent deficits were the result of an unsymmetrical system that did not exert sufficient influence on members in surplus to compel them to adjust their balances of payments. The deficit of the United States about which many other members had complained was the mirror image of the persistent surpluses in some of their balances of payments. These members, however, blamed the predicament of the United States on its "benign neglect" of the balance of payments, which meant the preference of the United States to conduct its external and domestic policies without concern for its balance of payments.

The United States proposed a system that would be more mechanical as well as more symmetrical in compelling adjustment. Objective indicators based on increases or decreases in monetary reserves would point to the member or members that should take steps to adjust their balances of payments by appropriate measures, which might include changes in the par values of their currencies. The indicators would be decisive or at least

would raise a strong presumption that the member to which they pointed had the responsibility to take corrective action. Graduated pressures would be applied according to stages in the accumulation or loss of reserves. The amounts of reserves that would define these stages would be agreed with, or established by, the IMF. The pressures would resemble, but would not be considered, sanctions in the ordinary sense, because, by analogy to a concept of the original Articles and the First Amendment, disciplinary consequences could be attached to undesirable policies without treating the policies as breaches of obligation. The consequences, however, could be the same as those that were attached to actions classified by the Articles as violations of the treaty.\footnote{44. J. Gold, \textit{supra} note 1, at 148-216.}

The U.S. plan was based on two suppositions of some interest in international law and organization. One supposition was that there would be a widespread preference among other members for such a mechanical apparatus. The other supposition was that public opinion would more readily accept the mechanical operation of objective indicators than the exercise of discretionary authority by an international organization. The first supposition was shown to be unfounded because the representatives of other members made it clear that they preferred the exercise of discretion by an international organization. Members would have the opportunity to influence the judgments of the organization without the burden of having to rebut a presumption of responsibility for troublesome developments. For this reason members were not enthusiastic about even a weak presumption based on objective indicators. The correctness of the second supposition could not be tested because a par value system could not be restored.

The outcome of the efforts to reform the international monetary system was a tentative and incomplete \textit{Outline of Reform} that was transmitted to the Board of Governors of the IMF in June 1974 with the express realization that, at best, the reform would take place in the future.\footnote{45. \textit{Documents of Committee of Twenty}, \textit{supra} note 29, at 7-48.} A central feature of the \textit{Outline} was the restoration of a par value system, with the elimination of deficiencies that had been demonstrated in the operation of the original par value system. One improvement was recognition of the legality of floating in some circumstances. In the conditions of June 1974, there was no hope of instituting a par value system in any form, whatever the alleviations of its rigor might have been. The \textit{Outline} recommended a start on evolutionary reform by the adoption of a limited number of immediate steps during an interim period.

Such a project did not appeal to some members because it did not represent a thorough reform. The United States, however, pressed for the return to legality by means of an amendment of the Articles even if no more would be achieved than the legalization of practices that were then illegal. This attitude prevailed and led to the Second Amendment of the Articles, the negotiation and drafting of which were completed in March 1976. The Second Amendment became effective on April 1, 1978.


In the course of the period that succeeded the transmission of the Outline, the decision was reached that an amendment of the Articles should not concentrate on an interim period or on immediate steps, but should sweep across the full breadth of the Articles. The new provisions should be appropriate to the immediate situation, but should grant powers that would enable the international monetary system and the IMF to evolve without the need for further amendment, at least to meet foreseeable developments.

A major contest before the drafting of the Second Amendment was completed was the character of the exchange rate regime to be regulated by the Articles. Some members, with France most insistent among them, wanted some assurance of return to a degree of fixity in exchange rates. The United States resisted this attitude. It would not support any expression of the legal or moral superiority of fixed exchange rates at any time. The rejection of an obligation to maintain a fixed external value for currencies would enable members to concentrate on domestic policies. The fluctuation of exchange rates to accord with underlying conditions would produce exchange rates that were economically appropriate, and would encourage members, whether in surplus or in deficit in their balances of payments, to develop orderly underlying conditions and to eliminate too much fluctuation. The effect would be a stable system of exchange rates that would be more desirable than the imposition of fixed exchange rates, which, paradoxically, had not produced stability.

The United States succeeded in its opposition to any recognition of the desirability of fixed exchange rates. The main concession in the compromise with those members that preferred fixity at some time, although not an immediate return to it, was the inclusion in the Articles of a flexible par value system that could be called into operation if certain conditions were found to be satisfied. The decision to take this action could be made with a majority of eighty-five percent of the total voting power of members, which gave the United States a veto over a proposed decision.46

The outstanding characteristic of the provisions on exchange rates in the Second Amendment is that there is no insistence on a unified regime. Each member is free to choose its exchange arrangement, with the exception that a member may not maintain the external value of its currency in terms of gold. A member is free also to determine the external value of its currency under the chosen exchange arrangement. The Second Amendment departs from the design of the original Articles, under which only one exchange arrangement was permissible—a par value—and under which the par value had to receive the endorsement of the IMF.

The doctrine that exchange rates are a fit subject for international concern has not been abandoned, and, therefore, various safeguards have been adopted, including those that are listed here:

(a) Each member must observe certain obligations in the conduct of its

46. Articles of Agreement, Art. IV, § 4; id. Sched. C.
policies that bear directly or indirectly on exchange rates. These obligations are formulated for the most part in the language of soft law:

[E]ach 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.47

(b) The IMF must oversee the compliance of each member with the obligations quoted in (a) above.48

(c) The IMF must exercise “firm surveillance” over the exchange rate policies of members.49

(d) The IMF must adopt “specific principles for the guidance” of all members with respect to their exchange rate policies.50

(e) When requested, each member must consult with the IMF on the member’s exchange rate policies.51

These safeguards do not dispel the impression that, on exchange rates, the Second Amendment regresses a long way toward the sovereignty that members exercised before the IMF came into existence. The contrast between the original Articles and the Second Amendment is less stark if the operation of the par value system is taken into account. In the IMF’s administration of that system it was normal to give the benefit of the doubt to any member that was proposing a change in the par value of its currency. Nevertheless, the necessity for the IMF’s concurrence did have a disciplinary effect that cannot be wholly discounted.

One of the most difficult issues in any regime for exchange rates under international law, and an issue that cannot be avoided, will be the distribution of authority between the administering international organization and the countries subject to that administration. These countries will start always from the position that the exchange rates for currencies have been subject to national jurisdiction in the past. The quid pro quo for the surrender of sovereignty is modest. Under any legal regime, the voice that each country can have in the determination of exchange rates for the cur-

47. Id. Art. IV, § 1.
48. Id. Art. IV, § 3(a).
49. Id. Art. IV, § 3(b).
50. Id.
51. Id.
rencies of other members can be only a small one. The argument for surrender must be cast more in negative terms: avoidance of the disorder that would develop if there were no international pooling of authority. The guerdon is the second best, about which more is said below.

The freedom of members to choose their exchange arrangements and to determine the external value of their currencies is one of the three leading principles of the Second Amendment. The other two principles are that the role of gold in the international monetary system is to be reduced and that the SDR is to become the principal reserve asset in the system. Gold functioned poorly as the primary reserve asset. The Second Amendment has deprived it of this quality within the IMF, for example, by abrogating the official price, by prohibiting transfers of gold between the IMF and members in settlement of obligations, and by proscribing the use of gold as a denominator in terms of which the external value of currencies can be maintained. The Articles also include safeguards against the restoration of gold to anything like its former position in the IMF. Nothing in the Articles strips gold of its character as a reserve asset. Gold continues to be held in large quantities in the reserves of members, although it does not function well as a reserve asset. Monetary authorities are reluctant to make irreversible transfers of their gold because fluctuations in its price might make transferees seem improvident or shortsighted.

What is meant by the objective of making the SDR the principal reserve asset in the international monetary system is not clear. The United States preferred the word “principal” to other suggested adjectives, such as “central,” because “principal” implied more obviously that there would be other reserve assets. The United States was protecting the future legal position of the dollar. Below the surface of the language of the Second Amendment are the conclusions of many members that gold performed badly as the primary reserve asset and that an international monetary system based on a currency will not be optimal because the system will be dependent on the policies of the issuer of the currency.

Notwithstanding the imprecision of the objective that the SDR is to become the principal reserve asset, the objective can have normative effects. The Second Amendment has improved the characteristics of the SDR and has extended its uses. The Articles include provisions under which the IMF can do more along these lines. The IMF has already made some exercise of these powers, but no claim can be made that the SDR is approaching its assigned role in the system. One impediment on its road is

52. The Second Amendment made many changes that cannot be subsumed under these three principles, such as the “modernization” of the IMF’s financial activities and organizational structure, much of which reflected the IMF’s practice as it had developed over the years.
that too few SDRs have been allocated. Allocations have been obstructed by the volume of currencies held in reserves. An implication of the position that the SDR is supposed to reach is that currencies as well as gold will have diminishing roles as reserve assets, but there is no a priori assumption about the relative proportions that SDRs and other assets should have in individual or global reserves. The volume of reserve currency has increased because of the ease with which until lately currency could be borrowed in financial markets to augment reserves. The IMF has no powers to prevent excessive borrowing or excessive lending.\(^5\)

The increase in the number of currencies held in reserves is another monetary development of recent years. The deutschmark, Japanese yen, and Swiss franc have joined the company of the U.S. dollar, although the dollar is still held in much the largest amount.\(^6\) The variability of exchange rates is one explanation of the growth in the number of reserve currencies. Monetary authorities hold more than one reserve currency to reduce risk. Fluctuations also induce monetary authorities to move from one reserve currency to another in the management of their portfolio, with the consequence that these movements through the medium of exchange markets provoke further changes in exchange rates. Shifts from one reserve asset to another have been destabilizing even when there were fewer reserve assets. The IMF does not have clear authority to control the choice members make of currencies to hold in reserves or the decisions of members to switch from one currency to another, notwithstanding the principle of the Second Amendment that the SDR is to be elevated to the position of the principal reserve asset.\(^7\)

The changing fortunes of the U.S. dollar produce a pendulum effect in thinking about the future of the international monetary system. Should the system be based on a strong central currency, or would a multicurrency reserve system be preferable? The dominance of the dollar was formerly based on the power of the U.S. economy and the law governing the par value system. The dominance of the dollar has not ceased with the abrogation of the par value system.

