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Shifting Paradigms: Institutional Roles in a Changing World

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ARTICLES

SHIFTING PARADIGMS: INSTITUTIONAL ROLES IN A CHANGING WORLD*

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INTRODUCTION

IN July 1944, the representatives of forty-four allied powers met in Bretton Woods, New Hampshire, to plan the rebuilding of the international economic system in anticipation of the successful conclusion of the Second World War.[1] With greater or lesser enthusiasm, we now reach a time when we may celebrate the fiftieth anniversary of that conference. The accomplishments and setbacks of the system envisaged by that fateful series of meetings invite study.[2] This article focuses on shifts in the paradigm[3] of the international economic system envisaged by Bretton Woods, moments of institutional crisis that test the vitality of the system and its presuppositions. The article argues that a series of institutional crises, some as yet unresolved, has fundamentally transformed the system constructed at Bretton Woods and that its vitality rests on its ability to maintain fidelity to its original values.

Part I of this article examines the problems addressed by the Bretton Woods conference itself and attempts to identify some of the original

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1. For a discussion of the design and objectives of the Bretton Woods Conference, see Gerald M. Meier, *The Bretton Woods Agreement—25 Years After*, 23 Stan. L. Rev. 235, 237-45 (1971).

2. For what must be the leading work in English in this regard, with particular emphasis on the International Monetary Fund ("IMF"), see generally Richard W. Edwards, Jr., International Monetary Collaboration (1985); *see also* John H. Jackson & William J. Davey, Legal Problems of International Economic Relations 251-359 (2d ed. 1986) (discussing international economic regulation and Bretton Woods System).

3. On the concept of a "paradigm shift," a notion borrowed from the philosophy of science, see Michael P. Malloy, *Can 10b-5 for the Banks? The Effect of an Antifraud Rule on the Regulation of Banks*, 61 Fordham L. Rev. S23, S25-S26 n.12 (1993).

values underlying the Bretton Woods system.[4] Part II reviews some of the institutional crises that have caused paradigm shifts in the Bretton Woods system of international economic regulation.[5] Part III analyzes, in more detail, a current situation that could lead to an institutional crisis: the economic transformation of the fifteen republics of the former USSR.[6] Part IV concludes that this economic transformation need not result in a paradigm shift, a "challenge" to the presuppositions that underlie the current Bretton Woods institutions, but rather may be viewed as an "opportunity" to vindicate the original values of those institutions.[7]

I. BRETTON WOODS AND ITS ORIGINAL VALUES

The Bretton Woods conference and the institutional solutions that emerged from it must be understood against the background of international events in the two decades preceding it.[8] In some respects, the project of the conference was reactive: to reform the rubrics of international finance and trade to eliminate what were perceived as harmful and predatory practices prevalent during the 1930s. While some of these practices certainly predate that decade, the worldwide depression of that period encouraged the aggressive use of predatory finance and trade practices and exacerbated the consequences of such practices.

International trade is an important component of balance of payments between nations,[9] and the resulting inflow and outflow of goods and payments has a significant effect on the condition of domestic economies.[10] In this sense, nations are doubly interdependent. As a matter of fact, economic events in one nation or region have a greater or lesser impact on other nations or regions.[11] As a matter of policy, strategies for economic growth in any one nation or region must ultimately presuppose

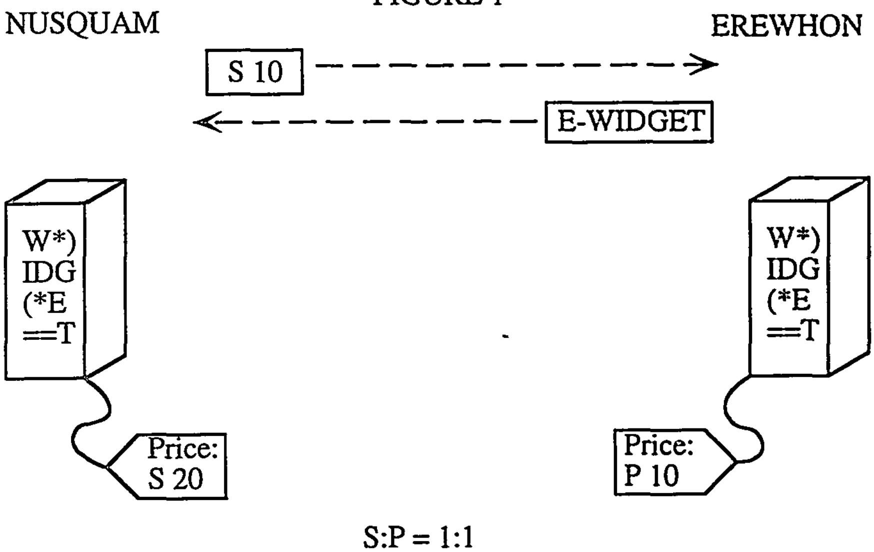
4. *See infra* notes 8-65 and accompanying text.
5. *See infra* notes 66-81 and accompanying text.
6. *See infra* notes 82-108 and accompanying text.
7. *See infra* notes 109-118 and accompanying text. Compare the words of one commentator who notes that :"the solution to this great challenge [of assisting the fifteen republics in becoming integrated into the world economy] is within our reach—and . . . it can be an important part of a global strategy to revive growth in the world economy. This challenge is an opportunity."
8. For a useful review and explanation of the historical impulses reflected in the Bretton Woods conference, see Edwards, *supra* note 2, at 4-8 (discussing background of conference and resulting institutions); Dominick Salvatore, International Economics 642-45 (4th ed. 1993) (discussing Bretton Woods system as gold-exchange standard system for oversight of rules of international trade and finance); Staff of the International Monetary Fund, The Role and Function of the International Monetary Fund (1985) (explaining origin of Bretton Woods system).
9. *See* Frederic S. Mishkin, The Economics of Money Banking and Finance 500-04 (3d ed. 1992) (discussing balance of payments methodology).
10. *See* Salvatore, *supra* note 8, at 1-4 (discussing international economic activity's effect on national economies).
11. *See id.* at 4-6 ("[T]here are many . . . crucial ways in which nations are interdependent, so that economic events in one nation significantly affect other nations (and vice versa).").

and rely upon the conditions for economic growth in world markets, given this interdependent situation.[12]

With the constraints imposed by the worldwide depression, nations came to rely to an ever-increasing extent on the manipulation of the rubrics of international finance and trade to reverse the deterioration of their respective national economies. A few oversimplified examples may suffice to illustrate the techniques of this manipulation.

