TREASURY DEPARTMENT

INTER OFFICE COMMUNICATION

DATE June 5, 1944

TO Mr. Luxford

FROM E. M. Bernstein

I am returning my copy to you with some markings on verbal points. Will you please return this copy to me ~~and also the copy of the first draft which I gave you some days ago~~?

On major points I have the following comments:

OK x Article II. The word "subscription" should be used instead of "quota" when it is a question of payment.

OK x Section 2 and Section 3 should be omitted completely. So far as the initial quotas go they should be determined by the table in Section 4. The formula should be included in Section 5 in the provision requiring periodic adjustment of quotas for which the formula may be the basis.

OK Article II, Section 6. A member country whose quota is increased can't pay the full amount of the increase immediately. If it has to make any payment in gold it may have to send it to the nearest depository. The provision should read: "Any member country whose quota is increased shall pay the full amount of the increase within one month of the date on which its director communicates the approval of his government to the increase in its quota."

See my re-write Article III, Section 2. I see no need at all for the first sentence at this point. If it is desired to retain it here it should be amended to read as follows: "All transactions between the Fund and member countries shall be at the par values of the currency of the member countries subject to such charges established by the Fund."

" Sentence 2 also seems to me a little less than perfect but we can go into that another time.

OK Section 3-b-3. I would add the par value of such country as initially agreed "with the Fund."

Section 3-b-4. Within two "business" days.

Article III, Section 4. The word "securities" can be dropped since it is already covered by the definition of currency. No part of this payment should be in gold for the first paragraph. It is doubtful whether there should be any gold payment in this connection even in the second paragraph.

Article IV. Substitute Section, Part A. "The holdings of the Fund of a currency of each member country, to the extent deemed by the Fund to be necessary for its operations, shall be deposited in the name of the Fund in the depository designated for that country in accordance with Article VII, Section 6." Corresponding changes should be made in the second paragraph.

Part B. It isn't clear to me what is meant by special depositories. See my proposed substitution for Article VII, Section 6.

Section 6. Substitution. "(a) Arrange with the member country to borrow from it such currency on appropriate terms and conditions."

"(b) Request the member country to sell such currency for gold on appropriate terms."

Note the verbal changes in Section 7.

Section 9, Part A. Avoid use of the term "exchange gold for currency." Use the terms "purchase, sale and repurchase".

Section 9, Part B. This statement is unsatisfactory. Take out the words "at the end of any financial year of the Fund", and add a sentence, "The Fund shall make provision for adjusting such gold payments to half the net sales at the end of its financial year."

Section 11, Part B. The Fund may levy.

Part C. Substitute the following, "Penalties on currency holdings in excess of quotas. The Fund may prescribe uniform penalties against member countries on the amounts of their currencies held by the Fund in excess of the quota for periods exceeding six months. The Fund may prescribe uniform graduated penalties on such holdings for successive semi-annual periods thereafter.

"The Fund may waive the penalties due in any semi-annual period on currency holdings repurchased by member countries under Parts A and C of Section 9, provided the amount repurchased in that period exceeds 12-1/2 percent of its quota."

Part D. "At the end of its financial year, the Fund may levy on member countries in proportion to their quotas charges sufficient to meet the expenses during that year."

Part E. I am not at all sure what the second sentence means. If the Fund sold sterling for dollars, would the Fund undertake to provide England with the dollars needed to retain the sterling?

Section 12. "any member country may be required to furnish whatever information is needed by the Fund in connection with any action it has requested the Fund to t ake."

Article V, Section 1. This statement isn't satisfactory. It may penalize a country for having taken action which may or may not be in accordance with the Fund policies without having been given previous notice. It should read something like this: "No member country may use the resources of the Fund to meet a large or sustained outflow of capital, and the Fund may require a member country to exercise controls to prevent such use of the resources of the Fund. For failure to comply with such a request the Fund may declare a member country ineligible under Article III, Section 5.

Article VII, Section 2. Instead of a majority of the votes cast, you better have it a majority of the member votes.

Section 3, Part B. There is no provision for who conducts the voting, no provision for nominating and no provision for dropping the person with the lowest number of votes. I suggest the following: "At least one month before the annual meeting of the board of directors, the executive committee shall call upon member countries to nominate directors to serve on the executive committee. Prior to the annual meeting, the executive committee shall notify all countries of the nominees. At the voting on the first ballot all nominees who receive less than 1 percent of the aggregate votes shall be stricken from the second ballot, but under any circumstances the nominee receiving the smallest number of votes shall be stricken from the second ballot. On each successive ballot the nominee with the smallest number of votes shall be stricken from the succeeding ballot."