The disturbing effects of switches among reserve currencies through the exchange markets led the IMF to consider the proposal of a Substitution Account.\(^8\) Under this proposal, members would have been able to deposit

\(^5\) Either development, however, may occasion the need for special discussion with a member under the IMF’s procedures for surveillance over exchange rate policies. See Selected Decisions, supra note 2, at 12.

\(^6\) R. Roosa, Reserve Currencies in Transition (1982).

\(^7\) Articles of Agreement, Art. VIII, § 7 provides:

> Each member undertakes to collaborate with the Fund and with other members in order to ensure that the policies of the member with respect to reserve assets shall be consistent with the objectives of promoting better international surveillance of international liquidity and making the special drawing right the principal reserve asset in the international monetary system.

The IMF has made no call for specific action under this provision.

\(^8\) See Gold, Substitution in the International Monetary System, 12 Case W. Res. J. Int’l L. 265 (1980). The multiplicity of reserve assets and the destabilizing effects of shifts among them promoted plans for the combination of assets in a single composite reserve asset
holdings of U.S. dollars in the Account and receive in return claims denominated in the SDR with characteristics and uses that would have enabled depositors to regard their claims as reserve assets. The deposits would not have resulted in a reduction in the depositors' reserves. The Substitution Account would have offered not only an alternative reserve asset, but also an opportunity for members to diversify their reserve assets, in effect, because the SDR is valued according to a basket of five leading currencies. Moreover, the diversification would have been arranged without going through the exchange markets and would have helped to construct an international monetary system based on the SDR instead of the dollar or reserve currencies.

The Substitution Account could have been established under a provision that was written into the Second Amendment as a technique for helping in the evolution of the international monetary system without the necessity for amendment:

If requested, the Fund may decide to perform financial and technical services, including the administration of resources contributed by members, that are consistent with the purposes of the Fund. Operations involved in the performance of such financial services shall not be on the account of the Fund. Services under this subsection shall not impose any obligation on a member without its consent.59

The Substitution Account would have been a structural development in the international monetary system and perhaps the beginning of a change in the international role of the U.S. dollar.

The active pursuit of the project was abandoned in 1980 for a number of reasons, one of which was the unwillingness of the United States to assume some of the financial obligations that would have been essential to make claims on the Account desirable reserve assets. The United States regarded the Account as a development in the international monetary system of benefit to all members of the IMF, so that it was not justifiable to expect the United States to accept special burdens to ensure that interest could be paid at all times and the impairment of capital avoided.

VIII. Present Conditions

Many critics assert that present international monetary arrangements are unsatisfactory. To the protestation that the world has grown accustomed to present arrangements and that their resiliency prevents collapse, the critics reply that the system has collapsed.

Some of the major criticisms of present conditions are summarized below. The leading criticisms relate to experience with exchange rates:

After nine years' experience with a floating exchange rate system, it is hard to deny that the results have been disappointing. Although

---

world trade has not been perceptibly impeded by floating rates and world capital markets have probably been better integrated in the 1970's than before, exchange rates—and also relative prices, i.e., "real" exchange rates—have been highly volatile. At the same time, macroindependence has not followed from floating rates. Finally, there is growing worry that the volatility of floating rates may threaten the viability of the dollar's role as international money, with resulting disruptive effects.60

Members have chosen to apply numerous and diverse exchange arrangements. A well-known counterproposal that was advanced when the results of the Bretton Woods Conference were known was that only the countries that conducted the major proportion of international trade and finance should be required to establish par values, while the currencies of other countries should be allowed to fluctuate in relation to the major currencies.61 Something like the reverse has happened. The major currencies float against each other, but other currencies are pegged in a great variety of ways. The profusion of exchange arrangements and differences in economic performance inspire repeated exhortations in favor of the coordination of national macroeconomic policies among members, so that, in the words of the Articles, "a stable system of exchange rates" can be achieved.62 At the same time, however, the profusion of exchange arrangements and the failure to coordinate macroeconomic policies make it more difficult for the IMF to announce specific principles for the guidance of the exchange rate policies of members. The expectations of the U.S. negotiators of the exchange rate provisions of the Second Amendment that experience would permit the formulation of a growing code of principles has not been realized. Nothing has been added to the three original principles,63 but the IMF repeatedly elaborates the procedures for consultation and surveillance.

The volatility and the misalignment of exchange rates dispel any expectation by the critics that present arrangements are likely to achieve the purposes of the IMF and contribute to world order. The variability of exchange rates has been much greater than under the par value system and has exceeded the degree of variability that the proponents of freedom from fixed rates had predicted.64

60. R. ECKAUS & D. LESSARD, INTERNATIONAL ECONOMIC POLICY—A COLLOQUIUM PHASE I RESEARCH FINDINGS I-24 (1983). “The experience of the last ten years has made most academic supporters of flexible exchange rates sadder but wiser . . . . The current system of flexible exchange rates has not functioned in a manner that even approximates the predictions of previously accepted theory.” Dunn, The Many Disappointments of Flexible Exchange Rates, in ESSAYS IN INTERNATIONAL FINANCE, No. 154, at 1 (1983); see also Lever, Without reform we face all the dangers of disintegration and its attendant consequences, The Guardian, May 24, 1982, at 9 (“The paradox has been that in seeking to gain greater national autonomy the governments of the major economies have in fact reduced it. As in many other fields, the acceptance of collective disciplines does not reduce but protects individual freedom of action.”)


63. SELECTED DECISIONS, supra note 2, at 11-12.

64. A massive number of studies of exchange rates under present conditions has ap-
Floating has not eliminated exchange rate targets, which means that many monetary authorities consider them desirable or essential. The volume of intervention in exchange markets has been substantial. Floating rates have not eliminated, and perhaps have not even reduced, the demand for reserves.

The justification of any form of regulatory jurisdiction must be to deter or minimize disorder. The weaker the authority to require the adjustment of balances of payments, the stronger is the need for resources to finance widespread disequilibria in balances of payments if the collapse of the international financial system, and with it the international monetary system, is to be prevented. In conditions of this character, the financial function of the IMF has become predominant. The volume of its transactions has escalated to absolute amounts and to proportions in relation to quotas that would have seemed inconceivable in earlier years. Far more members make concurrent use of the IMF's resources than ever in the past. In sum, the IMF encourages members to achieve a sustainable balance of payments position more effectively through its financial activities than through the exercise of its regulatory powers.

Certain consequences follow from this process. The ameliorative programs that the IMF supports must be adapted to the circumstances of each member. It is not easy to formulate a code of principles of conditionality for use of the IMF's resources without frustrating the need for individual response to a member's problems. Even so, the IMF's conditionality is frequently criticized as too standardized in its prescriptions. The IMF would find it tactically unwise to emphasize too strongly that it is pragmatic in taking account of the individual circumstances of members.

A regulatory code to which countries subscribe by membership in the IMF gives less cause for discontent. Countries are aware of the obligations of this code that they undertake by becoming members. Conditionality, however, gives scope for charges of oppressive behavior by the IMF in making its resources available, because a code of conditionality is probably not feasible or desirable. Countries are not asked to subscribe to such

---

65. [T]he exchange rate is far too important a price—because of its effects on domestic stability and activity, the balance of payments, and international trade and payments relations—to be treated with "benign neglect" as a "residual outcome" of domestic monetary and other economic policies. The very fact that monetary and other economic policies are part of the forces influencing the foreign exchange markets, makes it unavoidable that those responsible for these policies "have a view" on the exchange rate and take the possible impact of their policies on the exchange rate into account.

O. Emminger, Exchange Rate Policy Reconsidered 13 (Group of Thirty, Occasional Papers No. 10, 1982) (emphasis in original). Emminger asserts, however, that the United States is "a special case" and that free floating, with or without occasional intervention, is the only advisable policy. Id. at 18-20.

66. See infra Appendix B.
a code by becoming members. Any negotiation on the use of the IMF's resources can take on the appearance of an encounter. Finally, regulation through conditionality does not touch members that have no need to use the IMF's resources. Those members tend to be the countries that have leading roles in international trade and payments and that have most influence on the working of the international monetary system.

The critics of present monetary arrangements refer to them as a "non-reform," "non-system," or "codified anarchy," but other observers regard this charge as too extreme. Present arrangements, they point out, are based on a unifying principle that justifies the view that the arrangements constitute a system. The principle is that the orderly underlying conditions that are necessary for financial and economic stability will produce orderly exchange arrangements and a stable system of exchange rates. The markets have developed techniques for protecting traders and investors from the volatility of exchange rates. The allegation of the misalignment of exchange rates is based on current account considerations, but capital movements have an immense impact on exchange rates that could not be countered by intervention because of the cost that would be involved.

