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David J. Bederman

The Bank for International Settlements and the Debt Crisis: A New Role for the Central Bankers' Bank?

by
David J. Bederman†

INTRODUCTION

It began quietly, of course. What started as the lending spree of the last decade became the debt crisis of the next. The moment which marked the transition between the two nearly went unnoticed at the time. It could have been that last ill-advised loan by a bank desperate to salvage its balance sheet. Or perhaps it was the gentle downturn in the leading indicators of prosperity: declining productivity, shrinking credit, rising prices, lost jobs. New barriers to the international trade in goods and services were, no doubt, also a factor. But the enormous sovereign debt, having long accrued by the necessity of reconstruction and development, was undoubtedly the most visible cause of the critical situation.

This could be a memoir of 1981—or of 1931. While there are unquestionable differences in the genesis of the global depression of the 1930s and today's debt crisis,[1] enough similarities remain to explore the peculiar role of the one international financial institution that experienced both events: the Bank for International Settlements [hereinafter BIS or Bank].

The Bank, headquartered in Basel, Switzerland, was originally established to promote cooperation among the central banks of member nations. In so doing, the Bank's key function was to assist in the resolution of what was then the most pressing issue in international finance, the management and servicing of German reparations and Allied debts incurred as a result of the First World War.

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† A.B. Princeton, 1983; M.Sc. University of London, 1984; J.D. University of Virginia, 1987.

1. An exhaustive description of economic conditions today and fifty years ago is not possible here. *See generally* BANK FOR INTERNATIONAL SETTLEMENTS, FIRST ANNUAL REPORT (1931) [hereinafter BIS Ann. Rep.](a very careful assessment of what was considered to be the nadir year for finance in Depression Europe); W. ESKRIDGE, DANCE ALONG THE PRECIPICE 3-25 (1985) (a collection of essays, some of which treat the origins of the current debt crisis); Dell, *Crisis Management and the International Debt Crisis*, 40 INT'L J. 655 (1985) (an institutional history).

Today, the BIS has become the central bank of central banks. Although originally established by the governments of the United Kingdom, France, Belgium, Germany, Italy, Japan, and Switzerland,[2] the Bank now represents the interests of nearly all of the world's central bank institutions, and manages a significant share of their reserves.[3] Moreover, the BIS serves as a forum of cooperation among these entities. Despite this large sphere of influence, the BIS has been a reluctant actor in solving the world's debt crisis. The BIS, in this respect, has been described as mysterious and aloof.[4] Its directors and managers prefer to avoid publicity.[5]

This article examines how the Bank, given its structural and international legal character, can assume an important institutional role in the resolution of the current debt problem. Part I surveys the formative period of the BIS, placing special emphasis on the planning and formation of its constituent instruments, the BIS's solutions to the financial crisis of the period, and BIS decision-making after the Depression and the Second World War. Part II examines the Bank's activities in the early 1980s. During this time, the Bank vigorously arranged short-term "bridge" loans for sovereign governments on the verge of default. Part III examines the Bank's subsequent decision to retreat from this role and suggests three functions the BIS can offer central banks and governments to ease the current debt crisis. First, the BIS can promote central bank cooperation by expanding upon its already existing role in setting standards for debt exposures and monitoring international monetary flows. Second, the BIS can serve as a trustee for the receipt of debt payments, arguably the Bank's original *raison d'être*. Third, the BIS can establish itself as a lender of last resort. This third function may be an elusive and even undesirable goal. Not only are there significant institutional problems associated with the BIS assuming this function, but such a role might infringe on the mandates of other organizations.

It must be remembered that, in looking at proposals for expanding the competence of the BIS, it is first and foremost, a *bank*. No measure of legal legerdemain can change this essential characteristic of this unique international institution.

2. Convention Respecting the Bank for International Settlements, Jan. 20, 1930, 104 L.N.T.S. 441, *reprinted in* 24 AM. J. INT'L L. SUPP. 323 (1930) [hereinafter BIS Convention]. *See also infra* note 34 and accompanying text.

3. One authority estimates that the Bank for International Settlements [hereinafter BIS or Bank] manages ten percent of the world's official reserves. *See* Campbell, *The Bank for International Settlements — Out of the Shadows and into the Fray?*, in THE INTERNATIONAL DEBT PROBLEM AND ITS IMPACT ON FINANCE AND TRADE 27, 28 n.3 (Practicing Law Institute ed. 1983).

4. *See As Safe as the BIS*, ECONOMIST, Sept. 22, 1984, at 50 (Survey). *See also* Campbell, *supra* note 3, at 27.

5. *See As Safe as the BIS*, *supra* note 4 (noting that the former governor of the Bank of England was nearly knocked down by a Basel tram "as he scurried away from waiting reporters"); Wall St. J., Dec. 15, 1982, at 35, col. 2 (describing how central bankers attending BIS meetings slipped in and out an unassuming and unmarked door next to a pastry shop).

I.
THE DEBT CRISIS OF 1930 AND THE EARLY YEARS OF THE BANK

To analyze the importance of the BIS in today's debt crisis, it is first necessary to understand the background, structure and early activities of the Bank.

A. Origins

The World War I reparations problem set the stage for the entry of the BIS. During the 1920s, sovereign government debt consisted almost entirely of war debts. The Treaty of Versailles compelled Germany to make huge reparations payments.[6] The Allied nations had to repay the amounts they had borrowed from Great Britain and the United States to finance their war efforts.[7] This widespread debt wreaked havoc on international exchange rates, devaluing the Reichsmark in particular. The Versailles reparations plan further exacerbated Germany's indebtedness by requiring the Germans to pay off their debts by converting their Reichsmarks into other currencies.[8] Germany's only possible sources for paying its reparations were trifling reserves, foreign exchange earned in exports, and borrowing.[9] Of these alternatives, generating foreign exchange by exports was the most sensible. This alternative, however, was frustrated by the Allied demands, which stripped Germany of its colonies, eliminated its internal system of tariffs and duties, and placed intolerable burdens on its coal and steel industry.[10] The gold mark steadily lost its value until Germany defaulted on all cash payments in August 1922.[11]

The Dawes Plan of 1924 was the first coordinated international response to the problem of Germany's continued indebtedness. The Plan scaled down

6. *See* Treaty of Peace between the Allied and Associated Powers and Germany, June 28, 1919, arts. 231-44, Annexes I-VII, 1919 Gr. Brit. T.S. 4 (Cmnd. 153), 225 Parry's T.S. 188 [hereinafter Versailles Treaty] (establishing the German obligation to pay reparations and creating a Reparations Commission to enforce this action). These reparations ultimately amounted to over 225 billion gold marks, or around 20 billion U.S. dollars in 1920. *See* G. PAPI, THE FIRST TWENTY YEARS OF THE BANK FOR INTERNATIONAL SETTLEMENTS 21 (1951). *See generally* H. MOULTON, THE REPARATIONS PLAN (1924) (contemporaneous analysis of the reparations plan).

7. The war debts of the major Allied powers, particularly those of France, Russia, and Belgium, rivalled Germany's reparations. Europe's debt to America alone amounted to over $3.5 billion. G. PAPI, *supra* note 6, at 25 (citing CHASE ECONOMIC BULLETIN of Oct. 5, 1920).

8. *See* P. EINZIG, THE BANK FOR INTERNATIONAL SETTLEMENTS 27 (1930).

9. *See* J. KEYNES, THE ECONOMIC CONSEQUENCES OF THE PEACE (1919) (a famous critique of the reparations plan).

10. Versailles Treaty, *supra* note 6, arts. 118-58, 248-75. *See* J. KEYNES, A REVISION OF THE TREATY (1922) (calling for changes in the reparations regime when it became apparent that Germany would be unable to service its debt in the ways that Keynes had anticipated three years earlier).

11. H. SCHLOSS, THE BANK FOR INTERNATIONAL SETTLEMENTS 25 (1958). The Allied governments thereafter actually occupied the Ruhr region in Germany as a sanction for Germany's willful default. *See* G. PAPI, *supra* note 6, at 30.

Germany's annual reparations payments, continued the supervision of various aspects of German economic life (including the railway and banking systems), and offered a loan of 800 million gold marks to stabilize the currency.[12] The loan float was the key feature of the Plan, for it restored the confidence of foreign investors and triggered an unprecedented flow of foreign investment into Germany.[13] As long as foreign investment in Germany remained at high levels, Germany could meet its debt payments. The loan float thus averted a crisis by making management of Germany's debt unnecessary. It was not until 1929, when Germany's external borrowing was once again checked, that the loan float became ineffective in securing Germany's financial health.

The Young Plan of 1929 was proposed next to combat the downward spiral to default which once again shook Germany's financial stability. In February 1929, a new Committee of Experts, appointed by interested states and chaired by Owen D. Young, the American industrialist, political advisor, and diplomat,[14] met in Paris to consider solutions to the most pressing problems of this latest phase of the debt crisis. These problems included the adverse effects on exchange rates caused by the reparations transfers, growing trade protection, and the use of "commercialization" (flotation of bonds) and deliveries in kind to service the debt.[15] Proposals to solve these problems reflected the conflicting interests of the states involved and thus encountered support from some nations and opposition from others.[16] The Young Plan as adopted was nevertheless successful in reducing the size of the reparation amounts, rationalizing their payment schedule, and partially funding Germany's annual reparations payments through an additional round of international loans.[17]

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12. *See* Reports of the Expert Committees appointed by the Reparations Commission [hereinafter Dawes Report], Gr. Brit. Cmnd. 2105, 27 Accounts and Papers, State Papers (1924). Payment on this debt was to be made by increasing annuities financed by charges to railways and industry, taxes on transport, and disbursements from the Reich budget. *See* G. PAPI, *supra* note 6, at 42-44.

