

28 June 1945

Mr. Friedman

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Re: Liquidation of the Bank for International Settlements

Resolution V of the United Nations Monetary and Financial Conference recommends:

"Liquidation of the Bank for International Settlements at the earliest possible moment."^{1/}

The question as to the manner in which this is to be effected remains unsettled. The purpose of this memorandum is to investigate the various techniques which may be used in order to obtain the liquidation of the BIS.

A. Legal Status of the BIS

Pending - and pertinent to - determination of the technique to be used in obtaining the liquidation of the BIS, the question of which country's municipal law should govern the liquidation must be resolved. This leads into the question of the exact legal status of the Bank. The ambiguous and unusual legal nature of this institution is aptly brought out by E. L. Dulles in her book "The Bank for International Settlements at Work". She notes:

"It is, in many respects like other private corporations formed under the laws of Switzerland, and in others it is an independent international organization under the joint control of a group of states and Central Banks. It enjoys some privileges and immunities, but only in certain countries and in limited respects."^{2/}

The Bank's "extra-legal" character may be seen by reference to the terms of the Convention -- signed by representatives of Germany, Belgium, France, United Kingdom, Northern Ireland, Italy and Japan on the one part and Switzerland on the other -- which provided for the incorporation of the BIS in Switzerland. Switzerland undertook to grant the BIS's Charter the force of law, not to amend or add to it, and not to sanction amendments to certain of the Bank's

^{1/} United Nations Monetary and Financial Conference, Final Act and Related Documents, 1944, p. 22.

^{2/} Dulles, The BIS at Work (1932), p. 68. The author goes on to point out the existence of at least three different theories as to the nature of the Bank and its legal position. Also, see Hudson, The Bank for International Settlements (1930), 24 A.J.I.L. 561, who notes that "Many questions may arise concerning the status of the bank and the law governing its operations. It is clearly a Swiss corporation, but in many ways it is a hybrid which is outside the control of the Swiss Government." (p. 565).

Statutes except in agreement with the other signatory Powers.^{3/} The Bank's Charter provides for wide tax exemptions for the Bank.^{4/} The Charter also provides that --

"The Bank, its property and assets and all deposits and other funds entrusted to it shall be immune in time of peace and in time of war from any measure such as expropriation, requisition, seizure, confiscation, prohibition or restriction of gold or currency export or import, and any other similar measures."^{5/}

By the general Hague Agreement on German Reparations (January 1930), Germany, Belgium, Great Britain, Canada, Australia, New Zealand, South Africa, India, France, Greece, Italy, Japan, Poland, Portugal, Rumania, Czechoslovakia and Yugoslavia, recognized the corporate existence of the Bank as soon as constituted and agreed to take the measures necessary for freeing the "funds and investments of the Bank resulting from the payments by Germany" from all national or local fiscal charges. In addition, they agreed to grant the Bank immunity from restrictive measures in language substantially the same as quoted above from the Swiss agreement.^{6/}

In spite of the above, and in the absence of any other governing law, or controlling provisions in the Bank's Statutes or Charter, no conclusion seems warranted other than that Swiss law, insofar as applicable, must govern the liquidation of the BIS.^{7/}

B. Function of the BIS

In order to better appreciate the issue at hand, a short summary of the BIS's function must be presented. The BIS is a creature of the so-called Young Plan, which attempted to institute appropriate machinery for the complete and final settlement of the reparation problems resulting from World War I.^{8/} It was anticipated that the Bank would "provide an elastic element between the payments to be made by Germany and their realization. In consequence, the creditors will have further assurance that the effects of economic changes on the flow of payments will be minimized, and Germany for her part will have the possibility of assistance during temporarily unfavorable conditions."^{9/}

^{3/} Convention Respecting the Bank for International Settlements, Art. 1, 24 A.J.I.L. (1930 Supp.) 323.

^{4/} Constituent Charter of the Bank for International Settlements, para. 6-9.

^{5/} Id., para. 10.

^{6/} Williams, The Legal Character of the BIS (1930) 24 A.J.I.L. 665, 672.

^{7/} Hudson, op cit supra, arrives at substantially the same conclusion. Also, see Williams, op cit supra.

^{8/} The Young Plan, formally referred to as the "Report of the Committee of Experts," is set out in 24 A.J.I.L. (1930 Supp.) 81.