Neither fixed exchange rates nor free floating was acceptable to governments when the Second Amendment was negotiated. Either technique would have required too great a surrender of authority over domestic policy and too great a transfer of sovereignty to an international organization. The only practicable solution is the effort to achieve coordinated policies among countries under the supervision of the IMF. The solution may be second best, but it is the only feasible one in present circumstances.

IX. INTERNATIONAL LAW AND IMF

There are at least three ways in which international law has an impact on the international monetary system through the IMF as the central organization of the system. International law affects the day-to-day activities of the IMF, evolution of the IMF under existing powers, and reform by means of amendment of the Articles. Each of these processes will be discussed in turn.

A. Day-to-Day Activities

The IMF has been meticulous in its observance of international law

67. de Vries, Jamaica, or the Non-Reform of the International Monetary System, 54 FOREIGN AFFAIRS 577 (1976).
70. Articles of Agreement, Art. IV, § 4(a).
72. For the best survey of the system from the standpoint of the law, see K. DAM, supra note 18.
The IMF is empowered to interpret its Articles authoritatively, that is to say, with finality and binding effect for members and the IMF, if a question of interpretation of provisions of the Articles arises between any member and the IMF, or between members. This power is an exclusive one, because, when questions within either of these two categories arise, members are precluded from resort to some external tribunal. The power of interpretation relates to "questions," it should be noted, and not to disputes in any narrow sense. This unusual power might have led the IMF to take a cavalier attitude toward legal considerations, but this has not been the result, even though the power has been invoked only on rare occasions and for exceptional reasons. The existence of the power in the background enables the IMF to follow less formal procedures than those required for authoritative interpretations. The IMF takes decisions on legal questions by the same procedures it follows for other decisions. Although most interpretations are made in this way, they are subjected to the same scrutiny

73. J. Gold, The Rule of Law in the International Monetary Fund (IMF Pamphlet Series No. 32, 1980).
74. The IMF can borrow from private entities with the concurrence of the member whose currency the IMF borrows, Articles of Agreement, Art. VII, § 1, but the IMF has not yet exercised this authority.
75. Id. Art. XXIX; J. Gold, Interpretation by the Fund (IMF Pamphlet Series No. 8, 1966). A joint committee of the Boards of Governors of the IMF and the World Bank was appointed to consider certain matters arising from the application of the Palestine Liberation Organization to be accepted as an observer at meetings of the Boards of Governors. The problems that arose related to interpretation and possible amendment of the By-Laws of the Boards and not to interpretation of the Articles. Moreover, the findings of the Committee were advisory only. International Monetary Fund, Summary Proceedings, Thirty-First Annual Meeting 298-384 (1981).

Article VIII of the Agreement between the United Nations and the IMF, which came into force on November 15, 1947, declares that

The General Assembly of the United Nations hereby authorizes the Fund to request advisory opinions of the International Court of Justice on any legal questions arising within the scope of the Fund's activities other than questions relating to the relationship between the Fund and the United Nations or any specialized agency. Whenever the Fund shall request the Court for an advisory opinion, the Fund will inform the Economic and Social Council of the request.

Selected Decisions, supra note 2, at 406. The IMF has never requested an advisory opinion.
and legal discipline as would be applied if the procedures for authoritative interpretation were being followed.

The normal legal work of the IMF has not been on the margin of the IMF's activities. The approach has been creative in applying legal doctrines to problems of the IMF and the international monetary system and in contributing to the development of a coherent body of law within the IMF. The decisions relating to the use of the IMF's resources by its members are one example of bodies of complex rules that the IMF has developed over time for conducting its activities. The unique legal instrument called the stand-by arrangement and its progeny, the extended arrangement, have been invented by the IMF and have become the primary techniques by which the IMF makes its resources available. The two instruments enable other official entities and private entities, such as banks, to associate their loan agreements with the IMF's arrangements and in this way contribute to greater order in international monetary and financial affairs.

The adaptability of the IMF to new problems of the international monetary system as they emerge is demonstrated by the financial policies that have been instituted to deal with the difficulties of servicing sovereign debt. The policy on Enlarged Access to the IMF's resources, changes in the IMF's agreements to borrow, and the new relations with commercial banks are among the examples of adaptation that have equipped the IMF to exercise leadership and to collaborate with financial entities in avoiding the serious disorder that might result from international indebtedness.

**B. Evolution Under Existing Powers**

International law in the everyday activities of the IMF can operate only within the boundaries of the Articles and the rest of the corpus juris of the IMF as already developed under the Articles. The powers of the IMF to modify the existing corpus juris by new decisions, without amendment of the Articles, give the IMF extensive authority to promote the evolution of the international monetary system. The IMF has always had certain powers of variation, as they have been called, but these powers have been expanded by the Second Amendment.

The sweeping revision of the Articles by the Second Amendment was nevertheless modest when compared with the ambitions that were entertained when the Committee of Twenty was established. When work on the Second Amendment was completed, it seemed that further change in the

---

78. J. Gold, Order in International Finance, the Promotion of IMF Stand-by Arrangements, and the Drafting of Private Loan Agreements (IMF Pamphlet Series No. 39, 1982); Gold, Relations between banks' loan agreements and IMF stand-by arrangements, INT'L FIN L. REV., Sept. 1983, at 28-35.
79. J. Gold, supra note 1, at 336-52.
international monetary system would occur, whether or not by later amendments of the Articles. To provide room for evolution, and to avoid the necessity for further amendment if it could be avoided, at least for some time to come, the Articles contain a great many enabling powers, as they came to be called.\textsuperscript{80} In a sense, the negotiating conference of the representatives of member states, meeting in the Committee of Twenty, but not as part of the normal structure of the IMF, has been dissolved in favor of further negotiation, should there be the desire to initiate it, within the permanent framework of the IMF.

Negotiation within the organs of the IMF and evolution under the IMF's enabling powers do not preclude negotiations elsewhere. The Group of Ten, consisting of ten of the leading industrial members of the IMF, which may become the Group of Eleven if the nonmember Switzerland adheres to the IMF's General Arrangements to Borrow, remains in existence and can place on its own agenda any monetary topic that seems to be of sufficient interest. The members of the IMF whose representatives compose the Group of Ten can cast in the IMF a large majority of the weighted voting power of all members. If the group were to undertake frequent examination of the current or potential activities of the IMF, the group could be regarded as a steering committee, although not a committee appointed by any organ of the IMF.

The provisions of the Treaty of Rome\textsuperscript{81} on monetary matters were affected by the assumption that the par value system of the original Articles of the IMF would continue in existence. When the system began to show signs of strain, members of the European Community began to pay more attention to monetary relations among themselves and with countries outside the Community, in particular the United States. The outstanding legal development so far in the regulation of monetary relations within the Community has been the creation of the European Monetary System (EMS), which came into existence on March 13, 1979, under existing powers and without the need for amendment of the Treaty. The object of the EMS is a zone of monetary stability in Europe that would insulate the Community as far as possible from variability in the exchange rates of the currencies of non-Community countries. The EMS was seen to be a step toward European integration. At the heart of the EMS are exchange rate and intervention arrangements that have some affinity with the former par value system of the IMF, but also some basic differences from that system. The European currency unit (ECU), which has some characteristics of a monetary reserve asset, has been created to perform a variety of functions within the EMS and also to serve other purposes within the European Community.

The EMS was established for an initial period of two years with the intention that a final ("institutional") phase would then be installed. A

\textsuperscript{80} For Keynes's views at one time on such powers, see infra Appendix B.
more comprehensive monetary system would be constructed, with a European Fund at its center, and an ECU that was fully a monetary reserve asset. The European Community has decided to prolong the initial phase because the conditions have not been achieved in which the EMS can move to its final phase. The experience of the EMS raises the question whether a zone of true monetary stability can be established for currencies of such importance in an unstable world.

How far the EMS and the ECU could be developed, when the time comes, without amendment of the Treaty of Rome, is debated. According to the Community's Commission, much is possible under article 235 of the Treaty of Rome:

If action by the Community should prove necessary to attain, in the course of the operation of the common market, one of the objectives of the Community and this Treaty has not provided the necessary powers, the Council shall, acting unanimously on a proposal from the Commission and after consulting the Assembly, take the appropriate measures.82

Some members of the Community take a more conservative view of what can be done under article 235. They are more disposed to see proposed changes as political actions that should be submitted to legislatures. These members would rely on article 236 for substantial changes:

The Government of any Member State or the Commission may submit to the Council proposals for the amendment of this Treaty.

If the Council, after consulting the Assembly and, where appropriate, the Commission, delivers an opinion in favour of calling a conference of representatives of the Governments of the Member States, the conference shall be convened by the President of the Council for the purpose of determining by common accord the amendments to be made to this Treaty.

The amendments shall enter into force after being ratified by all the Member States in accordance with their respective constitutional requirements.83

The objectives of monetary stability and movement toward integration were amplified by the conclusions of the Presidency of the European Council on December 4-5, 1978:

It [the EMS] should be seen as a fundamental component of a more comprehensive strategy aimed at lasting growth with stability, a progressive return to full employment, the harmonization of living standards and the lessening of regional disparities in the Community. The European Monetary System will facilitate the convergence of economic development and give fresh impetus to the process of European Union.84

In evaluating the experience of the EMS to mid-1983, the Select Com-

82. Id. art. 235.
83. Id. art. 236.
84. COMMISSION OF THE EUROPEAN COMMUNITIES, Conclusions of the Presidency of the European Council of 4 and 5 December, in EUROPEAN ECONOMY 1 (March 1979).
mittee on the European Communities of the House of Lords in the United Kingdom wrote:

The first point to make . . . is that the EMS has survived. Its survival as a system may have been purchased at the price of its partial failure as a discipline; this is the kind of view expressed in descriptions of the EMS as "a mere crawling peg." But countries have not "left" it as they left the Snake.85

This assessment is reminiscent of the Abbé Sieyès's "J'ai vécu," but more can be claimed for the experience of the EMS. It may provide some guidance for the development of the international monetary system at large.