Assume that domestic suppliers of widgets in Nusquam are not competitive in relation to suppliers of widgets in Erewhon. In Nusquam, a domestically produced widget ("N-widget") is priced at 20 Nusquami Slugs ("S20"). In Erewhon, a domestically produced widget ("E-widget") is priced at 10 Erewhoni Plugs ("P20"). The exchange ratio of Slugs to Plugs is 1:1. Assuming comparable quality between N-widgets and E-widgets and no transaction costs involved in importing E-widgets into Nusquam,[13] E-widgets priced at S10 should outsell N-widgets priced at S20 in the Nusquami market. Correspondingly, N-widgets costing P20 will not sell in the Erewhoni market.[14]

FIGURE 1



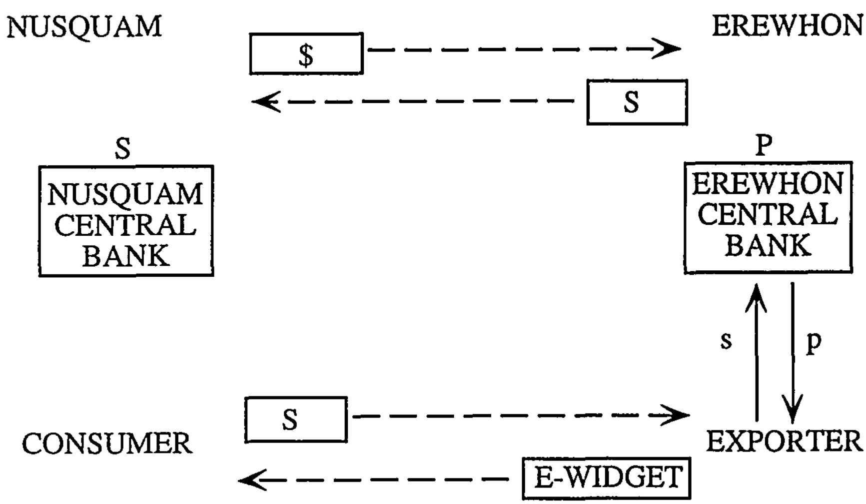
12. Michel Camdessus, Economic Transformation in the Fifteen Republics of the Former U.S.S.R.: A Challenge or an Opportunity for the World? 10 (address to Georgetown University School of Foreign Service, Apr. 15, 1992) ("In this interdependent world, growth in any country—including the United States—is linked to the growth of world markets.").

13. Even assuming reasonable transaction costs, E-widgets are likely to be more competitively priced in the Nusquami market than N-widgets.

14. *See* Figure 1. Again, assuming reasonable transaction costs, the cost of N-widgets in the Erewhoni economy are likely to be comparably affected to the added cost for E-widgets in the Nusquami economy.

In Erewhon, exporters of widgets will ultimately exchange their Slug earnings into Plugs. Thus, the Erewhoni Government will have a charge upon the Nusquami Government for the conversion of Slugs into Plugs, gold, or some other convertible currency.[15]

FIGURE 2



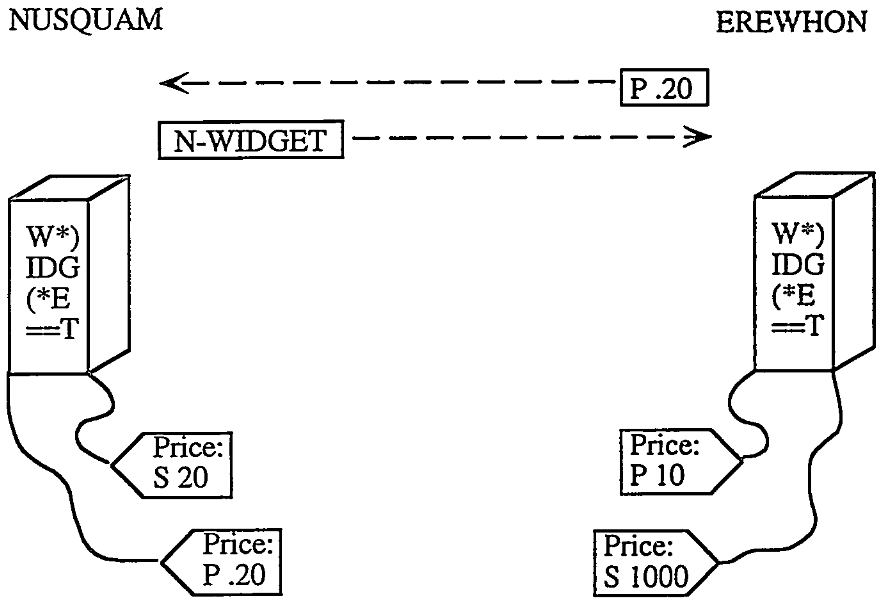
Let us further assume that the domestic widget suppliers are an important sector of the Nusquami economy, which is relatively less developed than that of Erewhon. The effects of this situation on Nusquam, particularly in economically troubled circumstances, will be critical. The Nusquami Government may decide to remedy the situation by devaluing the Slug and thus making the Slug to Plug exchange ratio 100:1.

The result is that N-widgets become more competitive compared to E-widgets. In the Nusquami market, an N-widget still costs S20 while an E-widget now costs S1000. Correspondingly, in the Erewhoni market, an N-widget now costs P.20 while an E-widget still costs P10.[16]Widget suppliers in Nusquam benefit, but widget consumers in Nusquam will now pay at least 100 percent more for widgets. The effect in the Erewhoni economy will be the reverse. Yet, the quality of the goods involved remains unchanged.

The Erewhoni Government is unlikely to remain indifferent to this situation. It may counter by devaluing the Plug, at the very least to restore the S:P exchange parity, but possibly to give an exchange advantage to the Plug over the Slug. One can imagine a downward spiral of successive devaluations. This process destabilizes the economies of both countries

15. *See* Figure 2.
16. *See* Figure 3.

FIGURE 3



S:P = 100:1

and may affect the economies of other nations as well.[17]

Another possible solution available to the Nusquami Government would be to increase the cost of imported goods by establishing import duties. The imposition of a 200 percent duty, for example, would increase the cost of E-widgets in the Nusquami market from S10 to S30, making them uncompetitive with respect to N-widgets still priced at S20. Again, the effect is to increase the cost to Nusquami consumers by at least 100 percent.[18]

Another alternative would be to impose a quota on the importation of E-widgets. By the function of supply and demand, this should raise the price of E-widgets in the Nusquami market and create some increased market share for N-widgets. An extreme version of this would be to bar the importation of E-widgets. Any of these alternatives is likely to prompt a countermove by the Erewhoni Government to limit or exclude

17. This effect becomes even more evident if the Slug to Plug exchange ratio is established indirectly through the pegging of each currency to some other measure of value, for example gold or a convertible currency such as the U.S. dollar. In such a case, the effect of devaluation is immediately and directly visited upon all other national currencies similarly pegged. The adverse economic effects on international trade then spiral downwards in a broader arc.