13. *See* P. EINZIG, *supra* note 8, at 27.

14. *See* DICTIONARY OF AMERICAN BIOGRAPHY 808-11 (J. Garraty ed. 7th Supp. 1981). Young believed that the creation of the BIS might be "the most constructive job done in our generation." *Id.* at 810.

15. *See* The Times (London), Mar. 5, 1929, at 15 (contemporaneous report of the meeting's agenda).

16. One contemporaneous observer noted:

> The desire of Germany to throw on the creditor nations the responsibility for exchange stability was in contrast to the wishes of the creditors to have payments similar to non-political international obligations. The idea of commercializing payments would make the German hope of later downward revision [of reparation amounts] less attainable, and would serve the interest of the French in that Germany could not default without financial suicide. Deliveries in kind were an aid to German payment, but were contrary to the interest of English export trade.

E. DULLES, THE BANK FOR INTERNATIONAL SETTLEMENTS AT WORK 5-6 (1932).

17. Under the Young Plan, Germany would pay 37 annuities totalling 2.05 billion gold marks (1.9 billion for the original reparations plus O.6 billion for service on the Dawes Plan), 19 annuities averaging 1.6 billion, and three annuities averaging 900 million gold marks. *See* Report

The idea for creating a bank for international settlements originated in the negotiation of the Young Plan. Although for centuries there had been proposals for an "international bank,"[18] plans for concrete central bank cooperation accelerated after the Great War.[19] Economists, such as John Maynard Keynes, had expansive visions for a "Supernational Currency Authority" that would provide the much needed exchange stabilization.[20] Other commentators warned against raising expectations about the Bank's potential activities too high.[21]

In truth, the framers of the Young Plan had only modest intentions for the new financial institution. The Bank would be commercial in character and independent of political influence.[22] It would primarily act as trustee or agent for the governments participating in the Young Plan's financing arrangements for war debts and reparations.[23] The essential rationale for the Bank was thus to depoliticize debt payments and to structure them in such a way that they could be made from income generated by existing international trade and investment.[24]

During the year between the adoption of the Young Plan in June 1929 and the foundation of the BIS, the debt crisis intensified. German exchange rates plummeted.[25] France and Germany bickered over payments scheduling

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to the Committee of Experts on Reparations, June 7, 1929, Gr. Brit. Cmnd. 3343, 17 Reports of Commissioners, at 16-19 (1929) [hereinafter Young Plan]; G. PAPI, *supra* note 6, at 52 n.12. *See also* H. SCHLOSS, *supra* note 11, at 28-29 (noting goal of reducing German reparations without also reducing Allied war debts). The Young proposal was also referred to as the "New Plan."

18. *See, e.g.*, H. SCHLOSS, *supra* note 11, at 3-4 (describing plans for a "Christian Bank" in Geneva in 1675 and proposals to the League of Nations in the early 1920s).

19. *See* Recommendations of the International Economic Conference, Genoa, Gr. Brit. Cmnd. 1650, 23 Accounts & Papers State Papers (1922) (resolutions 3 and 12 called for central bank cooperation to regulate credit). In 1933, the World Economic Conference in London repeated this call and suggested that the BIS would be an appropriate venue for that activity. *See* BIS Fourth Ann. Rep. 10 (1934). *See also* H. SCHLOSS, *supra* note 11, at 7-24 (detailing instances of actual central bank cooperation in the nineteenth century); P. EINZIG, *supra* note 8, at 11-24.

20. R. HARROD, THE LIFE OF JOHN MAYNARD KEYNES 460 (ed. 1971).

21. One scholar wrote of Keynes' proposal: "The idea is magnificent, but it is not banking." P. EINZIG, *supra* note 8, at 6.

22. Young Plan, *supra* note 17, at 10-14.

23. *Id.* at 11-14.

24. *See* E. DULLES, *supra* note 16, at 11. But the motivations of some of the parties may have been less congenial. French and German intentions were characterized in this way:

> The French wanted [the BIS] because they hoped it would help them mobilize their share of the German indemnity, that is, to substitute progressively a debt by Germany to private investors in all countries for a debt to the French Government. The Germans wanted it because they hoped it could help them in bringing about the necessary expansion of their export trade.

A. PIGOU & D. ROBERTSON, ECONOMIC ESSAYS AND ADDRESSES 207 (1931). Some other scholars were concerned that the Bank could promote inflationary tendencies in world markets. *See* P. EINZIG, *supra* note 8, Chapters IX - X.

25. *See* G. PAPI, *supra* note 6, at 55-60.

and sanctions.[26] The Reichsbank even threatened not to cooperate in founding the Bank; but the Reichsbank later withdrew its objection when it became apparent that its creditors would simply proceed without it.[27]

The organizational structure of the BIS was decided in Baden-Baden in October 1929 and later in The Hague in January 1930.[28] The January 1930 Hague Conference adopted the fourteen international agreements used to bring the Young Plan into force, including the Bank's constituent documents.[29] The central document was the Reparations Agreement with Germany,[30] including Annex VIII, which contained a Trust Agreement[31] authorizing the BIS to carry out the Young Plan.[32] The Reparations Agreement also established a procedure for resolving disputes arising out of the Plan's execution and the Bank's operation.[33] These instruments legalized the trustee function of the BIS under the Young Plan, but they did not provide for the actual creation of the entity.

The creation of the Bank was accomplished with a Convention signed by the major parties to the Young Plan (Germany, Belgium, France, Great Britain, Italy, and Japan) and the government of Switzerland.[34] The Charter[35]

26. *See* H. SCHLOSS, *supra* note 11, at 32-33.

27. The Reichsbank apparently feared that the BIS was being established to exercise the same extraordinary control over the German economy that the former Reparations Commission, created by the Versailles Treaty, *supra* note 6, art. 233, Annexes II and IV, had exercised. *See* E. DULLES, *supra* note 16, at 34.

28. *See*, H. SCHLOSS, *supra* note 11, at 32-36.

29. *See* E. DULLES, *supra* note 16, at 35.

30. Reparations Agreement with Germany, Jan. 20, 1930, art. 6, 104 L.N.T.S. 244, Gr. Brit. Cmnd. 3484, at 18-27, *reprinted in* 24 AM. J. INT'L L. SUPP. 262 (1930) [hereinafter Reparations Agreement].

31. Reparations Agreement with Germany, Jan. 20, 1930, Annex VIII, Trust Agreement, 104 L.N.T.S. 328, Gr. Brit. Cmnd. 3484, at 68-79, *reprinted in* 24 AM. J. INT'L L. SUPP. 284 (1930) [hereinafter Trust Agreement].

32. This form of trust agreement (*contrat de mandat*) appointed the BIS the joint and sole trustee of the creditor governments. Simons & Radicati, *A Trustee in Continental Europe: The Experience of the Bank for International Settlements*, 30 NETH. INT'L L. REV. 330, 332 (1983). The Bank also held the German government's certificate of debt, together with the annuity coupons due under the Young Plan. Trust Agreement, *supra* note 31, art. 2, para. b. Article 3 provided a mechanism to "smooth" payments in Reichsmarks given prevailing exchange conditions. A provision for postponement of the annuity payments was also included. *Id.* art. 11.

33. Reparations Agreement, *supra* note 30, art. 15. For the effect of this provision on the international legal character of the Bank, *see infra* notes 50-51 and accompanying text.

34. BIS Convention, *supra* note 2. Conspicuously absent was the United States, which did not want to participate officially in an institution whose primary purpose was the management of German reparations. It might be recalled that the United States was not a party to the Versailles Treaty, *supra* note 6, which had imposed these conditions on Germany. The United States also did not officially participate in the Young Plan conferences. *See* S. DOC. NO. 187, 71st Cong., 2d Sess., exhibit B (1929) (the full text of Secretary of State Stimson's rejection of participation in the BIS); H. SCHLOSS, *supra* note 11, at 27; E. DULLES, *supra* note 16, at 83 (citing May 16, 1929 State Department communiqué); New York Times, May 17, 1929, at 3, col. 1. For more on this fateful decision, *see infra* notes 213-18 and accompanying text.

35. Constituent Charter of the Bank for International Settlements, Jan. 20, 1930, 104 L.N.T.S. 445, *reprinted in* 24 AM. J. INT'L L. SUPP. 324 (1930) [hereinafter BIS Charter].

and the Statutes of the Bank[36] also established the Bank, specifying its capitalization,[37] reserving seats for member States' Central Bank governors on the BIS Board[38] and granting to member States veto power to block BIS market operations within their territory.[39]

The selection of Basel as the site for the Bank was controversial. Some countries preferred London because it had a stronger claim of preeminence in international banking at the time.[40] Though Basel was not a banking center, it was nevertheless a wise choice for the Bank's situs, particularly considering Switzerland's neutrality in the Second World War.[41] Moreover, as discussed in the next section, it made no difference legally where the BIS was located since the Convention effectively prevented any interference by the host state.[42]

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36. Statutes of the Bank for International Settlements, 104 L.N.T.S. 449, Gr. Brit. Cmnd. 3484, at 113-28, *reprinted in* 24 AM. J. INT'L L. SUPP. 326 (1930) [hereinafter BIS Statutes].