The work of the Group of Ten and the EMS are not the only examples of change in the international monetary system that is considered or takes place outside the IMF. The broadest powers to develop the system, however, are those of the IMF. What are some of these powers? Exchange arrangements, once again, are crucial. The Articles provide that "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."86 The IMF could give specific content to this obligation by calling on members to follow certain policies. Obligations of collaboration have been applied by the IMF in the past to clarify what it expects of members under such obligations.87 The IMF is directed by the Articles to oversee the compliance of each member with its obligations on exchange arrangements.88 The direction emphasizes a function that the IMF would have even in the absence of the direction.

"To accord with the development of the international monetary system," the IMF "may make provision for general exchange arrangements."89 The first clause, particularly in the use of the word "accord," implies that the IMF is not departing from the general opinion among members on the way in which the international monetary system has developed when the IMF makes provision for general exchange arrangements. The IMF cannot go beyond recommendations notwithstanding the more peremptory appearance of the second of the two clauses quoted above. The function of the IMF is to express to all members, including those that may have doubts, the desirability of a particular kind of exchange arrangement. To make it clear that the IMF's endorsement is a recommendation and not binding on members, the provision that confers on the IMF the power to endorse general exchange arrangements declares that the right of members to choose their exchange arrangements remains unimpaired. It is likely, however, that most members would accept the IMF's recommendation, if they were not already acting in conformity with it, because the IMF is authorized to take a decision recommending a gen-

86. Articles of Agreement, Art IV, § 1.
87. J. Gold, supra note 1, at 390-409.
88. Articles of Agreement, Art IV, § 3(a).
89. Id. Art. IV, § 2(c).
eral exchange arrangement only if the decision is supported by eighty-five percent of the total voting power.

A third power in connection with exchange rates is that the IMF can adopt "specific principles for the guidance of all members" with respect to their exchange policies.\textsuperscript{90}

Lastly, the IMF is authorized to call into operation the provisions on the par value system that are included in a schedule of the Articles.\textsuperscript{91} This system is more flexible than the original par value system and is free from some of the earlier drawbacks. The Articles spell out the circumstances in which the IMF could decide to vivify the par value system:

The Fund may determine, by an eighty-five percent majority of the total voting power, that international economic conditions permit the introduction of a widespread system of exchange arrangements based on stable but adjustable par values. The Fund shall make the determination on the basis of the underlying stability of the world economy, and for this purpose shall take into account price movements and rates of expansion in the economies of members. The determination shall be made in light of the evolution of the international monetary system, with particular reference to sources of liquidity, and, in order to ensure the effective operation of a system of par values, to arrangements under which both members in surplus and members in deficit in their balances of payments take prompt, effective, and symmetrical action to achieve adjustment, as well as to arrangements for intervention and the treatment of imbalances. Upon making such determination, the Fund shall notify members that the provisions of Schedule C apply.\textsuperscript{92}

Some features of this provision deserve comment. First, the circumstances in which the IMF could act under the provision can be considered an ideal to which members have subscribed, notwithstanding the resistance of the United States to the expression of any bias in favor of a par value system. The provision was undoubtedly part of the compromise with France in contemplating the possibility of an eventual return to fixed rates. Another explanation may be that the United States expected that this particular ideal would not be attained, as is often the fate of ideal solutions. Second, some of the conditions that must be satisfied, such as those relating to intervention and the treatment of imbalances, imply agreements among members. The terms of these agreements are not prescribed by the Second Amendment,\textsuperscript{93} although the IMF could take initiatives to encourage members to reach the necessary agreements and could assist in negotiating the terms.

Lastly, it will have been noted that two provisions that enable the IMF

\begin{itemize}
\item[] 90. \textit{Id.} Art. IV, § 3(b).
\item[] 91. \textit{Id.} Art. IV, § 4; \textit{id.} Sched. C.
\item[] 92. \textit{Id.} Art. IV, § 4.
\item[] 93. \textit{On the curious legal compromise by which Article VIII, § 4 on official convertibility was retained but deprived of practical application, see J. Gold, \textit{Use, Conversion, and Exchange of Currency Under the Second Amendment of the Fund's Articles} 26-32 (IMF Pamphlet Series No. 23, 1978).}
\end{itemize}
to support certain kinds of exchange arrangement, although not to force them on members, permit the IMF to act only with a majority of eighty-five percent of the total voting power of members. The decisions for which this majority is necessary are the recommendation of general exchange arrangements and the activation of the par value system. Although there is no obligation to apply a general exchange arrangement that the IMF has recommended or to establish a par value if the par value system has been called into effect, a member may be too embarrassed to exercise its independence. The other two powers of the IMF that have been mentioned—the powers to give content to the duty of collaboration and to adopt specific principles of guidance on exchange rate policies—can be exercised by decisions taken with a majority of the votes cast.

The reduction in the role of gold in the international monetary system is a principle of the Second Amendment because of opposition to gold as the primary reserve asset. The price of gold as a commodity had disturbed the functioning of gold as a reserve asset and as the common denominator of the par value system. A prominent U.S. expert once described the London gold market as "a time bomb resting at the very foundation of the Bretton Woods system." Moreover, gold could not be relied on to supplement monetary reserves. The volume of production and the disposition of newly produced gold were governed by considerations of profit and not by the needs of the international monetary system.

The Second Amendment has deprived gold of its former official price and prevented the emergence of a new official price, forbidden the maintenance of the external value of currencies in terms of gold, proscribed the use of gold as the common denominator if a par value system were restored, abrogated the definition of the SDR by reference to gold, forbidden the discharge of obligations between the IMF and members with gold, and required the IMF to dispose of one-third of its gold holdings. The Second Amendment has been effective in bringing about a radical, and not a gradual, reduction in the role of gold in the IMF itself.

94. C. COOMBS, THE ARENA OF INTERNATIONAL FINANCE 68 (1976) (recounting the vicissitudes to which the international monetary system was subjected by gold); see Gold, supra note 53.
96. Id. Art. IV, § 2(b).
98. Id. Art. XV, § 2.
This result does not eliminate gold from monetary reserves or stifle the acceptability of gold to monetary authorities. Freeing the price of gold from all restraint and the consequential fluctuations in price, however, have deterred monetary authorities from disposing of their gold, so that it is now inactive to a large extent as a monetary reserve asset. If use in support of a currency is part of the definition of a monetary reserve asset, gold scarcely meets the test.

Some well-known economists and some other public figures urge the restoration of gold to a more prominent, and even a central, role in the international monetary system. This support for gold, which sometimes becomes a campaign, is an expression of dissatisfaction with the present state of the system. The Congress of the United States appointed a Gold Commission to study and make recommendations on the policy that the U.S. Government should follow on the domestic and the international role of gold. The Commission reported in March 1982 and recommended against the restoration of a par value system based on gold as the common denominator, but it also recommended that the IMF should not make further dispositions of its gold in case such a system were restored.\(^{101}\)

The Second Amendment has improved the characteristics and extended the uses that can be made of the SDR. The IMF is authorized to carry the process further so that the SDR can become the principal reserve asset in the international monetary system. The IMF has taken a number of decisions under this authority, but so far no action has been taken that can be considered a structural development in the functioning of the SDR in the international monetary system. A suggestion that might have had that effect was made by a former Managing Director of the IMF, who proposed that members should hold SDRs in proportions to other reserve assets that would be fixed from time to time, so that the IMF could control the total volume of official liquidity, but nothing has come of this proposal so far.\(^{102}\) Nor has anything happened so far to give effect to proposals that SDRs as reserve assets and SDR-denominated claims and liabilities that are not SDRs proper should be linked in some way, so as to mitigate the drawback that the SDR proper is exclusively a reserve asset and cannot be held by private entities.\(^{103}\) The proponents of the ideas for linking the SDR and its simulacrum allege that broader uses would be made of both and that spread of the market-SDR would help the SDR proper to become the principal reserve asset in the international monetary system.\(^{104}\)

---


\(^{102}\) Witteveen, 44 IMF Survey 313, 315 (1975). For a criticism of the idea, see J. Murphy, The International Monetary System: Beyond the First Stage of Reform 190-94 (1979).

\(^{103}\) Articles of Agreement, Art. XVII, § 3(i).

\(^{104}\) See International Money and Credit: The Policy Roles (G. von Furstenberg ed. 1953); Coats, The SDR as a Means of Payment, 29 IMF Staff Papers 422
ECU proper by promoting the use of the market-ECU. Members of the European Community have done much to encourage the spread of the market-ECU because the ECU symbolizes the hope of closer integration within the Community.

C. Amendment

If there were to be agreement on reform of the international monetary system, that is to say, change that could not be put into effect by decisions taken in the course of what have been called above the everyday activities of the IMF, or by the exercise of its so-called enabling powers, or by agreements made outside the IMF, there would remain amendment of the Articles. So far there have been two Amendments: the First was primarily for the purpose of creating the SDR, and the Second was designed to take account of the collapse of the par value system and to "modernize" the IMF. Modernization meant, to a large extent, incorporation within the Articles of many of the policies and practices that had been developed in the day-to-day activities of the IMF. The effect of this process might be to reduce the flexibility that had made it possible for the IMF to develop the policies and practices.