18. *Cf.* Sylvia Nasar, *The High Price of Protectionism*, N.Y. Times, Nov. 12, 1993, at D1 (discussing cost to consumers of tariffs and other trade barriers).

N-widgets from its domestic market. As in the case of tariffs, non-tariff barriers ("NTBs") to trade such as quotas will tend to push up the price of goods to consumers within the importing country.[19]

In abstract terms, the direct or indirect effects of any of these measures is likely to be negative, either long or short term. Furthermore, if the widget sector is an important component of Nusquami development strategy, these measures may well have the unintended effect of retarding development of the Nusquami economy.

Indeed, the significant adverse effects of such "beggar thy neighbor" policies, both within individual national economies and in the less efficient allocation of resources throughout the international system, informed the approach taken at the Bretton Woods conference. The essential project of the conference was to create an institutional setting in which such predatory, and ultimately self-defeating, policies could be contained or eliminated. The conference established other institutional devices to address problems faced by relatively less developed or less competitive national economies such as Nusquam.

It is against this background that the Bretton Woods system emerged. The Articles of Agreement, or "Charter," of the International Monetary Fund ("IMF") identified several institutional objectives.[20] First, the IMF would promote international cooperation by providing the institutionalized machinery for consultation and collaboration of members on international monetary issues.[21] Second, the IMF would facilitate balanced growth in international trade and thus contribute to higher levels of employment, real income, and the development of productive capacity of members.[22] Third, the IMF would promote exchange stability, orderly exchange arrangements, and facilitate the avoidance of competitive currency depreciation.[23] Fourth, the IMF would foster a multilateral system of payments and transfers for current transactions[24] and would seek to eliminate the use of exchange restrictions that might hinder the growth of world trade.[25] Fifth, the IMF would make convertible financial resources available to member states, on a temporary basis and with

19. In the case of tariff barriers there is at least some offsetting gain to the state treasury from tariff revenues, as well as some minimal reduction in unemployment and welfare benefit costs. *See id.* In the case of NTBs, however, the incremental increase in the cost of the imported goods is captured by the importers and the foreign suppliers, not the state treasury.

20. Articles of Agreement of the International Monetary Fund, 60 Stat. 1401, T.I.A.S. No. 1501, 2 U.N.T.S. 39 (opened for signature and entered into force Dec. 27, 1945), *as amended*, 20 U.S.T. 2775, T.I.A.S. No. 6748 (May 31, 1968; effective July 28, 1969), 29 U.S.T. 2203, T.I.A.S. No. 8937 (Apr. 30, 1976; effective April 1, 1978) [hereinafter IMF Articles].

21. *Id.* art. I, ¶ i.

22. *Id.* art. I, ¶ ii.

23. *Id.* art. I, ¶ iii.

24. On the concept of "current transaction" for these purposes, see *id.* art. XXX(d).

25. *Id.* art. I, ¶ iv.

appropriate safeguards,[26] to permit these states to correct international payment imbalances without resorting to destructive "beggar thy neighbor" techniques.[27] Finally, the IMF would seek to reduce the duration and magnitude of such imbalances.[28]

At the technical level, these objectives were embodied in a number of provisions of the IMF Charter. The IMF was given the authority to supervise a code of conduct for exchange rate policies and restrictions on payments for current account transactions.[29] This authority was intended to eliminate the possibility of predatory rate fluctuations and the rigidity of close adherence to an exchange measure of value such as gold. The Charter required each member to establish an exchange par value for its currency in terms of gold or the United States ("U.S.") dollar as of July 1, 1944.[30] Having done so, the IMF Charter required the member to maintain the market rate of the currency within one percent above or below par.[31] Par value could be changed only under specified conditions and in accordance with specified procedures.[32] Restrictive or discriminatory exchange arrangements, on either a bilateral or regional basis,[33] were to be avoided but members experiencing dislocations as a result of the war were permitted to continue current restrictions on a transitional basis.[34]

Another goal of the IMF was to provide members with financial resources, typically on a short term basis, to assist them in complying with the exchange requirements while trying to correct or avoid trade imbalances.[35] The members' payments, in gold, convertible currencies, and their own currencies, for their assigned subscriptions to the IMF created these resources.[36] Thus, these resources would be available to a member—in the form of "credits" purchased with national currency, rather than as loans[37]—on a short term basis to meet balance of payments

26. Regarding "conditionality" of drawing rights of members, see Edwards, *supra* note 2, at 232-35.

27. *See* IMF Articles, *supra* note 20, art. I, ¶ v.

28. *See id.* art. I, ¶ vi.

29. *See id.* art. IV.

30. *See id.* art. IV, ¶ 1(a).

31. *See id.* art. IV, ¶ 3.

32. *See id.* art. IV, ¶ 5.

33. *See id.* art. VIII, ¶ 3.

34. *See id.*

35. *See id.* art. I, ¶¶ v-vi.

36. *See id.* art. III, ¶ 3 (discussing subscriptions).

37. It is nevertheless common to see such transactions referred to as "borrowings" or "loans." *See, e.g.*, Salvatore, *supra* note 8, at 645 (discussing "borrowing" from IMF). Nevertheless, as a technical matter, member drawings on the IMF resources are "cast in the form of a purchase [of convertible currency by the drawing member] and sale [by the IMF] with a repurchase obligation." Edwards, *supra* note 2, at 223. Nevertheless, in terms of the economic realities of the transaction, it is appropriate to view it as a loan, since the "purchase" is made with the member's own currency, which, from the member's point of view, is not a medium of exchange, and the "repurchase" by the IMF is, in economic reality, a repayment of the proceeds of the original transaction by the member. *Cf.* Michael P. Malloy & James T. Pitts, *Post-Mortem on Retail Repurchase Agreements:*

problems, with repayment of the credits in exchange for the member's currency.[38] Enlarged draws of these credits from successive "tranches" of IMF resources would involve progressively restrictive conditions imposed by the IMF on the member's economic policies.[39]

A second institution emerged from the Bretton Woods conference, the International Bank for Reconstruction and Development, commonly called the World Bank.[40] If the IMF is, in a sense, a central bank of nations that oversees international financial and monetary policy, the World Bank is a public international building and loan society. The member states provide the capital of the World Bank, giving them the right to borrow from the bank for the financing of development projects.[41]

Several institutional objectives guide the World Bank. First, the World Bank is to assist in reconstruction and development in member states' territories by facilitating capital investment for productive purposes.[42] Second, the World Bank is to promote private foreign investment by means of guarantees or participations in loans and other investments made by private investors.[43] Where sufficient private capital is not available, the bank may provide financing for productive purposes out of its own capital, borrowed funds, or other resources.[44] Third, the World Bank is to promote long range balanced growth in international trade and to maintain balance of payments equilibrium by encouraging international investment for the development of members' productive resources.[45] Fourth, the World Bank must, as a basic operating principle, arrange the loans made or guaranteed by it, in relation to international loans from other sources, so that the more useful and urgent projects will be dealt with first.[46] Finally, the World Bank must conduct its operations "with due regard to the effect of international investment on business conditions in the territories of members"[47] and it was also to assist in the smooth transition from a wartime economy to a post-World War II peacetime economy.[48]

Where were the Regulators?, 3 Ann. Rev. Banking L. 89, 102-04 (1984) (arguing that proper characterization of private sale/repurchase agreement is collateralized loan).