^{9/} Id., pp. 88-89.

Specifically, as noted in its Statutes adopted at the Hague Conference on Reparations in January 1930, the Bank's objects are:

"to promote the co-operation of central banks and to provide additional facilities for international financial operations; and to act as Trustee or Agent in regard to international financial settlements entrusted to it under agreements with the parties concerned."^{10/}

With reference to the latter objective, the BIS was constituted to act as trustee or agent in connection with the following financial settlements and transactions:^{11/}

- 1) The receipt, administration and distribution of the German annuity payments pursuant to the Hague Agreements of January 1930;
- 2) The receipt and distribution as fiscal agent for the trustee of funds payable pursuant to the terms of said Hague Agreements by Bulgaria, Hungary and Czechoslovakia;^{12/}
- 3) The receipt and distribution of funds - (a) relative to the service of the German External Loan of 1924, (b) the German International 5 $\frac{1}{2}$ % Loan 1930, (c) the Austrian Government International Loan 1930.

The annuity payments required by Germany, Hungary, Bulgaria and Czechoslovakia pursuant to the agreements mentioned above were suspended by the creditor powers' acceptance of the Hoover Moratorium, which provided for suspension of inter-Governmental debts falling due during the year July 1, 1931 - June 30, 1932. At least two specific attempts have been made since then to reach an effective agreement as to the general problem of reparation payments which the Young Plan had failed to solve - the London Protocol of August 11, 1931 and the Treaty of Lausanne of July 9, 1932 - neither of which were successful. The Lausanne Agreement made elaborate provision for voiding the Young Plan annuities and floating a new bond issue. The agreement reached was not to be effective until ratified by the Creditor Powers, who, in turn, announced that they would not ratify until they had reached an agreement with their own creditors, viz., the United States. At the outbreak of World War II, the Lausanne Agreement still had not been ratified and since reparation payments were suspended pending ratification of the Agreement, such payments have, for the most part, been suspended since the Hoover Moratorium.

^{10/} Art. 3. See 24 A.J.I.L. (1930 Supp.) 326, 327. Chapter III of the Statutes defines more specifically the powers of the Bank.

^{11/} The Trust Agreement Between the Creditor Governments and the Bank for International Settlements is carried as Annex VIII to the Hague Conference on Reparations, January, 1930. See 24 A.J.I.L. (1930 Supp.) 284.

^{12/} The pertinent agreements may be found in 25 A.J.I.L. (1931 Supp.) p. 10, et seq.

The servicing of the German bond issues referred to above was not affected by the Hoover Moratorium, the London Protocol, or the Lausanne Agreement; however, the German Government has not made any payments to the BIS on either account since July 1, 1934. (But the German Government did enter into individual agreements with certain governments and made payments to certain classes of bondholders). In May 1938 the German Government announced that it did not consider itself the legal successor of the former Republic of Austria as regards loans contracted by Austria. Accordingly, as from June 1, 1938, it suspended payment on the Austrian Government International Loan 1930.^{13/}

Three letters recently written by Mr. McKittrick, President of the BIS, are pertinent to the issue at hand, were addressed to the Secretary of the Treasury (dated May 2, 1945 and May 17, 1945) and the other (dated May 2, 1945) was addressed to the British Chancellor of the Exchequer. In each of these, the history of the Bank's position with reference to one or the other of the problems indicated above is reviewed. The May 2nd letter addressed to the Secretary of the Treasury is written as "Trustee" of the German Government International 5 $\frac{1}{2}$ % Loan 1930 and the German External Loan 1924. Specific attention is called to the obligations of the German Government and the rights of the bondholders. Mr. McKittrick concludes:

"In consequence, we trust that the Governments on whose behalf the Loan was issued and who have ceded to the Bondholders in guarantee part of their rights, will take all possible steps as soon as circumstances permit to ensure that the engagements solemnly entered into be respected, that the arrears be paid, and that the service of the Loan be resumed in accordance with the conditions of the international agreements and the contracts which govern it. In our capacity as Trustee of the Loan, we have the honour, by the present communication, to make the formal request that appropriate measures to this end be taken."

The May 17 letter, addressed to the Secretary of the Treasury, is of the same tenor as the above except that it concerns the Austrian Government International Loan 1930.