Proposed amendments take effect if accepted by three-fifths of the membership and by members having eighty-five percent of the total voting power. The practical consequences of this requirement are discussed below.

X. A NEW BRETON WOODS?

On a few occasions in the recent past, a prominent spokesman for an industrial country, disgruntled by international monetary vicissitudes, has suggested that a new Bretton Woods Conference might be convened to consider reform of the international monetary system. Developing countries have made this appeal more frequently. The Intergovernmental Group of Twenty-Four on International Monetary Affairs (the Group of Twenty-Four), composed of the representatives of developing countries, issued a communiqué in April 1983 in which the following passage appeared:

Ministers . . . underscored the fact that the current monetary and financial system suffers from many shortcomings and inequities, notably, the inadequate share of developing countries in decision making, wide and erratic fluctuations in exchange rates, lack of symmetry in surveillance, excessive dependence on a few key reserve currencies, failure to increase international liquidity in line with the growth of world trade, and increasing inadequacies in the resources of the international financial institutions. In the light of these considerations,

---

105. Articles of Agreement, Art. XXVIII. For the amendment of three "safeguarded" provisions, acceptance by all members is required.
they were of the view that an international conference on money and finance should be convened to find appropriate solutions to these problems. 106

The few spokesmen for industrial countries have explained, after their initial statements, that they really had intended a conference once sufficient progress had been made toward common understandings. This procedure was followed for the original Articles. The Bretton Woods Conference was preceded by more than two years of discussion among officials and other experts. A diplomatic conference was not summoned for the purpose of reaching agreement on the First and Second Amendments. The First Amendment was preceded by a long period of study and negotiation in the Group of Ten, the Second Amendment was preceded by discussions in the ad hoc Committee of Twenty and by its successor, the Interim Committee of the Board of Governors on the International Monetary System. Most of the topics mentioned in the communiqué of the Group of Twenty-Four could be the subject of decisions by organs of the IMF without the need for amendment of the Articles.

The topics mentioned in the communiqué as an agenda for reform of the international monetary system are clearly within the scope of the system. Some calls for a new Bretton Woods Conference propose to include within the agenda subjects that do not fall within the boundaries of the international monetary system, even though little has been done to define that concept with precision. Proposals of an expansive agenda follow the precedent of the terms of reference of the Committee of Twenty. The resolution of the Board of Governors establishing the Committee directed it to advise and report on all aspects of reform of the international monetary system, including proposals for amendments of the Articles. The resolution then continued:

In considering and reporting on the matters covered by (a) above, the Committee shall give full attention to the interrelation between these matters and existing or prospective arrangements among countries, including those that involve international trade, the flow of capital, investment, or development assistance, that could affect attainment of the purposes of the Fund under the present or amended Articles. 107

As is evident from the Outline of Reform, the Committee of Twenty concentrated most of its attention on the international monetary system and not on related matters.

The interrelationship among the elements in the terms of reference of the Committee of Twenty are undeniable. The terms of reference implied a negotiation more in the nature of an economic than a monetary conference. The difficulties of an economic conference might be even more profound than those that arose in the negotiation of the law of the sea and that still obstruct consensus after the drafting of the treaty.

XI. PROPOSALS FOR CHANGE

A weakness of the present time is that there are no political economists with the prestige and influence of Keynes and White who could promote the common understandings that would be the necessary precondition of an international monetary conference. The task is far more difficult now because of the distribution of power throughout the world. It becomes fanciful to think back to the time when the task of creating an international monetary system could have been initiated and carried forward almost to completion by the representatives of only two countries. If there are no leaders of the caliber of Keynes and White, there are nevertheless abundant proposals for change. Most of the proposals could be made effective under the existing powers of the IMF or by means of agreements among groups of countries, which could be administered by the IMF. Another characteristic of the proposals is that, for the most part, they have been made by persons who are not responsible for national policy.

Little, if any, support is expressed for a worldwide return to fixed rates of exchange on the model of the former par value system or the par value system in the present Articles or some adaptation of either system. There is support, however, and probably growing support, for target rates or zones and intervention policies to ensure that exchange rates move toward and not away from the targets or zones, and for administration of such a mechanism by the IMF. Some of these proposals are more concerned with the misalignment than with the volatility of exchange rates. The variations on the theme of target rates or zones are manifold.

The behavior of exchange rates has inspired repeated speeches and other declarations in favor of official intervention in the exchange markets. The main purpose of the campaign has been to get the United States to join in a concerted policy of intervention. The United States has subscribed on many occasions to a policy of intervention to prevent disorderly exchange markets, but the tendency has been to give a narrow interpretation to disorder and, therefore, to follow a practice of minimal intervention. The hubbub in favor of a more active policy of intervention has subsided to a considerable extent as a result of the largely negative conclusions of the Jurgensen Report of March 1983.

Intervention need not imply an agreement to stabilize exchange rates among currencies at particular relationships, but an agreement for stable

---

relationships would require intervention, as is demonstrated by the EMS. Proposals have been made that such an agreement should be entered into by the United States, the Federal Republic of Germany, and Japan, or by the five members that issue the currencies in the basket that determines the value of the SDR. The parties to the latter agreement would include the United Kingdom and France as well as the other three countries.111

A return to fixed rates, whether among three or five leading currencies or among a wider number, and whether under the par value system that is included in the Articles or under some different arrangement, is improbable in the foreseeable future. For a return to fixed rates, it would be necessary to assume that a common rate of inflation would prevail and that currencies would be less vulnerable to capital flows than in the past. Members participating in an agreement would have to be willing to subordinate monetary policy to maintenance of the fixed rates. A collective agreement on flexibility in changing fixed exchange rates, which seems to be the way in which the EMS has developed, would raise the objection that fixed rates are not fixed if they are subject to frequent change. Furthermore, it might be necessary to find a country that would be willing to be at the center of the system in the role that the United States performed under the par value system. The United States has objected that this role was highly disadvantageous to it and is not likely to undertake it again with a light heart. The United States might demand safeguards, which would mean that its role would be different from the one it performed in the past. The possibility that the issuer of another currency might take on the role of the issuer of the central (or pivot) currency, or be accepted in that role, is even more remote.

The argument has been advanced by one author that the world economy is inherently unsymmetrical in its functioning and that the legal endorsement of asymmetry is impracticable. He cites the criticism by other countries that the central role of the U.S. dollar was favorable to the United States as an example of the dislike for asymmetry. The conclusion he draws from this argument is that reform by treaty should be avoided and that the evolution of practices would be preferable.112 U.S. officials, in defending the present Article IV, explained that general principles would emerge under the procedures of the Second Amendment. Increasingly detailed decisions on procedures for surveillance have been developed, but not a body of principles.

After the Committee of Twenty was dissolved, the Board of Governors resolved, on the basis of the Committee's Outline of Reform, that: "the Fund shall seek to gain further experience in the use of the objective indicators, including reserve indicators, on an experimental basis, as an aid in assessing the need for adjustment, but shall not use such indicators to

111. House of Commons Committee Second Report, supra note 108, at xli; Towards a New Bretton Woods, supra note 109, at 120.
112. Cooper, Prolegomena to the choice of an international monetary system, 29 Int'l Org. 95-96 (1975).
establish any presumptive or automatic application of pressures." 113 This direction dealt with the need for adjustment, which does not necessarily, but may, require a change in the external value of a currency. The Fund has not taken any decision on objective indicators. The EMS, however, includes a “divergence indicator” based on the deviation of the exchange rates for a currency from its central rate in terms of the ECU.

The multiplicity of reserve assets, among which reserve currencies represent the largest active component, and the destabilizing effects of movements from one currency to another in the management of reserve portfolios keep the idea of a Substitution Account alive, although only barely. 114 For the same reasons, numerous proposals are made to strengthen the SDR so that it could become the principal reserve asset in the international monetary system. 115 An attraction of the SDR is that it is not a national asset, although increasingly its characteristics resemble those of currencies in contrast to gold as the original model. The value of the SDR is affected by national policies, because the method of valuing the SDR is based on a basket of currencies, but the composition of the basket is determined by international considerations. 116

The IMF has no regulatory authority over movements of capital. To control or not control them is a decision for the monetary authorities of each member. Freedom for capital movements has had both beneficial and detrimental consequences. Harmful consequences have followed from the practice of many countries in regulating the transactions of banks with nonresidents more lightly than transactions with residents, and from the practice of reduced taxation on foreign-owned banks. Branches, subsidiaries, and affiliates of foreign banks tend to become established in countries in which these practices are followed.

113. SELECTED DECISIONS, supra note 2, at 354.
114. H. WITTEVEEN, supra note 109, at 15-16; TOWARDS A NEW BRETON WOODS, supra note 109, at 132; GROUP OF THIRTY, RESERVE ASSETS AND A SUBSTITUTION ACCOUNT: TOWARDS A LESS UNSTABLE INTERNATIONAL MONETARY SYSTEM (1980). The report of the Group of Thirty stated in part:

It is clear, in the opinion of the Study Group, that there is a serious reserve asset problem in today’s international monetary arrangements. In particular, it is unlikely that the dollar can continue indefinitely to provide some 80 percent of the world’s foreign exchange reserves. It may be felt that it is inappropriate for any national currency to play this central role and that efforts should be made over the longer term to establish the primacy of an international reserve asset; or it may be felt that there is a disequilibrium in the existing pattern of reserve holdings which can only be satisfied over time with the growth of other national currencies as reserve assets; or, even if neither of these long-run aims is subscribed to, it may be felt that the present situation leads to avoidable instability in foreign exchange markets.