Section 6. Add the following: "The Fund shall designate in each member country as a depository for the holding of its local currency of such country, the central bank or other bank approved by the director of the country concerned.

"The Fund shall designate in some member countries as general depositories (or offices or agencies?) for the holding of gold, the central bank or other place of safe keeping approved by the director of the country concerned.

"The Fund may designate any approved places of safe keeping in member countries for the holding of any other assets of the Fund." (No approval required here.)

Section 7. "and shall publish at quarterly intervals, or more frequently if deemed desirable, a summary statement of its transactions, etc."

"The Fund may publish such other reports as it deems desirable for carrying out its purposes and policies."

Article VIII, Section 4. "When a member country withdraws or is dropped from membership in the Fund and the Fund's holdings of its currency exceed its quota, all other member countries undertake to purchase from the Fund the amounts of such currency they may need from time to time in the purchase of goods for export or in payment of obligations to the former member country.

"Each member country unconditionally guarantees that when it withdraws or is dropped from the Fund and the Fund holds its local currency in excess of its quota, its currency held by the Fund may be sold to member countries and that such currency will be free for use in the purchase of goods for export or in payment of obligations to it.

"Each member country unconditionally guarantees ~~that~~ the value of such currency held or sold to the member country ~~shall be assured~~ against exchange depreciation until it has been used in making payments."

Section 5. Liquidation. This whole section needs probably a lot more work than it has had. This is a good statement as it stands and I havn't had time to go through it to see how it differs from what I am now sending you.

"(a) Debts of the Fund shall have a prior claim on the assets of the Fund. They shall be paid in the specified currency or in gold.

(b) The procedure for general liquidation shall be as follows: List the countries in inverse order of the Fund's holdings of their currency relative to their quotas and number them successively from one to _____.

On the first drawing Country 1 shall draw all of its currency and as much gold as is necessary to reach the position of Country 2, at which time Country 2 shall draw all its currency. On the second drawing Countries 1 and 2 shall draw as much gold as is necessary in proportion to their quotas until they reach the position of Country 3, at which point Country 3 shall draw all its currency. These successive drawings shall be continued until all the gold has been exhausted. At that point, all countries will draw in their own currencies the portion of their quotas paid out to all countries with a higher number. Thereafter, the Fund's remaining holdings of each successive currency will be divided successively among all member countries in a lower position pro rata until the aggregate payment to each country reaches the position of the country next below in the list. This will continue until all of the Fund's holdings are divided.

I attach a table showing concretely how this would work out for 13 countries having aggregate quotas of $5 billion, the Fund holding $4560 million in local currency and $490 million in gold.

This is probably the best way of liquidating the Fund.

The alternative that I am also suggesting is in no way different from the one outlined above although it sounds much simpler. I should have to work out the details for handling the gold.

Alternative

(a) Debts of the Fund shall have prior claim and be paid in specified currency or in gold.

(b) Divide all the currencies pro rata according to quotas. Any country can repurchase its currency from any other country with that country's currency and member countries are under obligation on liquidation to make such sales.

(c) List the countries that have wound up with their own currency in inverse order by ratio of quotas ultimately returned in their own currency. Now divide gold among all countries pro rata, with countries high on the list given the option of acquiring the gold of countries lower on the list in return for their local currency. I think this won't be complicated when it is worked out in detail.

Further provision on liquidation. "Each country unconditionally guarantees that its currency distributed to other member countries in liquidation will be free for use without exception in the purchase of goods for export or in payment of obligations to it. Furthermore, each country unconditionally guarantees the currency so distributed against exchange depreciation until the funds have been used in making payments in accordance with the above."

Article IX, Section 2. Title. Gold purchases based on parity prices.

Section 3. Title. Foreign exchange dealings based on par values.

Article IX, Section 10. Section B should be omitted. You have it in a more appropriate place under "Transitional Arrangements."

Section 10. Add at the end of the sentence "in the internaational balance of payments of member countries.

Article X, Section 1. "Arrangements and practices which impede payments and transfers for international transactions on current account.

Article XII, Section 2. The definitions are unsatisfactory. We will have to give you alternative ones.

Article XIII, Section 4. Insert new provision C: "No transactions in exchange shall be undertaken by the Fund until three months after the date set for its operations to begin. Such transactions can be undertaken then only if rates of exchange, satisfactory to the member countries and the Fund, have been set for countries having 75 percent of the aggregate quotas. No transaction shall be undertaken by the Fund in the currency of any member country until a rate of exchange satisfactory to the member country and the Fund has been agreed."

Section 5. I suggest the expiration date of June 30, 1945.