38. *See* IMF Articles, *supra* note 20, art. V, ¶ 7.

39. *See id.* art. V. *See generally* Salvatore, *supra* note 8, at 646 (describing progressive "tranches" from which drawing are made and increased supervision and conditions imposed in each succeeding tranche).

40. *See* Articles of Agreement of the International Bank for Reconstruction and Development, opened for signature and entered into force Dec. 7, 1945, 60 Stat. 1440, T.I.A.S. No. 1502, 2 U.N.T.S. 134, *as amended*, 16 U.S.T. 1942, T.I.A.S. No. 5929 (Dec. 17, 1965), Introductory Article [hereinafter IBRD Articles].

41. *See id.* art. II (membership and capital).

42. *See id.* art. I, ¶ i.

43. *See id.* art. I, ¶ ii.

44. *See id.*

45. *See id.* art. I, ¶ iii.

46. *See id.* art. I, ¶ iv.

47. *Id.* art. I, ¶ v.

48. *See id.*

We can detect here an intentional interrelationship between the institutional objectives of the IMF and the World Bank. For example, both institutions have an interest in the development of productive capacity.[49] Both are concerned with promoting exchange stability.[50] The IMF addresses the abuses of the inter-war period through regulation and oversight of exchange practices and provides short term relief for interim problems of disequilibrium. The World Bank addresses nations' underlying developmental concerns by providing direct and indirect assistance without resort to the abuses of the inter-war period.

There was, however, a third perspective to the approach of the Bretton Woods conference to the problems of economic interdependence: transparency of trade. When national trade regulation and barriers to trade are used to advance domestic development by beggaring one's neighbors, efficient allocation of resources is impeded—that is, transparency of national borders for purposes of the transfer of goods and capital is occluded. In economic terms, it matters little whether this occlusion is the result of predatory devaluation of currency or manipulation of trade costs through protectionist trade barriers. Yet the third aspect of the problem, maintaining the transparency of trade, had to be treated if the dangers of the inter-war period were to be avoided.

To some extent, of course, both the IMF and the World Bank reflect a concern with trade in their declared institutional purposes. Each is directed by its charter to facilitate the development of balanced growth in international trade.[51] However, for these institutions, such balanced growth is at best an empirical by-product of their primary regulatory mandates. The assumption of the Bretton Woods conference was that, although the three elements of international economic regulation—finance, development, and trade—were necessarily interrelated, distinct institutions would be created to oversee each element.[52] Hence, a third institutional device was required to address the maintenance of transparency of trade directly.

This third institution was the International Trade Organization ("ITO").[53] A charter for this organization was finally drafted in Havana in 1948,[54] but an increasingly protectionist U.S. Congress repudiated the

49. *Compare* IMF Articles, *supra* note 20, art. I, ¶ ii ("development of . . . productive resources") *with* IBRD Articles, *supra* note 40, art. I, ¶ i ("development of productive facilities"), art. I, ¶ ii ("finance for productive purposes"), art. I, ¶ iii ("development of . . . productive resources").

50. *Compare* IMF Articles, *supra* note 20, art. I, ¶ iii ("promote exchange stability") *with* IBRD Articles, *supra* note 40, art. I, ¶ iii ("maintenance of equilibrium in balances of payments").

51. *Compare* IMF Articles, *supra* note 20, art. I, ¶ ii ("facilitate the expansion and balanced growth of international trade") *with* IBRD Articles, *supra* note 40, art. I, ¶ iii ("promote long-range balanced growth of international trade").

52. *See* Edwards, *supra* note 2, at 5-6.

53. *See id.* at 6.

54. *See* Jackson & Davey, *supra* note 2, at 295.

charter, which failed to achieve implementation.[55] This was, in effect, the first institutional crisis of the Bretton Woods system. The end result was that the General Agreement on Tariffs and Trade ("GATT"),[56] an ostensibly transitional collection of international trade rules formulated in 1947,[57] substituted functionally for what was to have been a fully coordinate institution within the Bretton Woods system.[58]

Certain key provisions of the GATT address various aspects of the beggar-thy-neighbor scenario that occluded the transparency of international trade in the 1930s. For example, states that are contracting parties of the GATT generally must accord "most-favored-nation" treatment to all other contracting parties with respect to customs duties and charges.[59] A related rule generally requires "national treatment" of the product of contracting parties, that is, nondiscriminatory treatment in relation to like domestic products, with respect to internal taxes and other internal charges.[60] The GATT also generally prohibits quotas and similar quantitative restrictions on imports.[61] The GATT subjects export subsidies to regulation and oversight by the contracting parties *en banc*.[62]

Even with such limiting rules in place, transparency of international trade could not be achieved since the contracting parties already had in place broad and significantly restrictive tariff systems applicable to imports of goods into their respective territories. The major affirmative project undertaken by the GATT, therefore, was the progressive elimination of tariffs.[63] This project has continued through seven successive rounds of negotiations[64] and is now confronting the rarified issues of the eighth round, which had sought to extend GATT principles to such previously uncovered areas as trade in services, agricultural products, foreign investment, and intellectual property rights, as well as to improve the GATT's rather cumbersome dispute settlement procedures.[65]

55. *See id.*

56. General Agreement on Tariffs and Trade, 55 U.N.T.S. 194 (1947) (as amended) [hereinafter GATT].

57. *See id.* art. XXIX (relation of GATT to ITO Charter).

58. On the operations of the GATT, see Edwards, *supra* note 2, at 63-68; Salvatore, *supra* note 8, at 272-79.

59. *See* GATT, *supra* note 56, art. I.

60. *See id.* art. III; *see also id.* art. XIII (nondiscriminatory administration of quantitative restrictions on imports and exports); art. XIV (exceptions to nondiscrimination rules).

61. *See id.* art. XI.

62. *See id.* art. XVI. *Cf. id.* art XVIII (rules for governmental assistance to economic development).

63. *See id.* art. II (schedule of initial tariff concessions).

64. *See, e.g.*, Salvatore, *supra* note 8, at 273-75 (describing seven completed rounds of tariff negotiations).