Id. at 3.

115. These proposals include a change in the structure of the IMF that, in effect, would merge the General Department and the Special Drawing Rights Department, eliminate the holding of currencies, and construct the IMF on the basis of the SDR only. Amendment of the Articles would be necessary. J. POLAK, THOUGHTS ON AN INTERNATIONAL MONETARY FUND BASED FULLY ON THE SDR (IMF Pamphlet Series No. 28, 1979).

The United States, concerned about the detrimental consequences of such practices, has proposed an agreement with other countries under which Eurobanks would be subject to controls and regulations on their activities. The parties to an agreement would impose the same reserve requirements on off-shore as on domestic banking operations. The U.S. initiative has not led to agreement. In the absence of agreement, the United States is now attracting Eurocurrency business by authorizing international banking facilities on U.S. territory. Under these facilities, certain transactions with nonresidents are exempted from the reserve requirements and regulations on interest rates to which the transactions formerly were subject.

Recommendations by international bodies are made on aspects of the supervision of banking by the European Community's Groupe de Contact of supervisory authorities and by the Committee on Banking Regulations and Supervisory Practices, meeting under the auspices of the Bank for International Settlements and composed of representatives of the central banks of the Group of Ten and Switzerland.

The problems that arise as a result of the activities of banks that operate internationally have focused increasing attention on the need for understandings on responsibility for the liquidity and solvency of these banks that go beyond the limited recommendations of the two bodies mentioned above:

Most large banks have substantial relationships with scores of countries. Obviously, the ideal LLR [lender of last resort] for an international bank would be an institution that represents the world community. It is equally obvious that such an institution will be a long time coming. Cooperation and consultation among national LLRs may compensate to some extent for the lack of an appropriate international institution, but such arrangements are cumbersome to negotiate and may be unreliable in a crisis.

The indebtedness already contracted by sovereign borrowers, with national banks and in the Euromarkets, has created a threat to the financial and monetary systems because of the difficulty of servicing and repaying the debt. To deal with accumulated debt, and the threat it poses, a flood of ideas has gushed forth, and the flow has not ceased. A number of the proposals would require new legal measures, particularly when the proposals involve the assumption of some form of official responsibility for

---

117. For a discussion of some of the difficulties, see House of Commons Committee Second Report, supra note 108, at lxxi.
120. R. DALE, BANK SUPERVISION AROUND THE WORLD 5-7 (1982).
the indebtedness. None of these proposals has made progress so far in the corridors of government. The necessity for new legal authority is a barrier, even if there were no other objections, because of resistance to "bailing out" commercial banks. The difficulties of the debtors are taken to be evidence of the imprudence of the banks. It is argued that the banks should not be allowed to transfer their risks to the public and should not be encouraged to repeat their imprudence.

The Report of the U.S. Gold Commission has not silenced those critics of present national and international economic policy who advocate the solution of return to a monetary system based in some way on gold. It is difficult to conceive of such a reform of international monetary relations that would not involve amendment of the Articles.

Many more proposals for change have been advanced, mostly by economists in their academic publications, in official hearings, and in the press. The proposals referred to briefly above fall into a few broad categories and seek:

(1) a degree of stability in exchange rates;
(2) control of the volume and composition of official liquidity;
(3) improvement in the status of the SDR; and
(4) control of transborder credit.

To these categories can be added another:

(5) strengthening the IMF.

The categories are not wholly discrete, which is another way of saying that they are related to each other in an international monetary system.

XII. DIFFICULTIES OF CHANGE

An economist has written:

America emerged from both world wars as the dominant power militarily, industrially, and financially, and the dollar became the global currency. It is a fact of historical tradition that the top currency is provided by the top power. Money is a political phenomenon that reflects—and partly conditions—the political configuration of the world. My second observation is thus: The top political power has usually had a commanding role in determining or vetoing the nature of the international monetary system.

It should have become apparent from this article that the legal history of the international monetary system since the negotiation of the original Articles supports the view that the system has been fashioned, developed, and changed primarily under the influence of the United States. The United States was the advocate of, and the chief influence on, the original Articles; actively supported the GAB, which was thought to be primarily for the benefit of the United States; pressed for the creation of the SDR; was the immediate actor in bringing about the collapse of the par value system;

insisted on the legalization of freedom to choose exchange arrangements and on the decline in the position of gold in the international monetary system; and refused to accept obligations that might have made it possible to establish a Substitution Account. The prospect of worldwide change in the system or in the international law governing it is negligible or nonexistent unless the United States sponsors or supports a change. This truism applies to all three manifestations of international law that have been mentioned above—in the everyday activities of the IMF, evolution under present powers, and amendment of the Articles.

It is incontestable that the United States should act only when it sees that its own interests will be promoted, but its own interests can correspond with those of the world at large. Enlightened self-interest is not the same as the automatic equivalence that was once claimed between the interests of General Motors and those of the country.

The United States is not likely to rush to judgment about its self-interest. A former Secretary of the U.S. Treasury has explained that the United States can afford to wait:

Generally we tend to do the right things only in extremis . . . only when the sight of the gallows becomes so clear that it finally clarifies our minds. Since we are a rich country, we can muddle along, and muddle along we do most of the time. I suppose one of the comforting thoughts, in conclusion, is that as you look at other countries, you don’t really see too many models that are any better. Where they are better, it’s sometimes because the country is smaller, and the problems are not quite as complex as they are in our case.124

When the United States makes a proposal for change, it does not follow that other members will conclude that it serves their interests as well. The experience with the proposed Substitution Account is an example of the disagreement that can arise about whose interest would be promoted. Principles of uniformity and symmetry come to the surface whenever efforts are made to develop the international monetary system. Members prefer uniformity—sameness—in benefits and burdens. If it is unrealistic to insist on uniformity because it is inconsistent with a world in which there are different classes, the principle to which members adhere is symmetry—comparability in benefits and burdens. The proposal of a Substitution Account was favored by the Carter Administration and actively supported by the Under Secretary of the U.S. Treasury for Monetary Affairs. The reaction of at least some members to the proposal has been described by Henry C. Wallich, a distinguished member of the Governors of the Federal Reserve System of the United States:

Whether the project will be reactivated is uncertain at this time. But if progress is to be made, it would have to rest on a more complete agreement concerning the purposes of a substitution account. There has always been some ambivalence between two views of the account:

---

as a long-term structural improvement in the world monetary system, and as a conceivable means for bailing out the dollar from possible short-run difficulties. In the American way of thinking, the support of the proposal has always rested on its long-term rôle. It is not well designed to serve the purpose of dollar support in the short run, even if that purpose were regarded as desirable.\footnote{125. Address by Henry C. Wallich to a meeting of the Institut für Wirtschaftsforschung, at Hamburg (June 12, 1980).}

An irony of the failure of the project was that it might have helped to diminish the function of the U.S. dollar as the main reserve currency. As the international monetary system developed symptoms of instability, members asserted increasingly that the United States had a favored position and that the United States was able to pursue its policies and neglect the interests of the system as a whole. The United States, however, emphasized the disadvantages that were forced upon it because of the central role of the dollar. That view seems to have been concurred in at one time by other countries that resisted the status of reserve currencies for their currencies. The resistance by these countries has diminished, and has even been replaced by encouragement, perhaps because of the benefits resulting from the accumulation of the currencies by oil-exporting countries.

Sometimes, a proposal arouses political as well as economic ambitions, with the result that negotiations can become prolonged and complicated. When the United States has sought a structural development in the system, European members, usually led by France, have seen an opportunity to moderate the influence of the United States. The GAB was negotiated on the assumption that the United States would be the main and perhaps the only beneficiary. This assumption explains why the participants in the GAB are bound only to consider whether they are willing to lend when loans are requested. The participants are not obliged to lend when the Managing Director proposes to make a call on them.\footnote{126. \textit{Selected Decisions}, \textit{supra} note 2, at 119-20.} The participants feared that if they undertook to lend, the United States might be able to arrange for the use of the IMF’s resources without meeting the IMF’s standards of conditionality.

For the same reason, the participants established a procedure among themselves for deciding whether to agree when the Managing Director proposes that they lend. In this procedure, the participant that was seeking to use the IMF’s resources, which were to be supplemented for the purpose by the proposed loans to the IMF, would not be able to cast its votes. A member that seeks a stand-by arrangement or a transaction is not debarred from having its votes cast when the IMF decides whether to comply with the member’s request.

In the negotiation of the First Amendment, a strenuous effort was made to rescind the IMF’s power of authoritative interpretation of the Articles. The objection was advanced that weighted voting power was inappropriate when interpretation was the issue, but the objection took account of the
large proportion of the total voting power of all members that the United States could cast. The outcome was a compromise that appears to be unworkable.

The experience of the Eighth Quota Review\textsuperscript{127} shows that change may be difficult even when the Administration in the United States concludes that a particular development in international monetary affairs that has the support of other members is desirable. If legislation is necessary, the project may be jeopardized by the diversity of interests, including domestic political interests, among members of the U.S. Congress. The legislation was obtained on this occasion by including provisions in it to tighten the control of Congress over the Administration in a wide range of the IMF's activities.\textsuperscript{128} Some of the instructions issued by Congress on the positions that the Administration can or must take in the IMF are of dubious relevance to the Articles of the IMF, and are not wholly consistent with each other. The instructions are not directed toward the IMF itself and, therefore, were not the subject of international controversy or legal objection.