37. *See* BIS Statutes, *supra* note 36. The authorized capital was set at 500 million Swiss gold francs, divided into 200,000 equal shares. *Id.* art. 5. The subscription was divided into equal parts between the central banks of Belgium, Britain, France, Germany, and Italy, as well as two banking consortiums in Japan and the United States (J.P. Morgan & Company, The First National Bank of New York, and the First National Bank of Chicago). *Id.* art. 6.

Additional shares were offered to the original subscribers. *Id.* art. 7. Since the United States never participated in the BIS, its additional shares were marketed publicly and are still traded today. *See A Solid Gold Cadillac Among Bank Stocks*, FORTUNE, Mar. 31, 1986, at 145 (appraising the value of BIS bank shares).

38. Governance for the Bank is vested in its Board. BIS Statutes, *supra* note 36, art. 27. The original BIS Statutes contemplated a 25-member board composed of: (1) the governors of the central banks of Belgium, France, Great Britain, Italy, Japan, and the United States; (2) another person from each of these countries (two from France and Germany during the operation of the Young Plan); and (3) up to nine members nominated by the governors of the other central banks holding BIS shares. *Id.* art. 28.

Even though the United States declined its official seats on the Board in 1930, Americans were co-opted in the first years of the Bank, and two served as its chairman and president until 1935. *See* H. SCHLOSS, *supra* note 11, at 145. Japan was voluntarily stripped of its seats on the Board after World War II. *See* Treaty of Peace between Japan and the Allied Powers, Sept. 8, 1951, arts. 8 & 16, 3 U.S.T. 3169, T.I.A.S. No. 2490, 136 U.N.T.S. 45; 1 A. PEASLEE, INTERNATIONAL GOVERNMENTAL ORGANIZATIONS 66 n. 2 (rev. 2d ed. 1961) (citing Swiss announcement of Jan. 8, 1953 concerning Japanese renunciation of rights). Today, the Board has thirteen members, with only three co-opted members (usually the central bank governors of Switzerland, Sweden, and the Netherlands). *See* BIS Fifty-sixth Ann. Rep., back cover (1986).

The Board elects a president and chairman. BIS Statutes, *supra* note 36, art. 39. But by a 1937 amendment to the BIS Statutes these positions need not be vested in the same person. *See* H. SCHLOSS, *supra* note 11, at 42.

39. BIS Statutes, *supra* note 36, art. 20. Additionally, the central bank governors must give their assent to any amendment of the essential provisions of the BIS Statutes. *Id.* art. 60. *See also* E. DULLES, *supra* note 16, at 74-75.

40. *See* P. EINZIG, *supra* note 8, at 62-73.

41. *See infra* notes 79-80 and accompanying text.

42. *See* BIS Convention, *supra* note 2, art. 1 "Switzerland undertakes to grant . . . the following constituent charter having force of law: not to abrogate this charter, not to amend or add to it. . . ." *Id.*

B. Legal Character

The legal status of the Bank was initially unclear. Contemporary writers immediately noted its *sui generis* character: the BIS had an "international basis" but was also a creature of Swiss law.[43] Because of its unusual legal personality, there were extraordinary problems concerning the BIS's immunity from process, as well as regulatory authority over its commercial activities.

The Young Plan unquestionably contemplated an international institution that would owe "no single fiscal allegiance" to any nation,[44] although mention of the Bank's international legal personality was later dropped from its constituent instruments.[45] Yet its founders intended that the Bank would be "assimilated to ordinary commercial and financial practice" and would be a "useful instrument for opening up new fields of commerce, of supply and of demand."[46] It would be a profit-making entity.[47] In short, it was intended as a bank.

Only a few questions concerning the Bank's legal status were resolved at the time of its founding in 1930. Its constituent instruments did, however, resolve the question of whether or not the BIS had immunity from process by allowing the Bank to sue and be sued in municipal courts for cases arising from its commercial activities.[48] In this sense, the BIS was not an extraterritorial entity.[49]

There was also the issue of what law governed the Bank's operations, particularly in its execution of the Trust Agreement. Some scholars argued that because of the international arbitration provisions contained in the Reparations Agreement, BIS Convention, and Constituent Charter,[50] the

43. *See* E. DULLES, *supra* note 16, at 68; Williams, *The Legal Character of the Bank for International Settlements*, 24 AM. J. INT'L L. 665, 667-69 (1930).

44. Young Plan, *supra* note 17, at 12.

45. *See* Reparations Agreement, *supra* note 30, art. 6 (recognition of the "corporate existence" of the Bank). The original language of article 6 recognized the BIS as an "international body corporate" (*de personne juridique internationale*). *See* Williams, *supra* note 43, at 670-71.

46. Young Plan, *supra* note 17, at 10 & 11.

47. BIS Statutes, *supra* note 36, art. 53. But the provisions of this clause guide the very conservative dividend policy of the Bank. Only twelve percent of net profits are ever allowable as dividends. *Id.* art. 53, para. b. and c. Six percent is the rule, however. *Id.* art. 53, para. b. The remainder of profits inure to the benefit of the creditor governments under the Young Plan. *Id.* art. 53, para. e.

48. BIS Statutes, *supra* note 36, art. 57.

49. Hudson, *The Bank for International Settlements*, 24 AM. J. INT'L L. 561, 566 (1930) (noting that Bank officials have no diplomatic immunities, even though the salaries of non-Swiss officers will not be taxed).

50. *See* Reparations Agreement, *supra* note 30, art. 15 (establishing the arbitration procedure). The Arbitral Tribunal consists of five members: an American (the chairman), two nationals of states neutral in World War One, a German, and a national of a state-creditor of Germany (most likely, France). *Id.* art. 15, paras. 1 & 2. Judges *ad hoc* may also be appointed. *Id.* art. 15, para. 3. The Reparations Agreement also provided that disputes about the Tribunal's jurisdiction were to be referred to the Permanent Court of International Justice. The Rules of Procedure

legal authority for the Bank's activities was "internationalized."[51] Thus, in their view, public international law was the applicable law. Other scholars suggested that while the BIS and its correspondents (member central banks and the Swiss Government) had recourse to international arbitration, Swiss law still applied to the internal operations of the Bank.[52] The prevailing view today is that the applicable law for the Bank has been entirely internationalized for all but its most technical and local functions.

Finally, there was the concern that not enough nations recognized the immunities of the BIS and that, as a result, its assets were at risk of attachment or expropriation.[53] To rectify this problem, the Bank's Constituent Charter immunized the BIS from taxation and expropriation by the Swiss government.[54] In the following years, states also issued unilateral decrees, announcing that they would not interfere with the Bank's property or the funds entrusted to it.[55] In 1936, a number of additional nations adopted an agreement to this effect.[56] The United States government, to date, has never officially recognized the Bank's immunities.[57]

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for the full Tribunal, or for a sole arbitrator if so elected, are given in Annex XII of the Agreement, 104 L.N.T.S. 391, *reprinted in* 24 AM. J. INT'L L. SUPP. 321 (1930).

The Tribunal was also mentioned in the BIS Convention, *supra* note 2, art. 2 (any dispute between Switzerland and other signatories to be referred to the Tribunal); the BIS Charter, *supra* note 35, para. 11; and the BIS Statutes, *supra* note 36, art. 56.

51. *See* Williams, *supra* note 43, at 667-69. At the time the BIS was established, four different theories were advanced to describe its legal character. The one argued by Sir John Fischer Williams was that the Bank was fully "internationalized." *Id.* The second theory was premised in civil law, and emphasized the fact that the Bank was a public corporation. A third theory, derived from an analogy to the common law principle of chartering, held that the only legally significant event for the BIS was that Switzerland granted its charter. Finally, there were a variety of hybrid approaches which emphasized both the international and municipal characteristics of the Bank. For a full précis of these theories, see E. DULLES, *supra* note 16, at 71-74.

These theories may be largely irrelevant today since the Bank has come to think of itself as a purely international institution. *See* THE BANK FOR INTERNATIONAL SETTLEMENT AND THE BASEL MEETINGS 103-04 (1980) (issued by the Bank to celebrate its fiftieth birthday). This view seems to be confirmed by modern writers. *See* 1 H. SCHERMERS, INTERNATIONAL INSTITUTIONAL LAW 31 (1972).

52. *See* Delaume, *The Proper Law of Loans Concluded by International Persons: A Restatement and a Forecast*, 56 AM. J. INT'L L. 63, 78-79 (1962). *See also* Aktiebolaget Obligationsinteressenter v. BIS, Judgment of May 26, 1936, Bundesgericht [BG], 62 Entsheidungen des Schweizerischen Bundesgerichts [BGE] II 140 (describing applicable law under the Trust Agreement for the Young Plan, and ruling that the BIS could be held only to the limited standard of trusteeship provided for in the Trust Agreement). *See also* Simons & Radicati, *supra* note 32, at 333-34 (analysis of this case); 2 H. SCHERMERS, *supra* note 51, at 641.