65. *See id.* at 278-79 (discussing prospects for success of eighth "Uruguay Round").

II. Institutional Crises and Paradigm Shifts

Even in its formative period, the Bretton Woods system of international economic regulation was subjected to an institutional crisis that altered the structure of the system. The refusal of the U.S. Congress to implement the ITO Charter caused a structural realignment in the system. The result was the persistence of the GATT as a curious hybrid, lacking many of the formal characteristics of an "international organization"[66] but nonetheless functioning as a coordinate institution within the system.[67] This Part of the article reviews some of the other past institutional crises that may have caused paradigm shifts in the Bretton Woods system of international economic regulation.

A. *Repudiation by the Eastern Bloc*

While the conference participants contemplated that the Bretton Woods system would be a set of "universal," though specialized institutions, the repudiation of membership by most Eastern Bloc countries, including the Union of Soviet Socialist Republics ("USSR"), robbed the system of the general applicability originally contemplated.[68] Only now, in the aftermath of the political transformation of Central Europe and the political collapse of the USSR, is this distortion of the system being rectified.

B. *Aggressive Use of Exchange Controls*

Despite expectations that exchange controls would have limited utility within the rules of the IMF Charter, the opposite has generally been the case. Exchange controls and exchange arrangements have persisted, despite their ostensibly "transitional nature," under the charter.[69] Further, states have often employed them as economic sanctions.[70] Indeed, states have made attempts to enforce such controls transnationally through provisions of the IMF Charter requiring member deference to such con-

66. *See* Ian Brownlie, Principles of Public International Law 679-81 (3d ed. 1979) (identifying traditional criteria of legal personality in international organizations as permanent associations of states with legal objects and organs, distinction between the organization and its members, and internationally exercisable legal powers).

67. For a discussion of the role of the GATT, see William A. Lovett, *The Current World Trade Agenda: GATT, Regionalism, and Unresolved Asymmetry Problems*, 62 Fordham L. Rev. 2001 (1994).

68. *See, e.g.*, Edwards, *supra* note 2, at 24-25 (discussing varying attitudes of Eastern Bloc countries to IMF prior to collapse of USSR).

69. IMF Articles, *supra* note 20, art. VIII, ¶ 2(a) (prohibition of restrictions on current payments). One stated exception to this prohibition is during periods when the IMF itself is experiencing a scarcity in its holdings of a particular member's currency. *See id.* art. VII, ¶ 3. Another exception is for "transitional arrangements" for exchange restrictions, subject to a requirement of notification to the IMF. *See id.* art. XIV, ¶ 2. A final exception is for supervision by the IMF. *See id.* art. XIV, ¶ 3.

70. *See* Michael P. Malloy, Economic Sanctions and U.S. Trade 594-610 (1990 & 1993 Cum. Supp.) (discussing prevalence of currency restrictions as sanctions and relation between economic sanctions and IMF procedures).

trols where imposed consistent with the charter.[71] Thus, the practice concerning exchange controls under the IMF Charter would not seem consistent with the underlying charter objective of eliminating restrictions on current financial transactions.[72]

C. *1971 Convertibility Crisis*

The U.S. decision in 1971 to devalue the dollar and to refuse to allow redemption of dollars for gold represented the clearest example of an institutional crisis leading to a paradigm shift.[73] The immediate result was that the international monetary system was adrift throughout much of the 1970s and was reformulated by the end of the decade in several very significant ways.

Instead of the system of exchange parities established in the original version of the IMF Charter, a system of "managed floats" was established.[74] In addition, gold and the dollar have largely been replaced as the exchange system "pegs" in favor of the IMF-generated "special drawing right" ("SDR"), which is essentially a measure of value representing the value of a "basket" of currencies designated by the IMF.[75] While this system, to some degree, has made the exchange rate system relatively less stable, the system is also less susceptible to the sort of crisis precipitated by the U.S. action in 1971.

D. *1982 LDC Debt Crisis*

The LDC debt crisis, beginning in 1982 with Mexico's announcement that it would not service its external debt, was and continues to be a major institutional crisis for both the IMF and the World Bank.[76] It remains a crisis—even if we may have become accustomed to living with it. It has heightened interest in the management and oversight of the global banking market, and one may reasonably ask what role the IMF

71. *See* Richard W. Edwards, Jr., *Extraterritorial Application of the U.S. Iranian Assets Control Regulations,* 75 Am. J. Int'l L. 870, 873 (1981); *see also* Gerhard Wegen, *The Practical Implications of Article VIII.2.b.*, 62 Fordham L. Rev. 1931 (1994).

72. *Cf. supra* notes 20-28 and accompanying text (discussing IMF objectives).

73. For a discussion of the background of the President's decision to "close the gold window" and to impose other financial measures, including an import surtax, see United States v. Yoshida Int'l, Inc., 526 F.2d 560 (C.C.P.A. 1975) (upholding President's imposition of the surtax). As Edwards has pointed out, it was not the refusal to redeem dollars for gold, but the accompanying refusal to intervene in the exchange markets to maintain dollar exchange rates within the limits then required by Article IV that constituted a violation of the IMF Charter. *See* Edwards, *supra* note 2, at 497-98.

74. *See* Dominick Salvatore, *The International Monetary System: Past, Present, and Future*, 62 Fordham L. Rev. 1975 (1994).

75. *See* Figure 4, *infra*. On the SDR as the principal reserve asset in the international monetary system, see Edwards, *supra* note 2 at 635-38.

76. On the LDC debt crisis and some regulatory responses to it, see Michael P. Malloy, The Regulation of Banking 952-54 (1992).

should take in regulating this market.[77]

The crisis also precipitated a paradigm shift with respect to the relative

FIGURE 4

SDR Valuation Basket
(As of January 1, 1991)

Currency	Percentage Weight	Amount of Currency Units
U.S. dollar	40	0.572
Deutsch mark	21	0.453
Japanese yen	17	31.8
French franc	11	0.800
Pound sterling	11	0.0812

roles of the IMF and the World Bank. Despite the original expectation that the IMF would be involved in relatively short-term adjustment assistance, while the World Bank would be involved in long-term resource commitments, particularly in support of developmental projects, it may be that the two institutions have drifted into each other's respective areas of concern.[78]

E. *Increasing Prominence of Regionalism*

Cutting away from the universal and generally applicable character of the Bretton Woods system, the increasing prominence of regionalism in international economic arrangements, particularly in the area of international trade, also poses an institutional crisis for the system. Current and proposed regional arrangements do not have the precise symmetrical fit exhibited by the Bretton Woods model of international economic regulation.[79] As these regional approaches continue to gain prominence, they are likely to require a reassessment of some underlying premises of the Bretton Woods system.[80]

77. *See* Stephen T. Zamora, *Regulating the Global Banking Network—What Role (If Any) for the IMF?*, 62 Fordham L. Rev. 1953 (1994).