The contretemps has been described in the following vigorous paragraphs in a speech delivered by Dr. Wallich on December 29, 1983:

On the other hand, the history of the passage of this legislation through the Congress is bound to create deep concern for those interested in the international financial role of the United States. It is difficult to read this episode in any sense other than indicating a reduced willingness of the American public to take an internationalist position in financial and economic affairs. The legislation passed only with great efforts, many compromises, and quite narrowly. It was loaded down with a large number of provisions reflecting both domestic and international political concerns. Provisions that might have affected the smooth functioning of the international financial institutions were barely avoided. Why, one must ask, is this happening at a time when the United States economy is becoming increasingly open and interdependent with the rest of the world? We were more internationally oriented when our foreign sector was of the order of two to three percent of GNP, as in the period following the creation of the Bretton Woods institutions, than we are now when it has passed 10 percent.

Perhaps these difficulties could have been reduced had the legislation been presented in a different context and argued on less dramatic grounds. This eighth IMF quota increase occurred at a time of difficulties for developing countries and potentially for their creditors. Perhaps inevitably this made crisis management the primary argument for the U.S. contribution. But, at the same time, this was a routine updating of the resources of the International Monetary Fund, such as had occurred at regular five-year intervals, with a couple of exceptions, since the founding of the institution. For the United States to remain a member in good standing in an institution which it had itself created and in which it still plays a leading role would seem to be a persuasive argument. That the legislation preserved this U.S.

\textsuperscript{127} Id. at 376-85.
role transcends in importance any other aspects. 129

A leading role in the IMF for the United States may be preserved in the sense that the quota of the United States has been increased, and approximately the same proportion of its voting power has been maintained. It is too early to conclude that the legislation has limited the power of the U.S. Administration to take progressive initiatives in the IMF or to support the initiatives of others. The consequences of a hamstrung Administration would be even more regrettable if the attitude of Congress that found expression in the new legislation indicates a hostility to international monetary cooperation or to international organization in general. 130

Keynes was nervous about close control of the IMF by the U.S. Congress, at least in the everyday activities of the IMF. In applauding the creation of the U.S. National Advisory Council by the original Bretton Woods Agreements Act, he wrote:

The Council has to report to Congress once a year and must keep itself reasonably free from public criticism. But the idea and the hope is that a considerable time can be allowed to pass before it has to go to Congress again for any additional powers or additional finance. For the first time the Administration possesses an organ for international collaboration on economic and financial affairs which is relatively independent of Congress. That, for all of us, is a step forward, the importance of which is not to be under-estimated. 131

Agreement on change has become more difficult to achieve not only because of the different interests of members but also because of the greater dispersion of economic or financial power throughout the world. If change requires amendment of the Articles, acceptance by high proportions of members and voting power are required. The proportions were always high, but the necessary proportion of total voting power was made even higher by the Second Amendment, which increased the proportion from eighty percent to eighty-five percent. A motive for this change was to allow the United States to consent to increases in its quota under which its proportion of voting power would fall below twenty percent without loss of a veto over proposed amendments.

The effect of the acceptances required for amendments is that many groups of members can prevent proposals from coming into force. The United States remains the only member that can exercise a veto without the support of other members. The tendency of groups of other members to coalesce in reaching positions has grown over the years. Numerous combinations have come into existence. Developing countries, oil-exporting countries, the Group of Ten, members of the European Community, the five members whose currencies compose the SDR basket, and the seven members that attend Summit Meetings do not exhaust the combina-

131. 26 Keynes, supra note 30, at 233 (footnote omitted).
tions. A complex interweaving of interests means that numerous and sometimes labyrinthine compromises are a practical necessity.

It is unlikely that an amendment to give effect to a single idea, however desirable it may be in the interest of all members, can be negotiated without provoking further proposals by some members. The First Amendment can be cited to rebut this presumption. The creation of the SDR was beneficial to all members, but developing members saw less benefit to them in the project. Allocations would be made at the same rate in proportion to quotas, and the quotas of developing members were modest or tiny. These members were more disposed to negotiate benefits in relation to the use of the IMF's resources. Developing members made proposals for this purpose.

The effect of rejection of these proposals was to create a determination on the part of developing members that the experience would not be repeated. They formed the Group of Twenty-Four in order to reach unified positions. Developed countries were shamefaced about the high-handed treatment that they had given developing countries and regretful that political animosity had been provoked. The Outline of Reform of the Committee of Twenty shows a different, and remarkable, change of attitude to the interests of developing members. The new attitude was apparent in the negotiation and drafting of the Second Amendment. Developing members are not powerful enough to ensure an automatic reaction in their favor, but they will be aware of their strategic strength in the negotiation of any further amendments of the Articles.

The need for compromise as a complication of, and even a deterrent to, proposals for change is not confined to amendment. A similar difficulty faces proposals for evolution under the powers conferred on the IMF by the Second Amendment. The original Articles were drafted on the assumption that a charter had been completed for the international monetary system, and great changes in it were not foreseen as likely. This assumption may be one reason why the requirements for amendment were so severe. The spirit in which the Articles were negotiated was that the everyday operation of the IMF should be as efficient as possible. This spirit meant that only for a few decisions of the IMF would a special majority be necessary. The basic majority of the votes cast would suffice for the adoption of most decisions, because that majority would be least likely to permit the obstruction of proposals for action by the IMF. The United States took the lead in advocating minimal reliance on special majorities, perhaps in the confidence that its predominant power in the world would be sufficient assurance of respect for its views.

A different spirit among some other members appeared in the negotiation of the First Amendment. European members were fearful that excessive allocations of SDRs would be made and that European members would be designated by the IMF as the recipients of SDRs when transfers of them were made by other members. This fear was reminiscent of White's objection to the creation of bancor as proposed by Keynes. The
six members of the European Community at that time had achieved so strong a balance of payments and reserve position that the IMF had sold a greater total of their currencies than of U.S. dollars in the transactions of the IMF. A majority of eighty-five percent of the total voting power would give these members a veto over proposals to allocate SDRs and some other crucial decisions in the operation of the new scheme. The novelty of that scheme was a strong argument in favor of so high a majority, and eighty-five percent became the rule not only for a number of decisions relating to SDRs, but also for other decisions affecting official liquidity.

The development that had occurred on the occasion of the First Amendment was carried to an extreme length by the Second Amendment. A vast increase took place in the number of decisions for which a special majority becomes necessary. Many motives existed for the choice of the categories of decisions for which special majorities are now required. Two explanations of a general character can be adduced. First, many of the powers that can be exercised by decisions taken with a special majority involve an evolutionary process. Some of the powers are substitutes for the agreement that could not be reached on proposals advanced in the negotiation of the Amendment. Second, special majorities recognize the need for compromises on evolution of the international monetary system in modern conditions.

When the Second Amendment was drafted, the opportunity was taken to reduce the number of different special majorities to two: eighty-five percent and seventy percent of the total voting power. The assignment of the higher or the lower majority to a category of decisions was not made with total logic. A distinction between decisions of evolutionary impact and operational decisions was observed as a rough criterion.

The higher majority gives an obvious veto to many groups of members, including developing countries, but the lower majority also gives developing countries a veto. A proposed decision, therefore, may provoke proposals for compensating benefits. Once again, the proposal of a Substitution Account provides an example: "[T]he developing countries announced potential demands as a condition for agreeing to the use of the IMF's gold to bridge at least in part any potential interest and capital deficit in the account." From time to time, some members have expressed dissatisfaction with a majority that gives a single member a veto. The United States has a veto when eighty-five percent of the total voting power is required for a decision. The United States, speaking through its National Advisory Council on International Monetary and Financial Policies, has explained its attitude to special majorities. This expression of viewpoint is of particular interest in relation to exchange rates:

The second, and closely related point, is that the system of voting majorities in the Fund will be revised considerably under the

133. Address by Henry C. Wallich, supra note 125.
amended Articles. Throughout the negotiations, the United States has taken a supportive but very cautious approach in the effort to make the Articles more adaptable to changing future needs. Thus a number of decisions which either are not authorized under the present Articles, or are authorized to be taken by lower majorities, have been made subject to a majority of eighty-five percent of the total voting power. This assures the United States and other countries that important changes of policy in the Fund will not be implemented unless they command wide support; and, in particular, the United States will be assured that it will have the ability to forestall any important policy decision which it considers to be against the interests of the United States or of the system as a whole.\textsuperscript{134}

These new exchange rate provisions are of critical importance both for the system as a whole and for the United States. They focus on the essential need to achieve underlying stability in economic affairs if exchange stability is to be achieved. They provide a flexible framework for the evolution of exchange arrangements consistent with this broad focus. And they help to ensure that the United States is not again forced into the position of maintaining a value for its currency that is out of line with underlying competitive realities and that costs the United States jobs and growth due to loss of exports, increased imports and a shift of production facilities overseas. Under the new provisions, the United States will have a controlling voice in the future adoption of general exchange arrangements for the system as a whole; and will have full freedom in the selection of exchange arrangements to be applied by the United States, regardless of the general arrangements adopted, so long as it meets its general IMF obligations.\textsuperscript{135}

\section*{XIII. A Concluding Comment}

Pessimistic views have been expressed on the possibilities for a firmer and broader rule of law on exchange rates and on other aspects of international monetary relations. Some views have been based on the hypothesis that such a development is necessary but insufficient. The interdependence of countries makes it impossible for them to pursue independent policies in either external or domestic monetary matters. Countries are affected by both the external and the domestic policies of other countries. International monetary reform alone would not be successful, because it would not touch domestic policies.