53. *See* Hudson, *Immunities of the Bank for International Settlements*, 32 AM. J. INT'L L. 128, 129 (1938) (describing July 1933 meeting where these concerns were expressed).

54. *See* BIS Charter, *supra* note 35, paras. 5-10.

55. *See* Hudson, *supra* note 53, at 131-33. Many of these declarations provided for international arbitration in the event of a dispute. *Id.* (citing, among others, Austrian, Chinese, Finnish, and Norwegian legislation to this effect).

56. *See* Protocol Regarding the Immunities of the Bank for International Settlements, July 30, 1936, art. 1, 197 L.N.T.S. 31.

57. *See* Hudson, *supra* note 53, at 133. The United States could not extend immunities to the Bank, because to do so would have circumvented its withdrawal from the gold standard. The government promised to reconsider its position "when and as circumstances may change." *Id.*

C. Functions

The proper scope of the Bank's duties was another critical issue. In 1930, its creators granted the Bank both mandatory and optional functions. Its mandated duty as a trustee and payment agent under the Young Plan,[58] although the subject of intense negotiation at the time, was relatively uncontroversial in the drafting of its statutes. It was the Bank's optional functions, particularly those pursuant to its stated primary objectives of promoting central bank cooperation and providing additional facilities for international financial operations,[59] that concerned commercial banks.[60] They did not want the BIS to compete with them in lucrative areas of business.

In order to assuage these fears, the Bank's statutes designated very specifically which operations the institution could and could not perform. Among the permitted activities are all gold transactions,[61] buying and selling securities and other instruments either for central banks or for its own account,[62] and making short-term advances to or borrowing from central banks.[63] The Bank can also open current accounts with central banks and accept their deposits,[64] act as a central bank's agent or, in extraordinary cases, act as its own agent,[65] and, most importantly, act as a trustee in connection with international settlements.[66] Conversely, the BIS cannot issue sight notes, accept bills of exchange, make advances or open current accounts for governments (as opposed to central banks), nor acquire a predominant interest in a business concern or a permanent interest in real property.[67]

The Bank has, however, circumvented some of these prohibitions. For example, the Bank avoided the bar on government lending, attached largely for political reasons,[68] by investing in short-term treasury bills and similar securities.[69] The Bank could also have evaded the prohibition against accepting bills of exchange by discounting bills.[70] Nevertheless, prudential considerations of maintaining liquidity, rather than formal prohibitions, more effectively restrained expansion of the Bank's activities.[71]

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58. *See supra* notes 22-24 and accompanying text.
59. BIS Statutes, *supra* note 36, art. 3.
60. *See* P. EINZIG, *supra* note 8, at 52-53.
61. BIS Statutes, *supra* note 36, art. 22, paras. a, b & c.
62. *Id.* art. 22, paras. e, f, g, and h.
63. *Id.* art. 22, para. d.
64. *Id.* art. 22, paras. i & j.
65. *Id.* art. 22, paras. k & l. For the BIS to establish its own agency requires a two-thirds vote of its Board.
66. *Id.* art. 22, para. m.
67. *Id.* art. 25.
68. *See* E. DULLES, *supra* note 16, at 46.
69. *See* P. EINZIG, *supra* note 8, at 55.
70. The acceptance business was undoubtedly the most competitive banking practice at the time. *Id.* at 54.
71. The Bank was able to fulfill its liquidity requirement (BIS Statutes, *supra* note 36, art. 26) without a formal reserve limit. *See* P. EINZIG, *supra* note 8, at 76, 81.

D. The Bank's Early Actions

The Bank's effectiveness was tested immediately after its creation. Germany's debt troubles had intensified, and it became apparent by the spring of 1931 that Germany would be unable to meet its obligations, even under the Young Plan.[72] The remainder of the European economy was also failing. Under the authority of the 1930 Reparations Agreement, the new Bank entered the crisis by arranging and agreeing to serve as trustee for emergency loans to Bulgaria, Czechoslovakia, and Hungary.[73] The Bank arranged an international loan to Austria in 1930. Meanwhile, the Bank also served as trustee for the financial arrangements involved in the transfer of the Saarland from France to Germany.[74]

Though states discussed the Bank's potential to assume responsibility in servicing all internationally controlled debts,[75] events simply overwhelmed the Bank in 1931. The entire global system of lending collapsed. This triggered the momentous shift away from the gold standard and the moratorium, proposed by President Hoover, on all debt payments.[76] The Young Plan, with its unrealized promise of debt depoliticization, payment rationalization, and commercialization may very well have been too little, too late.

Fortunately, failure of the Young Plan did not discredit the agency charged with its execution. The Bank withstood this disaster and soon began to function effectively once again. By 1934 the Bank had resumed short-term bridging loans to those central banks perennially in need, particularly the Reichsbank, the National Bank of Hungary, and the National Bank of Austria.[77] The Bank also organized two central bank syndicates for emergency credits to Hungary and Germany. This arrangement lasted until Hitler's ultimatum at Munich in 1938.[78]

During the Second World War, the Bank, with just one exception,[79] scrupulously observed its neutrality and acted in an entirely apolitical

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72. *See* E. DULLES, *supra* note 16, at 307-17, 375-83.

73. *See* Reparations Agreements with Bulgaria, Hungary, and Czechoslovakia, Jan. 20, 1930, Gr. Brit. Cmnd. 3494, at 150-55, 168-72; Gr. Brit. Cmnd. 3577 (Hungarian agreement), *reprinted in* 25 AM. J. INT'L L. SUPP. 10, 14, 19 (1931). *See* P. EINZIG, *supra* note 8, at 239-43 (reprint of these instruments). *See also* BIS Third Ann. Rep. 35-38 (1933)(details of the Bank's management of these loans).

74. *See* G. PAPI, *supra* note 6, at 111-14. The Bank also acted as financial agents for the French National Security Loan of 1937. *Id.* at 112.

75. *See* P. EINZIG, *supra* note 8, at 48 (discussing plans for the Greek external debt).

76. *See* E. DULLES, *supra* note 16, at 383-88, 414-50.

77. *See* R. AUBOIN, THE BANK FOR INTERNATIONAL SETTLEMENTS, 1930-1955, at 10 (1955).

78. *Id.* at 10-11. Germany repaid these loans with surprising alacrity. In the case of Hungary, a longer period was arranged with final repayment only being made in 1946. *Id.*

79. The Bank was intensely criticized for its conduct in what came to be called the Czech gold incident. After Germany invaded Czechoslovakia in March 1939, Germany ordered that all Czech gold be tendered to German accounts. The Bank apparently complied with this request. For the best description of this controversy, see H. SCHLOSS, *supra* note 11, at 102-12.

manner.[80] Nevertheless, the Allied powers, meeting at the Bretton Woods Conference in July 1944, voted to liquidate the Bank as soon as it was possible.[81] It is not clear whether this was an attempt to solidify support for the International Bank for Reconstruction and Development [hereinafter the World Bank] and the International Monetary Fund [hereinafter IMF] or whether this was an indication of suspicion of the BIS.[82] Regardless, the Bretton Woods Conference was not competent to disband the Bank. The United States also reconsidered its position on the matter, and the Conference dropped the proposal.[83]

After World War II, the BIS resumed its role as the fiscal agent of the Dawes and Young Plan loans, for which Germany agreed to begin repayments in 1953.[84] The Bank arranged numerous payments transfers in 1949[85] and assisted in the supervision of the Suez Canal tolls.[86] More significantly, the Bank sought new roles as a trustee for international settlements by serving as trustee for the Marshall Plan aid to Europe[87] and later for the Act of Pledge between the European Coal and Steel Community, the forerunner of today's European Communities, and the United States.[88] In addition to its trustee role, the Bank played a financial role by providing some of the initial funding for the World Bank in 1948.[89]

These developments ensured the continued legitimacy of the Bank as an agency for the reconstruction of Europe. Consequently, nearly all of Europe's central banks joined the institution in the years after the War.[90] But during that time, the Bank's activities remained limited. Indeed, at this time there was no need to expand its functions. However, that meant that the BIS

80. Before the war, the BIS declared its neutral stance. *See* BIS Tenth Ann. Rep. 17 (1940) (discussing the Board resolution to this effect). *See also* H. SCHLOSS, *supra* note 11, at 114-15; R. AUBOIN, *supra* note 77, at 15-16.

81. 1 PROCEEDINGS AND DOCUMENTS, UNITED NATIONS MONETARY CONFERENCE AT BRETTON WOODS, July 1-22, 1944, at 330 (1948), *reprinted in* U.S. Dept. of State, 3 INTERNATIONAL ORGANIZATION AND CONFERENCE SERIES, ser. 1.

82. *See* H. SCHLOSS, *supra* note 11, at 118-20.

83. *Id.* at 120-21. For more on the relationship between the BIS and the Bretton Woods institutions, see *infra* notes 89, 203-11 and accompanying text.

84. *See* Agreement on German External Debts, Feb. 27, 1953, 4 U.S.T. 443, T.I.A.S. No. 2792, 333 U.N.T.S. 3. Under the provisions of this agreement, Germany's debts from the First World War will finally be discharged in 1988. *See* H. SCHLOSS, *supra* note 11, at 44, 49.