78. *See* Dominique Carreau, *Why Not Merge the IMF and the World Bank?*, 62 Fordham L. Rev. 1989 (1994). *See also* Cynthia C. Lichtenstein, *Aiding the Transformation of Economies: Has the Fund Become a Development Bank and the World Bank the Fund?*, 62 Fordham L. Rev. 1943 (1994) (discussing institutional interrelationship between IMF and World Bank).

79. *See* Lovett, *supra* note 67, at 2004-12 (discussing problems of asymmetry in international trade).

80. In particular, the objective of transparency of national boundaries with respect to international trade is put into question by regionalization trends. Indeed:

> [t]he trend toward regional integration accelerated in 1992 both among industrial countries and developing countries. This reflected partly a deepening of existing trade arrangements and partly the stalemate in the Uruguay Round [of

III. ECONOMIC TRANSFORMATION OF THE FORMER USSR

We are therefore dealing with a system of international economic regulation that has suffered considerable strains over the past fifty years. Intervening events have partially frustrated or reshaped some of its original objectives. This Part of the article analyzes in more detail a current situation that could lead to an institutional crisis: the economic transformation of the fifteen republics of the former Soviet Union ("FSU").[81]

This crisis invites an obvious question: aside from its sheer size, what is so distinctive about the economic development project represented by the transformation of the FSU republics[82] that creates a potential crisis for the Bretton Woods system? One aspect of particular note here is the geopolitical linkage of the development project. Success of the political transformation of this Cold War nemesis depends, in no small part, on the success of the economic transformation.[83]

A second aspect that distinguishes this project is its challenge to developmental theory. On such a relatively grand scale, with a correspondingly narrower margin of error,[84] assumptions about developmental

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> GATT trade negotiations]—which intensified fears of unilateral defensive trade actions and the need to increase bargaining power vis-a-vis other trading blocs, especially with the advent of the European single market and the North American Trade Agreement.

IMF, Annual Report 16 (1993) [hereinafter 1993 Report].

81. The terminology used to refer to the former republics has varied, but the IMF has lately adopted "FSU" as the operative term. *See, e.g.*, IMF, International Financial Statistics: Supplement on Countries of the Former Soviet Union ix (Supp. Series No. 16, 1993) (presenting microeconomic data and explaining notes pertaining to 14 FSU countries) [hereinafter FSU Supplement].

82. *See, e.g.*, Camdessus, *supra* note 12, at 1 (noting that "magnitude of the problems facing the 15 republics is unprecedented").

83. *See* Jorge Braga de Macedo, *Comments*, *in* Georg Winckler, Central and Eastern Europe Roads to Growth 138 (1992). He writes:

> Economic agents will not change their behavior if they do not believe that the policy environment has also changed irreversibly. . . . [A] move to free trade that is thought to be temporary will be welfare worsening. . . . Self-fulfilling expectations make reforms enduring if they are based on the rule of law. . . .

Id. at 140; *see also* Georg Winckler, *Roads to Growth: A Summary of Main Issues*, *in* Georg Winckler, *supra*, at 4 (noting that "widespread distrust in the success of economic transition may further destabilize politics"); Thomas Friedman, *U.S. Asks Allies to Help Speed I.M.F. Aid to Russia*, N.Y. Times, Feb. 1, 1994, at A6, col. 1 (indicating U.S. concern over political need to support Russian reform efforts with immediate economic assistance).

84. One may think of the margin of error with respect to developmental strategies applied to this project in the following terms: when the instrumentalities of the Bretton Woods System are applied to a developmental project in a national economy of relatively small size, the effects of failure of development presumably have a correspondingly small impact on other "globalized" or interdependent economies. Hence, what is at risk is the economic and social gains of the development target economy, and the incremental economic gain of other interdependent economies. In the case of the FSU republics, however, the potential economic and social gains of the development target economies and the attendant economic gain of other interdependent economies are likely to be of a much greater scale, and hence the lost opportunities and negative economic effects of failure of the developmental project are likely to be significantly greater.

theory underlying the Bretton Woods System are put at risk. Thus, to the extent that these assumptions include the notions that stabilizing exchange rates and exchange rate policies leads to significant positive effects systemically,[85] and that the encouragement and enhancement of private investment are likely to lead to the realization of the policy values of the Bretton Woods System in the development target,[86] the challenge of transforming or reforming the economies of the FSU republics puts these notions to the acid test.

A third aspect that distinguishes this project from others is the practical circumstance that the economic situation in the FSU republics in many significant respects provides almost no economic infrastructure or preexisting practices from which development can proceed. A few examples in this regard may illustrate the point. By Western standards, there are practically no economic instrumentalities from which to build. Exchange rate policies and practices need to be reconstructed almost in their entirety.[87] The legal infrastructure with respect to investment and industrial property ownership has to be created virtually *de novo*.[88] The banking system is, by almost any objective estimation, in a primitive state.[89] This situation creates a radical challenge for development. De-

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85. *See, e.g.*, IMF Articles, *supra* note 20, art. I(iii); *see also* IMF, World Economic Outlook 6 (May 1993) ("The early experience of the former centrally planned economies has already demonstrated the crucially important link between structural reforms, macroeconomic stabilization, and successful economic transformation.") [hereinafter May Outlook].

86. *See, e.g.*, IBRD Articles, *supra* note ?, art. I(ii).

87. *See* FSU Supplement, *supra* note 82, at ix-x (discussing exchange rate policies of FSU republics).

88. *See e.g.*, IMF, World Economic Outlook 48 (October 1992) (discussing recent FSU legislation) [hereinafter October Outlook].

> In general, . . . the establishment of property rights and reform of the legal system [in the FSU republics] to provide an adequate framework for market activity have only just begun, including the removal of the multitude of anticompetitive laws and restrictive practices that have been in place for most of this century. Except in the Baltic states, there is limited knowledge of market-oriented legal systems and no modern legal tradition to draw upon.

Id. The situation has improved very little since October 1992. *See* May Outlook, *supra* note 86, at 64.

> Most countries of the former Soviet Union and Mongolia have begun to put commercial legislation in place, including property, bankruptcy, and antimonopoly laws. But the application of this legal framework has been uneven. Property rights are still inadequate and unclear, with the result that investment and production decisions have been delayed. Monopoly laws have not been enforced[,] and the trade regime is still too distorted to provide much of a check on monopoly power.

Id. This situation is complicated by the intransigence of the Russian foreign debt situation. *See, e.g.*, *Russian Debt Accord Elusive*, N.Y. Times, Oct. 9, 1993, at 8, col. 6; *see also* FSU Supplement, *supra* note 82, at xv (discussing foreign assets and liabilities).