The letter addressed to the British Exchequer summarizes the rights and obligations of the BIS arising out of the Hague Agreements of January 1930. It is maintained that "these agreements have established a legal connection between the British Government and the BIS with reciprocal rights and obligations". The British Government is requested to abstain from any action which may affect the Bank's rights and to do all in its power "to place the Bank in a position to exercise the rights which it possesses under the Hague Agreements". Finally, Mr. McKittrick states that, to the extent British action may adversely affect the Bank's position, the Bank will expect just compensation.

^{13/} See the Annual Reports of the BIS with reference to its activities as trustee and agent pursuant to the Young Plan and its successors.

In all of the above letters the Bank was emphatic in pointing out that it has never accepted the unilateral breaches of the agreements to which it is a party and that it has consistently and expressly reserved all its rights. The significance of the above review is two-fold. It appears obvious that the BIS will not willingly give up its position under the pertinent agreements and that for a number of years the BIS has been unable to perform its primary function.^{14/}

C. Ways in Which the BIS Can Be Made to Liquidate

Prior to entering upon a discussion of the technique to be used in bringing about the liquidation of the BIS, consideration should be given to the Bank's financial condition.^{15/} Article 26 of the Bank's Statutes provides, in part:

"The Bank shall be administered with particular regard to maintaining its liquidity, and for this purpose shall retain assets appropriate to the maturity and character of its liabilities."^{16/}

Of course, the fact that the Bank's management is under an express duty to administer the Bank's assets with a view to maintaining a liquid position, does not insure that such a result will follow. However, there is reason to believe that the Bank's officials have been conscientious in this direction.^{17/}

With the exception of its long term German investments, the Bank's assets appear to be in an extremely liquid state. In a note to the 1942-43 balance sheet, certified to by Price, Waterhouse and Co., it is stated that "after providing for the German Government Deposit out of investments in Germany, nearly 60% of the assets then remaining are covered by special contracts guaranteeing their gold value."^{18/} The actual status of the German investments cannot be ascertained. Mr. McKittrick, in his letter of May 2, 1945, addressed

^{14/} Since the Bank has lost most of its duties as trustee or agent under the various international agreements, its income has been principally derived from the investment and use of its capital and deposits. Its income derived from commissions earned as trustee or agent was less than 1% of its net income in the 1942-43 financial year. (See the BIS's 13th annual report, April 1, 1942-March 31, 1943). The Bank's position is now confined to facilitating central bank cooperation, which includes collection of relevant economic information. It also accepts deposits from central banks for their own accounts and the accounts of their governments and it performs some minor clearing operations.

^{15/} A detailed analysis is precluded by the absence of complete information.

^{16/} 24 A.J.I.L. (1930 Supp.) 326, 332.

^{17/} In the last annual report, which covered the period April 1, 1942 - March 31, 1945, at p. 321, it is stated that "As in the past, attention has constantly been paid to the maintenance of the greatest possible liquidity in the assets of the bank."

^{18/} See Annex I to the Thirteenth Annual Report of the BIS.

to the Secretary of the Treasury (p. 7), barely notes that "on 31st March 1945 the BIS possessed investments on the German market to a total of about RM 237 millions." Under the same heading he notes that the Bank has a liability to the Creditor Powers, with respect to the non-interest-bearing balance of the Annuity Trust Account, of approximately RM 125 millions^{19/} and a liability to the German Government of RM 62.5 millions.^{20/}

In the 1942-43 balance sheet, the Annuity Trust Account represents 31.6% of the total liabilities, and the German Government Deposit represents 15.3%. In other words, 46.9% of the BIS's liabilities are of a questionable status and may reasonably be offset against the Bank's German investments, if such proves desirable. By playing the one against the other, there can be no question of the Bank's ability to liquidate in a reasonable length of time without any loss to creditors or stockholders.