85. *See* Loan Agreement, Sept. 7, 1949, Belgium-Netherlands, art. 4, 117 U.N.T.S. 3; Loan Agreement, Sept. 7, 1949, United Kingdom-Belgium, art. 4, 106 U.N.T.S. 61; Loan Agreement, Sept. 7, 1949, France-Belgium, art. 4, 123 U.N.T.S. 13. All of these agreements were pursuant to the operation of the new European Payments System, sponsored by the Organization for European Economic Cooperation (OEEC). *See* R. AUBOIN, *supra* note 77, at 29-31.

86. *See* Declaration on the Suez Canal, Apr. 24, 1957, art. 5, para. a, 265 U.N.T.S. 299.

87. *See* R. AUBOIN, *supra* note 77, at 29.

88. For an excellent description of this legal arrangement, see Simons & Radicati, *supra* note 32, at 334-38. For more on the useful example the Act of Trust provides, see *infra* notes 160-64 and accompanying text.

89. *See* H. SCHLOSS, *supra* note 11, at 125 (noting that the original loan was for 17 million Swiss francs).

90. *See id.* at 143-44; R. AUBOIN, *supra* note 77, at 17.

was largely unprepared for the role it would undertake in the next major debt crisis, that of the 1980s.

II.
THE DEBT CRISIS OF THE 1980S AND BIS LENDING

In the 1970s and 1980s, the BIS became increasingly involved in arranging loans. This section traces the evolution of the BIS's lending practices.

Before the current debt malady became acute, the BIS rarely entered into the international lending market, although the Bank was permitted to make short term investments with the approval of the central banks concerned.[91] Long-term investments, in particular, were deemed risky because they limited the Bank's liquidity.[92]

The BIS did, however, participate in a handful of currency stabilization programs in the 1960s and 1970s. The first program took place in June 1966 when the BIS gave Britain, unwilling to seek assistance from the IMF, a $400 million line of credit.[93] The first oil shock of 1973 gave the Bank its second opportunity to promote equilibrium in member nations' accounts. The BIS took an active role in receiving deposits from oil producing countries, while granting advances to central banks of consumer countries or investing in their markets.[94] This policy was unremarkable because it was completely consistent with the Bank's liquidity mandate and the Young Plan's intention to cushion currency devaluations caused by reparation payments.[95]

What was remarkable was the Bank's innovative response to the deficit crisis of the 1970s, sparked by the ten-fold increase in petroleum prices. This problem could not be resolved by merely recycling money. Consequently, the BIS employed other methods to alleviate the debt crisis, including offering short-term facilities where the global payments deficit produced fiscal instability. The BIS offered its first short-term facility to Britain at the height of the sterling crisis in 1976. This loan amounted to $5.3 billion, and Britain repaid it at the end of six months, as stipulated.[96] In 1978, the BIS gave Turkey a small facility after its central bank badly mishandled its convertible lira deposits.[97] The Bank also intervened in cases where causes other than

91. *International Legal Notes, Fiftieth Anniversary of the Bank for International Settlements*, 54 AUST. L. J. 560, 561 (1980)[hereinafter International Legal Notes].

92. Long-term lending obviously ties up funds which could be used for other purposes and violates the Bank's "prime directive" of maintaining its liquidity. *See* BIS Statutes, *supra* note 36, art. 26.

93. International Legal Notes, *supra* note 91, at 561. *See also* BIS Thirty-seventh Ann. Rep. 170 (1967).

94. International Legal Notes, *supra* note 91, at 561.

95. H. SCHLOSS, *supra* note 11, at 127-31 (noting that these investments were wound-up by the 1953 London Agreement); R. AUBOIN, *supra* note 77, at 20-28 (assessing the Bank's balance sheet after World War II and its holdings).

96. *See* Fallon & Shirreff, *The Betrayal of East Europe*, EUROMONEY, Sept. 1982, at 19, 22. *See also* BIS Forty-seventh Ann. Rep. 144 (1977).

97. *See* Fallon & Shirreff, *supra* note 96, at 22.

the global payments deficit produced fiscal instability. Portugal's 1976 revolution, for instance, devastated its economy. The BIS granted Portugal a short-term facility, this time collateralized against Portugal's gold reserves.[98]

The Bank's vigorous entry into emergency lending operations began with a loan to Hungary as an attempt to stem the "regionalization syndrome," where commercial lending to an entire region evaporates when one nation in the area becomes unable to service its debts.[99] By the first quarter of 1982, foreign exchange had virtually disappeared in the socialist nations. There was a risk that Poland, Romania, and Yugoslavia would be unable to perform on their outstanding loans.[100] In January of 1982, the National Bank of Hungary was caught by surprise[101] when foreign depositors withdrew massive funds because they lacked confidence in neighboring Poland, which was then under martial law.[102] Fritz Leutwiler, then chairman and president of the BIS, foresaw the obvious: the dominoes of default would start falling in eastern Europe.[103]

Hungary had no direct recourse to the IMF to combat the loss of investments since it was not then a member.[104] It was an original subscriber to the BIS,[105] and had made full use of the $300 million line of credit from the Bank to which it was entitled.[106] Hungary, however, needed more to weather its shortfall. Within weeks the BIS embarked on a lifeboat operation by arranging a lending consortium among the Bundesbank, the Banque de France, and the Bank of England, which extended credits to Hungary amounting to $100 million.[107] Each of these central banks handled its lending limits, or tranches, differently. The Bundesbank obtained a government guarantee, the Banque de France underwrote a credit from the BIS, while the Bank of England put up its funds directly.[108] Thirteen other central banks also supplemented the loan by extending another $110 million credit.[109]

98. *Id.* (drawing a comparison to the later lending incident with Hungary).

99. The BIS vigorously criticized commercial lenders' practice of treating all nations in the same region alike. BIS Fifty-third Ann. Rep. 184 (1983).

100. *See* Fallon & Shirreff, *supra* note 96, at 21-22.

101. *Id.* at 19.

102. *Id.* at 22; *see also* BIS Fifty-third Ann. Rep. 126 (1983).

103. *See* Fallon & Shirreff, *supra* note 96, at 21-22.

104. *See* Articles of Agreement of the International Monetary Fund, Dec. 27, 1945, 60 Stat. 1401, T.I.A.S. No. 1501, 2 U.N.T.S. 39 [hereinafter IMF Articles]. At the time of Hungary's travails, it was applying for membership in the IMF, and "the prospect of membership was seen as a probable key to the re-opening of the international capital markets to Hungary as a borrower." BIS Fifty-third Ann. Rep. 164 (1983). Hungary officially joined the IMF in May 1982. *Id.*

105. The Magyar Nemzeti (Bank of Hungary) acquired its 4,000 shares in the Bank in June 1930. *See* H. SCHLOSS, *supra* note 11, at 144.

106. *See* Fallon & Shirreff, *supra* note 96, at 22.

107. *Id.*

108. *Id.*

109. Campbell, *supra* note 3, at 29.

These bridging loans were of three month's duration, with a three month roll-over option. The purpose behind this loan arrangement was to give Hungary enough time to negotiate a credit package with the IMF and to attract fresh medium-term credit from commercial banks.[110] Six months later, Hungary was still negotiating with commercial banks for new loans; consequently, the BIS arranged to extend a standby credit of $300 million for another six month term.[111] This was the last BIS-sponsored loan that Hungary needed during this period, and it was completely discharged.[112]

For the BIS to make these loans to Hungary was unquestionably an extraordinary action on the part of the Bank. BIS Chairman Leutwiler expressly said that the BIS viewed its action in Hungary as a "test case," designed to express confidence in that economy, which might, in turn, encourage new commercial lending.[113] German bank authorities intensely criticized the motivation behind the Bank's loans to Hungary, as being inconsistent with the essential purposes and policies of the BIS.[114]

Surprisingly, no one ever questioned the Bank's authority to make these bridging loans. These loans were effectively loans to governments, an action specifically forbidden under the BIS statutes.[115] The Bank, however, characterized the loans merely as assistance to a central bank authority within the ambit of the BIS's statutory powers.[116] Furthermore, some central banks argued that the BIS was not lending on its own books, but only acting as a conduit for central bank lending.[117] Though the Hungarian loans might be justified in this manner, it soon became clear that this justification was merely a pretense when the Bank baldly made emergency loans to Latin American governments.

Just as the financial situation in eastern Europe was stabilizing, the "regionalization syndrome" in Latin America brought the specter of default clearly into view.[118] The Malvinas/Falkland Islands conflict, beginning in April 1982, triggered a crisis in confidence not only regarding Argentina, but Mexico and Brazil as well. Consequently, when Mexico approached the BIS for help, the BIS chose to become an active lender in Latin America.

In the summer of 1982, Mexico experienced the outbreak of an unprecedented external payments crisis, triggered by a massive capital flight to the

110. *See* BIS Fifty-third Ann. Rep. 126 (1983).

111. *See* Wall St. J., Sept. 28, 1982, at 38, col. 1.

112. *See* BIS Fifty-third Ann. Rep. 164-65 (1983). Nonetheless, the Bank had to bend its lending rules in order to make another short-term loan to Hungary for $100 million in April 1983. *See* Wall St. J., Apr. 15, 1983, at 34, col. 4 (noting the resistance of Bundesbank President Otto Pöhl). It was later repaid. *See* Wall St. J., Oct. 6, 1983, at 51, col. 1.