89. *See, e.g.*, Tim Carrington, *Former Soviet Banking System Needs Big Dose of Resolution Trust Medicine*, Wall St. J., Nov. 29, 1993, at A8, col. 3 (discussing critical condition of the banking system in the FSU republics); *see also* FSU Supplement, *supra* note 82, at x-xi (discussing current condition of banking systems in FSU republics and difficulty of analyzing money and banking statistical data in light of that condition); 1993

velopment must not simply aid in the building of an economy but must assist in the creation of the factual predicates from which development might emerge.

A. *The Geopolitical Linkage*

The geopolitical implications of the multilateral response to development in the FSU republics raises the stakes considerably. Recently, increased political turmoil in Russia has resulted, in no small part, from the perceived failure of developmental objectives.[90] What may be even more disturbing is the recent dismissal and indictment of the reform-minded president of the Republic of Belarus, a state that would otherwise be a prime candidate for development,[91] apparently resulting from similar public dissatisfaction with the slow pace of development.[92] A decisive failure of developmental efforts in the FSU republics would almost undoubtedly result in a terrible *revanchisme* of autocratic rule and possibly a resurgence of Russian expansionism.[93]

Report, *supra* note 81, at 50 (finding weak Latvian banking system an "area of major concern").

Some efforts have already been undertaken in this regard, but with uncertain results at this stage. *See generally* Inna Vysman, *The New Banking Legislation in Russia: Theoretical Adequacy, Practical Difficulties, and Potential Solutions*, 62 Fordham L. Rev. 265 (1993) (discussing practical shortcomings of new bank regulatory initiatives in Russia). The critical underdevelopment of the banking system in the FSU republics is one of the major contributing factors to the slow pace of economic development.

> Perhaps the major reason that firms extend credit [to trading partners] through arrears is that failure to do so would disrupt supplies or shipments of inputs needed for production, resulting in closure. Normally, a creditworthy firm could fill the gap through the banking system. In the former Soviet Union, however, the financial system is still underdeveloped. In any case, it would be difficult for a bank (or another firm) to determine an enterprise's creditworthiness because of the rudimentary accounting system, the absence of a market to evaluate assets, the presence of soft budget constraints, and the possibility of a government bailout.

May Outlook, *supra* note 86, at 61-62.

90. *See, e.g.*, Steven Erlanger, *Finance Minister Shuns Yeltsin Plea and Quits Cabinet*, N.Y. Times, Jan. 27, 1994, at A1, col. 6 (discussing political struggle within Russian cabinet over pace and direction of economic reform); Steven Greenhouse, *I.M.F. Meeting Backs Yeltsin, With a Caveat*, N.Y. Times, Sept. 27, 1993, at A11, col. 4 (indicating Western finance ministers' support Yeltsin in his confrontation with Russian Parliament but with strong demand for economic reforms).

91. *See* FSU Supplement, *supra* note 82, at 10-13 (financial statistics on Belarus development); *see also* Douglas Jehl, *Clinton Promises Help for Belarus Before Changing Focus to Mideast*, N.Y. Times, Jan. 16, 1994, at 1, col. 3 (proposing economic aid for Belarus).

92. *See Belarus Parliament Ousts Leader*, N.Y. Times, Jan. 27, 1994, at A6, col. 1 (reporting ouster of Stanislav Shushkevich, Chairman of Parliament). *But cf.* Steven Erlanger, *Belarus Says Aide's Ouster Won't Stop Reform*, N.Y. Times, Jan. 28, 1994, at A6, col. 4 (reporting Belarussian Foreign Ministry insistence that ouster would not alter commitment to market economy).

93. *See, e.g.*, Adi Ignatius, *New Shade of Red: With Russian Reform Waning, Communists Mount a Comeback*, Wall St. J., Jan. 27, 1994, at 1, col. 1 (discussing resurgence of Communist Party in light of continuing economic hardships).

B. *Challenges to Development Theory*

The wide disparity among the relative stages of economic development of the FSU republics poses yet another problem.[94] It complicates the task of creating a multilateral response to the developmental problems of the FSU.[95] For instance, among the Baltic states, Estonia has so far successfully proceeded with its economic stabilization and reform program, achieving in 1993 "substantial moderation in the rate of inflation, growing confidence in the [Estonian currency], and the rapid growth of trade with industrial countries."[96] Similarly, Latvia has experienced marked economic improvement, based largely upon "strong monetary discipline, underpinned by a prudent fiscal policy and supporting incomes policy measures."[97] Only Lithuania appeared to be subject to substantial economic setbacks by early 1993.[98]

Intrusive exchange practices and inadequate payments systems continue to impede trade liberalization in the other FSU republics.[99] Russia, in particular, is beset with significant impediments to economic development.[100] Other states, such as Armenia,[101] Azerbaijan,[102] and

94. *See* 1993 Report, *supra* note 81, at 15.

> Progress in reform of trade and payments regimes has varied in the Baltic states and the states of the former Soviet Union. The Baltic states achieved the greatest progress in reorienting their policies toward market mechanisms, as part of comprehensive economic reforms supported by the use of Fund resources.

Id. Other states of the former Soviet Union have experienced greater difficulties in reorienting their trade regimes.

95. *See, e.g.*, Camdessus, *supra* note 12, at 3.

> This diversity [of resources among the FSU republics] requires that the reform programs reflect the republics' special circumstances. They need to develop a diversified strategy that responds to their own circumstances.

Id. The disparities in natural resources and other physical circumstances likewise complicates matters. Thus, some FSU republics are resource-rich. *See, e.g.*, *Turkmenistan Oil Deal*, N.Y. Times, Nov. 17, 1993, at D11, col. 6 (reporting Occidental Petroleum Corporation's successful bid to explore and develop oil deposits). Others are relatively resource-scarce. *See, e.g.*, Erlanger, *supra* note 93, at A6, col. 6 (noting Belarussian energy dependency on Russia). These FSU republics, however, may have other advantages such as strategic location along transportation and supply routes. *See, e.g.*, Jehl, *supra* note 92, at 10, col. 1 (providing map of Belarus indicating major regional railroad corridor).

96. *See* 1993 Report, *supra* note 81, at 49.

97. *Id.*

98. *See id.* at 50.

99. *See, e.g.*, *id.* at 15 (noting that FSU republics "have adopted a number of transitional payments arrangements that have posed an obstacle to effective import liberalization"). National systems for international trade and customs practices are also very uncertain among the FSU republics. *See* FSU Supplement, *supra* note 82, at xii.