As for the actual distribution of the Bank's assets, the only provision made in its Statutes is that the "general reserve fund" and the "legal reserve fund," after the Bank's liabilities are discharged, "shall be divided among the shareholders."^{21/}

1. Duration of the BIS. Another question which requires initial consideration before, and as a part of, attempting to determine which technique should be used in bringing about the liquidation of the BIS involves the length of time for which it was instituted. Article 4 of the Bank's Statutes provides, in part, that:

"As long as the New Plan as defined in the Hague Agreement of January, 1930 (hereinafter referred to as the Plan) is in force, the Bank (i) shall carry out the functions assigned to it in the Plan; * * *"^{22/}

^{19/} This is pursuant to the Article IV(e) of the Trust Agreement entered into with the Creditor Powers. 24 A.J.I.L. (1930 Supp.) 284, 289. There seems to be some question as to the actual status of this account. The note accompanying the 1942-43 balance sheet states:

"The Bank's commitment in respect of the Annuity Trust Account Deposits is not clearly established, but it is stated at its maximum amount in Swiss Gold Francs."

^{20/} Article IX of the Trust Agreement obligates the German Government to maintain "a non-interest-bearing deposit equivalent to 50 per cent, of the average deposit remaining in the Annuity Trust Account, but not exceeding 100 million reichsmarks."

^{21/} Statutes of the BIS, Article 54, 24 A.J.I.L. (1930 Supp.) 326, 339.

^{22/} 24 A.J.I.L. (1930 Supp.) 327.

The term "New Plan" is the name given to the "Experts' Plan of the 7th June 1929," (commonly referred to as the Young Plan). The Hague Agreements of January, 1930, accepted this Plan as "a complete and final settlement of German Reparations"^{23/} and provided for annual payments by Germany through 1987-1988.^{24/} Therefore, it seems reasonable to conclude that the incorporators contemplated the continued existence of the BIS at least through 1988.^{25/}

However, the Convention pursuant to which the Swiss Government granted the BIS its Charter was limited by its terms to 15 years.^{26/} But the fact that the Swiss Government also agreed to give the Bank's Charter the "force of law" and to obtain the assent of the Swiss people "for the maintenance in force during the whole of the Bank's existence" the provisions of the Convention^{27/} would lead to the same conclusion reached in the preceding paragraph. Nevertheless, the specific 15 year limitation cannot be ignored and it must be recognized that (in spite of the existence of a basis for imposing a moral obligation upon the Swiss Government to continue to be bound by the terms of the Convention until final payment is made under the Plan) there is a real question as to whether it is legally bound to renew its ratification of the Convention at the end of 15 years. Even granting that under normal circumstances the moral obligation might be weighty enough to compel favorable Swiss action, certainly it must have been contemplated that changed conditions could justify refusal to participate any further in the Bank's existence.

Another consideration is that in fact the Bank has not for quite some time performed any function pursuant to the Young Plan, which must necessarily be the basis of any plea that the Bank should continue in existence for any definite period. Of course, the Bank will insist that it has continuing rights and obligations. However, "rights and obligations" in the absence of any active function to perform fall far short of constituting a convincing agreement for continuing the Bank's existence.

^{23/} Article I, 24 A.J.I.L. (1930 Supp.) 263.

^{24/} Paragraphs 85-88, 24 A.J.I.L. (1930 Supp.) 95.

^{25/} This conclusion is strengthened by reference to article 55 of the Bank's Statutes which provides that the Bank may not be liquidated "before it has discharged all the obligations which it has assumed under the Plan." 24 A.J.I.L. (1930 Supp.) 326, 340.

^{26/} Art. 3, 24 A.J.I.L. (1930 Supp.) 323, 324.

^{27/} Id., Articles 1 and 3. Perhaps mention should also be made of the fact that no attempt is made anywhere to define "during the whole of the Bank's existence."

2. Liquidation Pursuant to the Bank's Statutes. References to voluntary or involuntary liquidation are surprisingly few. It is specifically provided that voluntary liquidation proceedings may not be instituted before the Bank "has discharged all the obligations which it has assumed under the Plan" and then only by a "three-fourths majority of the general meeting."^{28/} The "general meeting" referred to must mean "extraordinary general meeting," as Article 49 of the Bank's Statutes, which enumerates the reasons for convening the latter, provides that it "shall be summoned to decide upon any proposals of the Board * * * to liquidate the Bank."^{29/}

On the basis of the above, if it is desired to liquidate the BIS by voluntary proceedings, the Bank's present attitude towards its continuing rights and obligations must be changed. In other words, there must be an admission by all concerned that the World War I reparation problems are only of historical interest. Once this is done the Board of Directors will be in a position to convene the "extraordinary general meeting" and propose that the Bank be liquidated. Then, of course, there will still remain the task of obtaining the necessary majority.