113. *See* Fallon & Shirreff, *supra* note 96, at 27.

114. *Id.* (quoting Otto Pöhl statement that "central bankers should not give any advice to bankers on how to deal with customers").

115. *See* BIS Statutes, *supra* note 36, art. 25, para. c.

116. *Id.* art. 22, para. d.

117. *See* Fallon & Shirreff, *supra* note 96, at 27.

118. *See* BIS Fifty-third Ann. Rep. 126-31 (1983).

United States.[119] Unlike in the case of Hungary, however, the BIS swiftly and effectively arranged emergency financial support. In the first weeks of August, the BIS arranged a $700 million line of credit with the Federal Reserve Bank of New York. By mid-August, the United States government offered additional advances and guarantees.[120] But these arrangements were not enough to tide Mexico over until drawing rights under the IMF's Extended Fund Facility were negotiated. Thus, on August 30, the Federal Reserve Bank and the BIS each provided half of a $1.85 billion bridging credit to the Bank of Mexico.[121] Mexico repaid this loan in December when it had at its disposal the first lending tranche of its Fund quota and the drawing rights under the Extended Fund Facility.[122]

The country most profoundly affected by the "regionalization syndrome" was Brazil, and the BIS soon became involved in a rescue operation on behalf of that nation. In December 1982, the BIS granted Brazil a $1.2 billion bridging loan, later increased to $1.45 billion.[123] However, when the loan became due, Brazil was unable to pay because it had been denied further IMF credits for failing to meet the Fund's conditionality targets.[124] This placed the BIS in a decidedly awkward situation. The Bank's liquidity had been compromised because of its extensive emergency credits,[125] and now it faced a write-off on its debt.

The Bank twice granted extensions on the first $400 million tranche of the Brazilian loan, which had come due.[126] After threatening not to extend this repayment past July 15, 1983, the BIS backed down and deferred the debt indefinitely.[127] The Bank also could have demanded repayment by calling upon the guarantees of the central banks involved in the lending consortium to Brazil, but it did not.[128] Although it was clear that BIS officials did not relish this game of threatened default and proffered extension, Brazil did repay the larger portion of the loans, $1.05 billion, in December 1983.[129] The experience with Brazil began to dampen the Bank's enthusiasm towards

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119. *Id.* at 128.

120. *Id.* (noting that the official aid consisted of a one billion dollar advance payment for future oil imports along with financing guarantees for one billion dollars in food exports).

121. *See* Wall St. J., Aug. 30, 1982, at 17, col. 3. Mexico had originally asked for $1.5 billion, and later $1.68 billion. *See* Wall St. J., Aug. 24, 1982, at 35, col. 1. The Bank's contribution to this facility was thus $925 million.

122. BIS Fifty-third Ann. Rep. 128 (1983). Mexico received a $3.8 billion credit, drawable over three years, with the IMF. *Id.*

123. *Id.*

124. *See* BIS Fifty-fourth Ann. Rep. 151 (1984).

125. *Id.* Balance Sheet and Profit and Loss Account at 31st March 1984 (indicating the Bank's position after this year of extensive lending).

126. *See* Wall St. J., July 6, 1983, at 29, col. 2.

127. Wall St. J., July 12, 1983, at 2, col. 2 (announcing that the BIS would not extend the loan); Wall St. J., July 15, 1983, at 31, col. 1 (hinting that the Bank would reconsider its position since Brazil's budget cutbacks would placate the IMF); *God save Brazil, lest the central bankers won't*, ECONOMIST, July 16, 1983, at 65.

128. *See* BIS Fifty-fourth Ann. Rep. 151 (1984); Wall St. J., Aug. 30, 1983, at 12, col. 2.

129. Wall St. J., Dec. 1, 1983, at 53, col. 1; BIS Fifty-fourth Ann. Rep. 151-52 (1984).

emergency lending operations. Nevertheless, the Bank did participate in other such rescues.

By mid-1983, the Bank's attentions again turned to supporting some of Europe's weaker economies, particularly those of Yugoslavia and Portugal. Yugoslavia's case raised particular problems since, as Bank officials admitted, Yugoslavia's economic problems were "not so much of a temporary as of a medium-term nature."[130] The BIS was, after all, in the business of providing only short-term assistance.[131] This was the only lending policy that accorded with the Bank's mandate to preserve its liquidity at all costs.[132]

The Bank nevertheless made a bridge loan to Yugoslavia of $500 million, partly backed by a group of central banks and partly collateralized with a gold deposit.[133] Three hundred million dollars from this facility were rapidly disbursed, but then problems arose when there was disagreement about the negative pledge clauses on the gold collateral.[134] Although Yugoslavia repaid the whole loan by December 1983,[135] the Bank had learned to be careful requiring very stringent collateral terms for its medium-term loans.

In contrast, Portugal needed only a short-term loan adjustment. Moreover, the Bank's two tranches of lending to that nation were almost entirely collateralized.[136] A problem developed, however, at the end of the maturity period when Portugal's central bank was compelled to sell a portion of its reserves.[137] This triggered a precipitous drop in gold prices, which boosted the value of the dollar.[138] This sequence of events indicated that even when the BIS was loaning from its own books, backed with security, the world monetary system was still at risk.

In the years 1982 and 1983, the Bank lent nearly four billion dollars in its rescue operations for Hungary, Mexico, Brazil, Argentina, and Yugoslavia.[139] All these loans were limited to short maturity periods, usually six to nine months, although these installments were grudgingly extended when circumstances demanded. Most of these credit facilities were arranged with the sponsorship of central banks, either individually (like the United States' lead role in the Mexico loan) or, more commonly, in consortia. The BIS often secured the guarantees of the central banks involved before lending on its account. But, as happened with Hungary and then Brazil, these guarantees

130. BIS Fifty-third Ann. Rep. 165-66 (1983).

131. *See supra* notes 113-17 and accompanying text.

132. *See supra* note 71 and accompanying text.

133. *See* BIS Fifty-third Ann. Rep. 166 (1983).

134. *See* BIS Fifty-fourth Ann. Rep. 152 (1984); Wall St. J., Sept. 14, 1983, at 37, col. 5 (noting the release of the last $200 million to Yugoslavia).

135. Wall St. J., Dec. 2, 1983, at 5, col. 5.

136. *See* Wall St. J., Aug. 8, 1983, at 20, col. 5. Portugal was experiencing a repetition of the financial crisis which had hit it seven years before. *See supra* note 98 and accompanying text.

137. Wall St. J., Sept. 6, 1983, at 38, col. 4. Portugal had to sell 975,000 ounces and then 30 tons of gold to meet its obligations to the BIS. *Id.*

138. Wall St. J., Sept. 7, 1983, at 34, col. 4.

139. *See* Wall St. J., Dec. 2, 1983, at 5, col. 5.

did not place the Bank in a superior bargaining posture with the debtor nations but, rather, at a distinct disadvantage when it came to negotiating repayment of the loans. Debtor nations could exploit the Bank's position as an intermediary for other central banks and, thus, win more time to repay their debts.

The BIS also had the option of lending on its own account and seeking collateral, typically the gold reserves of the debtor nation. The Bank exercised this option in the cases of Portugal and Yugoslavia, since both countries were depositors at the BIS and, consequently, legally binding security arrangements could be facilitated.[140] These arrangements, as suggested above, were also not without their drawbacks. Making loans collateralized against gold could prompt surprising, and sometimes severe, currency fluctuations. Debtors faced with the necessity of selling gold reserves were, perhaps, justifiably reluctant to repay their loans. As a result, the Bank was itself reticent to enter into these arrangements, for fear of either adversely affecting global exchange rates or not being repaid.

Finally, the Bank often indirectly supported its debtors by promoting commercial lending. This was an explicit goal in the Hungarian life-boat operation.[141] In the case of Argentina, commercial banks had also made the startling demand that it secure a BIS bridge loan before it could receive additional financing.[142] This strange contingency requirement, if imposed in all cases, would have truly transformed the BIS into the lead international institution for sanctioning loans, displacing the IMF as the world's lender of last resort. The probability of this outcome will be weighed against the reality of the Bank's place in international finance in the following section.

III.
A Prospectus for the Bank's Future Role

The Bank has within its legal mandate the option of offering three general services to assist in resolving the current debt crisis: the promotion of central bank cooperation in all of its aspects, service as a trustee or agent for new methods of debt restructuring, and service as a "lender of last resort." Part A of this section will briefly review the Bank's efforts to establish clearing options and standards for lending, practices which it has fully embraced.[143] In contrast, there have been few plans to make the Bank a trustee in new debt reconstruction schemes, and little attention has been paid to the institutional framework for the execution of combination debt/equity conversions or swaps. Part B outlines one possible avenue for the Bank's participation in this area through the creation of national investment trusts. Part C

140. *See* H. Schloss, *supra* note 11, at 143-44.
141. *See supra* notes 110, 113-14 and accompanying text.
142. *Central Bank's Bank Resists Change*, Wall St. J., Dec. 15, 1982, at 35, col. 2.
143. This is not to minimize the importance of these activities, but rather to recognize they have become fully ingrained into the fabric of the Bank's day-to-day work.

analyzes the much-debated plan to make the Bank truly the lender of last resort—a potentially dangerous role. Finally, Part D discusses the Bank's inability to expand into a trustee and lender role unless the United States and Japan actively begin to participate in the Bank's work. Even if the Bank were not to assume this role, it may still be desirable for the United States to reconsider its 1930 decision and cooperate with the BIS by assuming its seats on the Board.