100. The IMF noted several problems, as of April 1993, including "the difficult conditions under which the [Russian] authorities had sought to implement stabilization policies and transform the economic system; [and] the dangers of financial instability, which was threatening to undermine the thrust of the entire [economic] reform program . . . ." *See* 1993 Report, *supra* note 81, at 50.

101. *See id.* at 51 (noting "the desperate economic situation . . . and the unprecedented decline in living standards").

102. *See id.* (noting "recent deterioration, particularly in budget performance").

Moldova[103] are in an especially perilous condition, in part because of internal violence.[104]

C. *The Economic Infrastructure*

Trade liberalization of central and eastern European economies in transition has been a particular focus of concern in recent international assessments of the situation in that area of the world.[105] This aspect of development has exposed some of the shortcomings in the economic infrastructures of these economies. For example, "difficulties in developing an adequate domestic revenue base and effective tax collection system are emerging as constraints on the sustainability of trade liberalization."[106] Furthermore, the economic situations within and among many of the FSU republics, excluding the Baltic states, have actually deteriorated in a number of significant ways that are likely to make development even more difficult to effect.[107]

IV. Economic Transformation and the Vindication of the Original Values of Bretton Woods

The challenge presented by the ongoing economic transformation of the FSU republics need not be viewed as a potential paradigm shift—not a challenge to the presuppositions that underlie the current Bretton Woods institutions—but rather, these may represent an opportunity to vindicate the objectives of those institutions. Whether those objectives are to be vindicated may depend, however, on the extent to which the Bretton Woods institutions, particularly the IMF, are willing to assume a proactive and primary role in the economic transformation. To date, there are reasons to doubt whether the institutions are willing to undertake such a role.

As late as April 1992, the Managing Director of the IMF delivered a formal address that seemed to commend the FSU republics to their own devices.[108] He repeatedly emphasized:

> Now comes the question of what [the economic transformation] will

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103. *See id.* at 52 (noting "a precipitous decline in GDP, financial imbalances, rapid inflation, a severe deterioration in . . . terms of trade, and an acute foreign exchange shortage").

104. *See* Camdessus, *supra* note 12, at 2.

105. *See, e.g.*, 1993 Report, *supra* note 81, at 15 (discussing global economy and trade liberalization in economies in transition).

106. *Id.*

107. *See id.* This report noted:

> Trade among the states of the former Soviet Union continued to decline sharply during 1992 and early 1993, as did their trade with the rest of the world. This partly reflected, and contributed to, the decline in economic activity across the former Soviet Union. . . . Many of these states have resorted to barter (including barter with countries outside the area of the former Soviet Union) . . . .

Id.

108. *See* Camdessus, *supra* note 12, at 6.

> cost. Let me stress a basic fact. The transformation of the economies of the 15 republics is essentially *their* task. International financial assistance is critical, but it can only be a complement to *their* efforts, *their* savings, *their* investment in infrastructure and in expanding the productive base of the economy. . . . Yes, *they* will do the work. And history shows us that is how economic transformation happens.[109]

Ironically, this pronouncement on economic history contradicts the opening insight of the address. He acknowledged that "[t]he magnitude of the problems facing the 15 republics is unprecedented. The challenge goes far beyond what is generally understood by the concept of economic transformation."[110] How is it then, if the challenge transcends our presupposed notions of economic transformation, that the FSU republics are to be constrained by past experience with economic transformation?

The economic transformation that must occur in the FSU republics is fundamentally different from the problems that ordinarily confront developmental tacticians. It is not a situation calling for concentrated economic adjustment efforts along a continuum of development. Rather, it is a situation requiring a fundamental *reconstruction* of entire societies in all their legal, economic, and physical dimensions. By treating the challenge presented by the FSU republics as simply another, albeit larger, example of economic adjustment, the Managing Director makes it, in broad outline, indistinguishable from all other economic adjustment challenges facing the Bretton Woods institutions. Thus, he observed:

> Because the IMF is a universal institution, we must consider these new demands in a global context and try to reconcile them with the other challenges to the world economy:
>
> - the heavy investments needed in the industrial countries themselves, to support their own growth in the decade ahead;
> - the investment needs of the developing countries, to promote their development, protect the environment, reduce poverty, and complete the job of solving the debt problem . . . .[111]

This homogenization of the varied challenges presented by economic transformation of the FSU republics and other continuing developmental problems is misplaced and dangerous. Without appropriate attention to the preeminent challenge represented by the critical situation in the FSU republics, there exists the very real possibility of fundamental instability in international peace and security surpassing even the pre-transformation period of the Cold War. Furthermore, this undifferentiated approach to current developmental problems subverts a key, original value of the Bretton Woods System: the priority of *reconstruction* over *development*.[112]

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109. *Id.*
110. *Id.* at 1.
111. *Id.* at 7.
112. Compare the IBRD Charter which states:

> The purposes of the Bank [for Reconstruction and Development] are:

The Bretton Woods System presupposed that reconstruction would naturally precede broader development efforts.[113] In the case of the FSU republics, however, that presupposition went seriously awry.[114] In a very real sense, they have existed in a state of suspended animation, never enjoying the post-war reconstruction that revitalized Western Europe. With that suspension now reversed, priority should be given to their reconstruction. Unfortunately, with the relative realignment of the role of the World Bank, originally charged with the reconstruction and development objectives of the System,[115] has caused these functions to apparently fall to the IMF, without the direct application of the World Bank's charter commitment to the priority of reconstruction efforts over developmental projects. This "lowest common denominator" approach to the critical task of economic transformation to the FSU republics may ultimately fail its fundamental purpose.[116] In that case, we may see the time when, economically and possibly politically, the call may go out to "[c]ry *Havoc*, and let slip the dogs of war."[117]

> (i) *To assist in the reconstruction and development of territories of members by facilitating the investment of capital for productive purposes, including the restoration of economies destroyed or disrupted by war, the reconversion of productive facilities to peacetime needs* and the encouragement of the development of productive facilities and resources in less developed countries.
>
> . . . .
>
> (v) To conduct its operations with due regard to the effect of international investment on business conditions in the territories of members and, *in the immediate post-war years, to assist in bringing about a smooth transition from a wartime to a peacetime economy.*

IBRD Articles, *supra* note ?, art. I, ¶ ¶ i, v (emphasis added).

113. *See id.*

114. *See supra* notes 68-69 and accompanying text (describing Eastern Bloc repudiation of Bretton Woods System).

115. *See supra* note 79 and accompanying text.

116. The IMF has already been subjected to growing criticism over its handling of the economic transformation of the FSU republics. *See, e.g.*, Friedman, *supra* note 84, at A6 (discussing U.S. concern over delays in IMF assistance to Russia).

117. William Shakespeare, Julius Caesar, Act III, at 273 (A.L. Rowse ed., 1978).