If the above procedure is rejected as being impossible due to the attitude of the Bank's present officials^{30/} and it is felt that a voluntary liquidation is desired, pressure must be applied to obtain a new Board of Directors in sympathy with the United Nations recommendation that the BIS be liquidated. However, even this may not be sufficient if the participants in the general meeting are not in accord.

Perhaps mention should be made at this point of the manner in which the Board of Directors is selected and who is eligible to participate in the general meeting. The Board of Directors is made up as follows:^{31/}

- 1) The governors of the central banks of Belgium, France, Germany, Great Britain, Italy, Japan and the United States, or their nominees, may participate as ex officio directors;

^{28/} Statutes of the Bank for International Settlements, Article 55, 24 A.J.I.L. (1930 Supp.) 326, 340.

^{29/} Id., Article 49, p. 337.

^{30/} There is good reason to believe that the Bank's present officials are not in sympathy with any attempt to liquidate the Bank. In 1943 the Board of Directors was composed of 3 Germans, 3 Parisians, 2 from Rome, 2 from Japan, 2 from London, and one each from Brussels, Stockholm, The Hague and Zurich. (Note that at the time, 12 directors represented Axis or Axis-occupied territory, while only 4 represented the Allies and Neutrals). See the Bank's 13 th Annual Report, April 1, 1942 - March 31, 1943.

^{31/} See Article 28 of the Bank's Statutes, 24 A.J.I.L. (1930 Supp.) 326, 333.

2) Seven persons representative of finance, industry or commerce, appointed one each by the governors referred to in (1) above (these directors hold office for 3 years and are eligible for reappointment), (a) if one of the governors does not exercise his power of appointment, a majority of the others may exercise it for him;

3) Not more than 9 persons (for 3 years) elected by the Board from a list of nominees submitted by the governors of central banks of every country, other than those mentioned in (1) above, in which capital was subscribed in the Bank at the time of its incorporation. Vacancies are filled in accordance with the same procedure by which the member to be replaced was selected.

As for participation in the general meeting, it is specifically provided that "ownership of shares of the Bank carries no right of voting or representation at the general meeting." This right exists in the central bank of the shareholders country in proportion to the number of shares subscribed in that country. If the central bank does not desire to exercise its rights, there may be substituted "a financial institution of widely recognized standing and of the same nationality, appointed by the Board, and not objected to by the central bank of the country in question." If there is no central bank, the Board may appoint a financial institution in the country to exercise the rights.^{32/}

Of significance in weighing whether an attempt should be made to replace the present Board of Directors is, where are the Bank's shares held? The latest, most complete breakdown shows that in 1943, of the 200,000 shares issued Germany held 110,000, Italy, England, Japan and the United States, 20,000 each.^{33/} On the basis of these figures, assuming that the Allied Control Council is able to exercise rights of ownership over the German held stock, either directly or through the central bank, the United States and Great Britain will be in a position to control the general meeting. And then it should be a comparatively easy matter for the two Governments to place the BIS into "voluntary" liquidation.

^{32/} Id., Article 15, p. 329; also, see Article 46, p. 336.

^{33/} The figures were obtained from an article which appeared in the February-March 1943 issue of the "Protestant," written by Heinz Poi, former editor of the Vossische Zeitung.

3. Liquidation by Order of the Swiss Government. Switzerland, as the State of incorporation, has the power to deprive the BIS of a situs. That is, the Swiss Government may refuse to continue to recognize the corporate existence of the Bank within its jurisdiction, and thereby place the institution in a position which would leave it no alternative but to liquidate. Of course, this assumes that no other country would accept its incorporation in light of the stand taken by the United Nations.

Any Swiss objection to following such a course would probably be on the basis that it would require the breaching of an international agreement or, at least, it would violate a moral obligation. The implications of this position have been referred to above. However, some repetition and elaboration is warranted.

If Switzerland is at all in sympathy with the United Nations' recommendation, it can reasonably adopt the attitude that any obligation which it might have had at the end of 15 years to renew the BIS's Charter pursuant to the Convention's terms, as adopted in 1930, has been erased by changed circumstances. Certainly the Bank's incorporators, present officials or the Swiss Government cannot ignore the cloud which has been cast over the Bank's activities throughout World War II. On this level, the plea might be made to the Swiss Government that not to deny the BIS a situs by refusing to renew the Convention would be tantamount to sanctioning the Bank's pro-Axis activities. Of course, the reception of this approach will depend in the first instance upon the "mood" of the Swiss Government. It can, as has the Bank, deny that the BIS has been anything but neutral during the past 6 years and ignore the evidence which the Allied Powers have accumulated.