A. Promotion of Central Bank Cooperation

The BIS has adopted both active and advisory approaches in promoting closer cooperation among member central banks. The most significant example of the Bank's active or direct interventions in the international financial market has been its recent designation as clearing agent for the European Community's composite currency, the ECU.[144] Although the ECU has yet to achieve widespread use, this may well change as it becomes the currency of choice in Euromarket operations.[145] ECU-denominated bonds may also someday present a credible alternative for world investment markets if the dollar continues to lose its value against European currencies.[146] The increasing importance of the ECU could possibly allow the BIS to assume the role as the guarantor of this market.[147]

The BIS has acted in an advisory capacity on numerous occasions. While serving as an independent advisor to central banks, the Bank has often sounded warnings of debt crises to the international financial community. In fact, the Bank's 1980 annual report noted the first glimmer of the impending debt crisis.[148]

The Bank also has served as the host agency for the Group of Ten[149] and the Committee on Banking Regulations and Supervisory Practices.[150] In this capacity, the BIS was chiefly responsible for drafting the extraordinarily

144. *See* 135 THE BANKER 41 (May 1986). The BIS credits and debits the accounts of the fifty-seven commercial banks party to the ECU's interbank market. Although the BIS monitors their accounts, it does not lend funds to cover any shortfall in them. *Id.*

145. For more on the ECU's use in international financial operations, see BIS Fifty-fifth Ann. Rep. 127-33 (1985).

146. BIS Fifty-fifth Ann. Rep. 132 (1985).

147. *See* THE BANKER *supra* note 144, at 41.

148. *See* BIS Fiftieth Ann. Rep. 114-20, 175-80 (1980); BIS Fifty-first Ann. Rep. 104-11, 164-68 (1981).

149. The Group of Ten Governors (G-10) was formed in 1961 by ten members of the International Monetary Fund: Belgium, Britain, Canada, France, Italy, Japan, the Netherlands, Sweden, West Germany, and the United States. *See* ECONOMIST, *supra* note 4, at 50. Switzerland joined later. Together these countries are instrumental in the General Agreements to Borrow (GABs), providing the IMF with additional tranches of funds. *See infra* notes 209-11 and accompanying text.

150. This Committee, the Basel Group, is composed of representatives of twelve industrialized nations: Belgium, Canada, West Germany, France, Italy, Japan, Luxembourg, the Netherlands, Sweden, Switzerland, the United Kingdom, and the United States.

influential Basel Concordats.[151] The Basel Concordats established guidelines for supervision of international banking operations, divided responsibility between home country and host country authorities, and clarified aspects of central banks' domestic functions as lenders of last resort.[152] These reports have been praised as introducing the idea of using "regulatory asymmetries," the different competences and interests of national bank regulators, to "modulate and rationalize international monetary flows."[153]

The BIS also has conducted studies on recent innovations in international banking in general and studies on particular issues such as off-balance sheet exposures for commercial banks.[154] The Bank has consistently expressed its concern that, left unsupervised, development of new instruments in international banking[155] could frustrate central banks' macroeconomic policies.[156] The urgings of the BIS for regulatory caution have not gone unheeded in this country. Both the Federal Reserve Board and the United States Congress have recently bolstered controls over international lending by banks.[157] The BIS will remain an influential proponent of stronger national bank regulation while it also supervises growing segments of the global monetary system.

B. Trustee for International Financial Settlements

The Bank's most significant mission to date has been to serve as a trustee for international settlements. After all, the BIS was founded primarily to serve as the agent for the Young Plan, and it was later revitalized by a role in

151. The Basel Group has issued two reports. The 1975 Concordat appears in *International Capital Markets: Recent Developments and Short-Term Prospects*, INTERNATIONAL MONETARY FUND 29-32 (Occasional Paper No. 7) (Aug. 1981). The Revised Concordat of May 1983 is reprinted in 22 I.L.M. 900 (1983) [hereinafter Revised Concordat].

152. Revised Concordat, *supra* note 151, at 901. The second report does not treat the issue of lending of last resort by central banks.

153. R. LOMBARDI, DEBT TRAP: RETHINKING THE LOGIC OF DEVELOPMENT 188 (1985).

154. *See Debt, Financial Stability, and Economic Growth, Hearing Before the Subcomm. on Telecommunications, Consumer Protection, and Finance of the House Comm. on Energy and Commerce*, 99th Cong., 2d Sess. 71 (1986)(reprint of BIS Report) [hereinafter House Report]; Editorial, 1986 J. BUS. L. 178.

155. These four major new instruments include note issuance facilities (NIFs), currency and interest rate swaps, currency and interest rate options, and forward rate agreements (FRAs). *See* House Report, *supra* note 154, at 9-12. *See also* Wall St. J., Oct. 29, 1985, at 32, col. 4 (warning about new bond and note issues).

156. *See Notes*, 136 THE BANKER 4 (July 1986); *Notes*, 135 THE BANKER 11 (July 1985) (analysis of the BIS Annual Reports in the past two years).

157. The Comptroller of the Currency and Federal Reserve Board announced revisions to their minimum capital guidelines on June 13, 1983, in response to the Revised Concordat. *See* 22 I.L.M. 930 (1983). The International Lending Supervision Act of 1983, Pub. L. No. 98-181, 97 Stat. 1278 (codified at 12 U.S.C.A. §§ 3901-12 (1987)), may have also been influenced by BIS concerns. *See* legislative history in Committee on Banking, Finance and Urban Affairs, International Lending Supervision Act of 1983, H.R. REP. NO. 98-175, 98th Cong., 1st Sess. (1983), *reprinted in* 1983 U.S. CODE CONG. & ADMIN. NEWS 1768, 1913-30. Congress did, however, criticize the Basel Committee for its secrecy and the subsequent lack of consistency in interpreting the Concordats. *Id.* at 1926-27.

the Marshall Plan and in the funding of the European Communities.[158] This part discusses the trustee functions which the BIS has performed in the past and those which it might consider in the future.

The Bank has performed two different types of trustee functions in the past: 1) supervising sovereign debt restructuring and 2) managing debt for development. The Bank's role in supervising sovereign debt restructuring is the paradigmatic example of the Bank's original purpose under the Young Plan.[159] This role did not exclusively focus on securing creditors' rights. Smoothing debt repayments, managing exchange rate fluctuations, reinvesting in German securities, and depoliticizing conditionality requirements were all elements of the Young Plan arguably intended to advance the interests of the debtor nation.

The Bank's role in the initial financing of the European Coal and Steel Community [hereinafter ECSC],[160] by contrast, exemplifies the Bank's second type of trustee function: managing debt for development. In 1954, in order to revitalize smoke-stack industries in Europe devastated by the War, the ECSC had to borrow heavily from the United States.[161] The ECSC borrowed $100 million which it, in turn, loaned to smoke-stack industries. The loan to the ECSC was backed by notes secured by pledges from these industries.[162] In an Act of Pledge,[163] the BIS was named as Depository, with the responsibility of holding the loan proceeds along with the borrowing enterprises' individual pledges.

The Bank, in effect, became the indenture trustee of these borrowing steel manufacturers to ensure that no subsequent indebtedness would degrade the ECSC's security.[164]

In the future, the BIS might attempt two additional trustee functions: 1) supervising the performance of today's sovereign debt and 2) converting sovereign debt into commercial equity. The first function, international agency

158. *See supra* notes 87-88 and accompanying text.

159. *See supra* note 24 and accompanying text.

160. Convention establishing the European Coal and Steel Community, Apr. 18, 1951, 261 U.N.T.S. 40. The original parties were Belgium, France, West Germany, Italy, Luxembourg, and the Netherlands. The ECSC was later absorbed by the European Communities. *See* Treaty Instituting a Single Council and a Single Commission of the European Communities, Apr. 8, 1965, art. 9, 10 O.J. Eur. Comm. (No. C 152) 2 (1967), *reprinted in* 4 I.L.M. 776 (1965).

161. *See* Simons & Radicati, *supra* note 32, at 335. The Export-Import Bank of the United States offered the twenty-five year loan, at 3.875 percent interest. This was the first time that a loan had been extended to the ECSC, as distinct from its member states. *Id.* For a summary of the ECSC's other public lending see *id.* at 345.

162. *Id.* at 335-36.

163. The Act of Pledge is contained in the Loan Agreement, Apr. 23, 1954, U.S.-ECSC, Apr. 23, 1954, 5 U.S.T. 2646, 2655, T.I.A.S. No. 3126, 238 U.N.T.S. 340, 348 (supplemented and amended).

164. Simons & Radicati, *supra* note 32, at 336-37.

supervision of the performance of today's sovereign debt, has been much discussed and tested.[165] This function has been discussed with respect to the IMF in particular. However, the IMF has made only uneven progress in enforcing conditionality, the economic, fiscal, and monetary reforms it imposes as a requirement for further support to combat balance-of-payments shortfalls. Indeed, the IMF has become so unpopular in this role that debtor nations have sought out other agencies to assume this supervisory function, most notably the World Bank.[166] Because there is unlikely to be a competition for laxity in debt supervision among these international agencies, the BIS would probably not enter into the politically charged function of overseeing sovereign debt. The officers of the Bank would never consider undermining the authority of the IMF in administering conditionality requirements.