Given the non-independence of nations' domestic as well as external policies, restriction of international cooperation to the area of exchange rates and external reserve positions is bound to be analytically unsound. The difficulties can be especially great if an attempt is made

\textsuperscript{134} Special Report to the President and to the Congress on Amendment of the Articles of Agreement of the International Monetary Fund and on an Increase in Quotas in the International Monetary Fund 20 (1976).

\textsuperscript{135} Id. at 23.
to impose a tightly drafted supranational rule of law pertaining exclusively to the international monetary system.

Should national governments be urged to develop such a comprehensive rule of law for the world economy and to subject their domestic policy actions to corresponding enforcement responsibilities of supranational institutions? A sufficient reason for rejecting that recommendation is its obvious impracticality. Despite the economic interdependence that undermines their sovereignty de facto, national governments are politically unable to take major steps to cede a substantial part of their sovereignty de jure.136

The conclusion of the author of this statement rests on the assumption that rules of law must be rigid or mechanistic in their operation. His preference is for the development of cooperative and discretionary decision-making about national macroeconomic policies, accompanied by a corresponding evolution of national and supranational institutions to promote the interdependence on which this preference is based.

It may be that in international economic relations all that can be hoped for in the coming years is "soft law" and more elaborate procedures for consultation,137 and that firm law will be the work of generations.138 Another economist, Alan Greenspan, has said, "better is better than not better."139

Discussing economic laws, one scholar has written:

It is also obvious that the type of rules which we have been discussing, although they are unquestionably rules of binding law, have in no way the character of religious commandments, laid down absolutely, obeyed rigidly and integrally. The rules here described are essentially elastic and adjustable, leaving a considerable latitude within which their fulfilment is regarded as satisfactory.140

The author was the anthropologist Bronislaw Malinowski, and he was discussing the economic laws of Melanesia. The analogy between savage society, as he called it, and the family of nations needs no emphasis.

137. McCulloch, Unexpected Real Consequences of Floating Exchange Rates, in ESSAYS IN INTERNATIONAL FINANCE 20 (No. 153, 1983) ("[I]nternational political realities precluded the 'choice' or 'design' of a new system. Perhaps Bretton Woods was a unique phenomenon, at least for modern times.").
138. Widman, Monetary Reform Requires Political Overhaul, J. COM., Mar. 3, 1983, at A4, col. 6 ("The shock of returning to economic isolationism would destroy free societies as surely as continued economic recession. Radical revisions of present policies which increase the power of supranational authority are the changes of generations. For now what we need is the maximum degree of economic policy coordination which can be achieved within the prevailing political framework.").
139. N.Y. Times, June 5, 1983, § S3, at 12; cf. 26 KEYNES, supra note 30, at 2-3 ("[T]he underlying truth, namely that none of these schemes will ever be accepted for their own beautiful eyes or special merits, but because as soon as one faces the probable alternative it is obviously so much worse.").
140. B. MALINOWSKI, CRIME AND CUSTOM IN SAVAGE SOCIETY 31 (1932).
APPENDIX A

EXCHANGE RATES AND SOVEREIGNTY UNDER H.D. WHITE'S STABILIZATION FUND

It will perhaps help toward understanding and induce a more sympathetic approach to the proposals which follow to state at the outset that something much more than the usual banking and stabilization functions are envisaged in the plan. There is urgent need for instruments which will pave the way and make easy a high degree of cooperation and collaboration among the United Nations in economic fields hitherto held too sacrosanct for international action or multilateral sovereignty. A breach must be made and widened in the outmoded and disastrous economic policy of each-country-for-itself-and-the-devil-take-the-weakest. Just as the failure to develop an effective League of Nations has made possible two devastating wars within one generation, so the absence of a high degree of economic collaboration among the leading nations will, during the coming decade, inevitably result in economic warfare that will be but the prelude and instigator of military warfare on an even vaster scale.¹⁴¹

The circumstances under which it may be wise to alter an exchange rate in order to correct maladjustments of the balance of payments have long been a matter of controversy among monetary theorists. But there is general agreement that an alteration in the value of a currency in terms of gold (or in terms of important currencies) is a very serious business and one not to be undertaken lightly. The change in the value of a currency in terms of gold or other currencies means that a change has by that act been imposed on the other currencies. When, for example, the dollar changes in terms of sterling, obviously sterling changes in terms of the dollar. Because all countries are to a lesser or greater degree affected by the action of any one country with respect to the value of its currency, it is only reasonable to demand that such action should not be undertaken without careful—and, if possible, impartial—weighing of the consequences of the action on other countries.

The purpose of requiring approval by the Fund as a condition of alteration of currency is to assure joint consideration of the merits of the proposed action and thereby avoid unilateral action taken to obtain presumed competitive short-run advantages irrespective of the consequences of the impact of the step on other countries or even on the same country. The mere fact that membership would be forfeited if a country acted in so important a matter contrary to the wishes of the majority would make countries hesitate to undertake lightly a change in their currency. The very discussion of the problem by competent representatives of various countries should in itself be a potent influence to avoid unnecessary changes. It would, moreover, be an assurance that when a change is made it would not be a signal for numerous other countries to follow in their own real or presumed interest . . . .

¹⁴¹ 3 J. Horsefield, supra note 7, at 40.
Some objection to this requirement will doubtless be raised on the ground that such a provision means that other countries pass judgment on what is a domestic monetary matter. The necessity for obtaining approval of other countries on such a matter will be regarded in some quarters as a serious infringement of sovereignty. There is some measure of truth in this but hardly enough to constitute a decisive reason for not participating in the Fund. Alteration of a currency affects other countries as well as the country making the change. It is, therefore, only reasonable to demand that the other countries have some say in the decision. Furthermore, all members would be surrendering their "rights" to an equal extent. Unless nations are willing to sacrifice some of their power to take unilateral action in matters of international economic relations, there is very little hope of any significant international cooperation—let alone collaboration.

To avoid giving richer nations greater authority on such matters, by virtue of their larger number of votes, it may be desirable to give each participant only one vote when questions of altering currency rates are being voted upon. As a last resort, a country always has the choice of withdrawing from the Fund so that it can always preserve its sovereignty in monetary matters if it feels it is being prevented by the Fund from taking action deemed important to its own interest.

The principle worked only tolerably well in the Tripartite Accord during 1935, 1936 and 1937, and better machinery for more adequate discussion and greater willingness to recognize the legitimate interests of other countries, needs to be developed to achieve best results. In evaluating the need for collaboration on questions of foreign exchange rates, it is well to remember that unilateral action can easily be neutralized by similar action on the part of other countries. When a competitive advantage is sought it is essential if it is to be successful that other countries do not take similar action. Otherwise the advantage hoped for is lost. Where the chief objective sought is not a competitive trade advantage in the international market but modification of the domestic price structure or money market, the favorable effects cannot be wholly negated by action of other countries. Since, however, the chief reason for establishing the requirement is to avoid competitive depreciation of currencies, the fact that unilateral action can be easily neutralized constitutes an important argument for securing approval of the Fund before taking such action.142

APPENDIX B

KEYNES ON DISCRETIONARY POWERS

Proposals for an International Currency (or Clearing) Union

Perhaps the most difficult question to determine is how much to decide by rule and how much to leave to discretion. If rule prevails, the liabilities attaching to membership of the system are definite, whilst the responsibilities of central management are reduced to a minimum. On the other hand,

142. Id. at 65-66.
liabilities which would require the surrender by legislation of too much of the discretion, normally inherent in a Government, will not be readily undertaken by ourselves or by the United States. If discretion prevails, how far can the ultimate decision be left to the individual members and how far to the central management? If the individual members are too free, indiscipline may result and unwarrantable liberties be taken. But if it is to the central management that the discretions are given, too heavy a weight of responsibility may rest on it, and it may be assuming the exercise of powers which it has not the strength to implement. If rule prevails, the scheme can be made more water-tight theoretically. But if discretion prevails, it may work better in practice. All this is the typical problem of any supranational authority. An earlier draft of this proposal was criticized for leaning too much to the side of rule. In the provisions below the bias is in the other direction. For it may be better not to attempt to settle too much beforehand and to provide that the plan shall be reconsidered after an initial experimental period of (say) five years. Only by collective wisdom and discussion can the right compromise be reached between law and license.143

Report to U.K. Ministers (February 7, 1944)

17. In the course of discussion, however, the American representatives were persuaded of the inacceptability of such a scheme of things, of the undesirability of starting off by giving so much authority to an untried institution, and of the importance of giving the member countries as much certainty as possible about what they had to expect from the new institution and about the amount of facilities which would be at their full disposal. In the final draft, therefore, all the technical matters at issue, except one, have been in the end settled on the expert level.

18. The one matter outstanding which flows from an initial difference of approach by the Clearing Union and by the Stabilisation Fund respectively, is as follows. Under the Clearing Union proposals the member countries were to bank with the institution, where they would have accounts on which they were free to operate in terms of a new international unit of account, to be called bancor. Under the Stabilisation Fund proposals the institution was to bank with the member countries, holding accounts with their central banks on which it would be free to operate in terms of each member's currency, so that no new international unit would be necessary. An international money of account, unitas, was mentioned in the Stabilisation Fund proposals but was only mentioned to be forgotten and played no effective part. Now this difference, however important, is nevertheless only a matter of technical form. A given set of proposals can be drafted in terms of either set-up so as to be identical in substance and legal effect.144

143. Id. at 6.
144. 25 KEYNES, supra note 21, at 404-05.