Another caveat comes to mind, if the 15 years limitation found in the Convention is effective, the Convention expired, unless it has been renewed, in January of this year. Nothing is known as to whether the Swiss Government has renewed the BIS's Charter, or whether it feels that affirmative action is necessary. In other words, to place reliance upon the 15-year limitation is a stroke in the dark, which might well represent wasted effort. But, over and above this, much of what has been said and of what could be said in the same vein is certainly a valid basis for approaching the Swiss Government with the suggestion that it revoke the BIS's Charter. If the Swiss are in sympathy, the approach they use, as long as it is effective, is only incidental.

4. Liquidation by Action of the Governments Within Whose Jurisdiction the Shares Are Held. If the methods previously suggested are rejected, the BIS could probably be liquidated as the result of direct action taken by the Governments within whose jurisdiction the shares are held. This action may take any one of several directions and need not be taken by all the Governments concerned.

It is unfortunate that a more complete breakdown of the BIS stock ownership and of the geographical distribution of its assets is not available. However, it is assumed that any affirmative action taken by the participants in the

Bretton Woods Agreements will precipitate similar action in any other countries concerned. An additional stumbling block which might be relied upon by those whom are not in sympathy with the proposed liquidation is the previously noted fact that virtually all of the Creditor Powers under the Versailles Treaty are bound to grant the BIS immunity from restrictive measures in the same manner as Switzerland is bound. The Creditor Powers so-agreed in connection with the Hague Agreements on Reparations of January 1930.^{34/} They, the Creditor Powers, could rightfully assert that the reparation settlement provided for in the Agreement has already been breached and that it would be unrealistic to pretend that World War I reparation payments will be received. Nevertheless, judging from the tone of Mr. McKittrick's letters discussed above, the Bank expects some "consideration" for the loss of its rights and potential earnings under the various agreements. *revised.* Against whom such claims may be asserted, their extent and validity are not within the provisions of this memorandum. *provision*

transfer?
Once it is agreed to take appropriate Government action, various techniques present themselves. The countries in which BIS stock is held could decree that the holding of such stock is inimical to its national interest and must be disposed of immediately. The threat of this action, with its unquestionable effect upon the market value of BIS stock, would, at least, have a tendency to compel the BIS to go into liquidation. The point is, once the BIS officials see that the United Nations mean "business" they will be provoked into the desired action.

A variation of the above proposal would be for the Governments concerned to take over direct ownership of the stock if they have not already, and in that position to institute any additional steps necessary to compel liquidation of the Bank. Or, the Governments, at least the Allied Powers, could (and perhaps should) confiscate a good portion of the Bank's assets within their jurisdictions as having been tainted with enemy interests. If the individual Allied Powers are reluctant to take this step, the Allied Control Council should be directed to include BIS property, to the extent that it represents German interests, within the jurisdiction of its decree vesting German external assets.

D. Conclusion

In summary, there are at least 3 possible techniques which may be adopted to obtain the liquidation of the BIS. The Board of Directors and the general meeting may, pursuant to the Bank's Statutes, vote the Bank into voluntary

^{34/} Set out in 24 A.J.I.L. (1930 Supp.) 259.

liquidation; Switzerland, as the incorporating State, may compel the Bank to liquidate by withdrawing its Charter; or, the Governments within whose jurisdiction BIS stock or property is held may take any one of several steps designed to compel the BIS to liquidate.

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The most direct and probably the speediest method would be to convince the Bank's officials that the United Nations are determined to see to it that the BIS is liquidated and that if voluntary proceedings are not instituted the Governments concerned take more drastic measures within their own jurisdictions. If it is obvious that this technique will not be effective without electing a new Board of Directors, it is suggested that the Swiss Government be approached and asked to revoke the Bank's Charter. If this fails, the United Nations must be prepared to utilize their governmental powers to obtain a sympathetic Board of Directors or to gain direct control over the Bank's stock and property within their jurisdictions and utilize the one or the other to procure the desired result.