The second function, converting sovereign debt into commercial equity, presents a different sort of trusteeship opportunity for the BIS. A number of these conversion schemes have been proposed,[167] many of which do not require the services of an independent sponsor and payment agent. But in one proposal, which suggests establishing national investment trusts, the need for an independent investment manager figures prominently. Under this proposal, shares in country specific closed-end investment trusts would be exchanged, at virtually no discount, for the current loans that commercial banks have in the private and public sector entities of the debtor nation.[168] The investment trust shares would later be offered on a secondary market to diversify the debt.[169] A rudimentary version of this plan inspired the creation of the Japan and Mexico Mutual Funds, both traded on the New York Stock Exchange, as well as a host of smaller investment trusts.[170]

This plan has been vigorously advanced by the International Finance Corporation [hereinafter IFC], a sister agency to the World Bank, specializing in long-term development finance with extraordinarily gracious lending

165. *See generally* C. BERGSTEN, W. CLINE & J. WILLIAMSON, BANK LENDING TO DEVELOPING COUNTRIES: THE POLICY ALTERNATIVES (1985); Bradlow, *The International Monetary Fund: An Overview of its Structure and Functions*, in INTERNATIONAL BORROWING: NEGOTIATING AND STRUCTURING INTERNATIONAL DEBT TRANSACTIONS 399 (D. Bradlow ed. 1986); Gold, *The Relationship between the International Monetary Fund and the World Bank*, 15 CREIGHTON L. REV. 499 (1982).

166. *See* M. DE VRIES, THE IMF IN A CHANGING WORLD, 1945-85, at 181-98 (1986).

167. Buchheit, *Converting Sovereign Debt into Equity Investments*, INT'L FIN. L. REV., Sept. 1986, at 10-12.

168. International Finance Corporation, A Proposal to Establish National Investment Trusts as Part of Debt Restructuring Programs 1 (Jan. 1984) [hereinafter IFC Report] (available in the office of the *International Tax and Business Lawyer*).

169. *Id.* This idea is hardly novel. Debt mobilization was one aspect of the Young Plan of 1930. *See supra* notes 15-17 and accompanying text.

170. IFC Report, *supra* note 168, at 5. The other investment trusts were established for Brazil, Korea, Taiwan, and the Philippines. Obviously, not all of these nations possess notable debt and the original intent of these funds was to diversify equity participation by institutional and individual investors. *Id.*

conditions.[171] There is no indication, however, that the IFC would either be willing to "promote the proposed national investment trust in relevant forums among commercial banks, institutional investors, and regulatory authorities,"[172] or be able to make a sizeable cash investment.[173] Moreover, it is integral to any debt-equity swap that adequate security be offered for the investments. Such security includes not only guarantees that the investment will not be expropriated by the government, but also guarantees that the value of the enterprise involved will not be compromised over time. The IFC's limited powers render it incapable of insuring either of these requirements.

The BIS has already, however, assumed comparable functions in executing the Young Plan and the ECSC Act of Pledge. This is not to overlook the important distinction between the use of commercialization techniques, implicit in the earlier instances of debt restructuring and reconstruction financing,[174] and the current emphasis on conversion to real equity (not simply debt expressed differently). Sovereign governments have imposed substantial restrictions on these conversions from debt to equity[175] and may be unwilling to agree to the intervention of even a neutral international institution to supervise subsequent performance. However, in Chile and the Philippines, two countries that have promulgated rules for debt-equity swaps, the central banks are to have the key regulatory authority for this process.[176] If more countries were to become interested in debt-equity swaps and an international trustee were considered, the BIS would be the natural body to fill that role. It alone among international financial institutions is both closely aligned to the interests of central banks and has a proven record for protecting the rights of creditors in these types of settlements. The Bank would also be able to make the needed initial capital contributions to make these equity-for-debt conversion schemes possible. The Bank's capacities make it an attractive choice to administer these plans.

C. *The BIS as the Lender of Last Resort*

When the pace of the debt crisis quickened in the 1980s, many financial analysts called for an institution that could provide the emergency relief needed to avert a financial apocalypse that could arise at any time and in any

171. *See The World Bank and the International Finance Corporation*, in INTERNATIONAL BORROWING: NEGOTIATING AND STRUCTURING INTERNATIONAL DEBT TRANSACTIONS 31 (D. Bradlow ed. 1986).

172. IFC Report, *supra* note 168, at 7.

173. *Id.* at 2.

174. *See supra* note 15 and accompanying text.

175. Buchheit, *supra* note 167, at 12-14 (an analysis of foreign investment regulations in the Philippines and Chile).

176. *Id.*

part of the world.[177] Many turned to the BIS, which seemingly desired the mantle of the lender of last resort.[178]

In many respects, the choice was obvious, and the conditions compelling. The BIS could respond more quickly and effectively than the IMF or World Bank in arranging the bridging loans needed to stave off default.[179] The exclusive membership of the BIS Board, its unity with the interests of central banks worldwide, and its expansive legal mandate all contributed to this capacity for decisive action.[180] The Bank's lifeboat operation for Mexico in 1982 took only forty-eight hours to launch. In comparison, IMF aid was only forthcoming after four months of negotiation.[181]

Bank officials nonetheless denied the prospect that their institution would become the teller of a permanent "crisis" window, as some commercial banks desired.[182] Doubts about the propriety of BIS loans arose even during the discussions of continuing assistance to Hungary in 1982.[183] On that occasion, the Bank went to extraordinary lengths to assure the financial community that aid to Hungary's central bank was only to resolve a temporary payments imbalance.[184] The three-year loan to Yugoslavia, negotiated in 1982, was also criticized by some BIS member central banks as being too long in duration.[185] Indeed, Fritz Leutwiler, BIS Chairman, said in February 1983 that it would be the last of its type. According to Chairman Leutwiler, the Bank did not want to continue to provide bridge financing without being able to see "an end to the bridge."[186]

The Bank's experience in making loans further reinforced its reluctance about becoming the lender of last resort. At first, all went well. In its June 1983 Report, the Bank described its lending operations for the previous year in approving language. "[T]he use of measures which under normal circumstances would be unthinkable" were necessary to keep the international financial system afloat.[187] While allowing sovereign defaults by refusing to provide aid would have the pleasing effect of prompting "both borrowers and

177. Lipson, *International Debt and International Institutions*, in THE POLITICS OF INTERNATIONAL DEBT 237-38 (M. Kahler ed. 1986).

178. *Id.*

179. *See* Gottlieb, *Global Bargaining: The Legal and Diplomatic Framework*, in LAW-MAKING IN THE GLOBAL COMMUNITY 109 (N. Onuf. ed. 1982).

180. *See supra* note 177.

181. *See supra* notes 119-22 and accompanying text.

182. Fallon & Shirreff, *supra* note 96, at 27 (the case of Hungary); Wall St. J., Dec. 15, 1982, at 35, col. 2 (commercial banks desiring to negotiate $1.1 billion loan required that Argentina secure BIS support).

183. Fallon & Shirreff, *supra* note 96, at 27-30.

184. *See supra* notes 101-17 and accompanying text.

185. Wall St. J., Dec. 15, 1982, at 35, col. 4. This loan was finally concluded in 1983, *see supra* notes 130-35 and accompanying text.

186. Wall St. J., Feb. 2, 1983, at 31, col. 1.

187. BIS Fifty-third Ann. Rep. 131 (1983).

lenders [to] think twice before again engaging in such imprudent credit arrangements,"[188] this solution would wreak havoc on the economies of responsible and irresponsible nations alike.[189] "The central-banking community of the western industrial countries has thus demonstrated in the clearest possible way its collective determination and ability to take prompt action in the face of dangers to the functioning of the international financial system."[190]

This stirring rhetoric soured as the Bank's lending experience grew in the next fiscal year. During that time, the BIS compromised each of the three guidelines for its lending decisions. These guidelines called for (1) the use of proceeds as short-term financing, (2) backing by solid collateral, and (3) linkage with automatic repayment, such as pending IMF facilities.[191] The protracted negotiations over Yugoslavia's negative pledge on the gold used as collateral in the 1983 loan endangered the Bank's security interest in that instance.[192] More significantly, the delay in Brazil's access to IMF funds placed the BIS in an intolerable position of having to choose between either rolling the debt over and losing valued liquidity or making a call on the central bank consortium which had guaranteed the loan.[193] Even though the Bank's liquidity was severely depleted in mid-1983,[194] it had no choice but to extend Brazil's repayment period. To have alienated the central bank governors who had provided the funds for the Brazilian emergency loan would have been unthinkable.

Institutional and legal factors also constrained the Bank's aspirations for becoming the lender of last resort. The Bank's imperative in preserving its liquidity, as required by its statutes,[195] was the chief reason noted for the change in its policy of offering bridging loans. According to the Bank's Annual Report for 1984, "The BIS is not a suitable vehicle for the realization of [long-term stability]; in particular, its resources, representing as they do an essentially liquid element in central banks' reserves, cannot be immobilized in medium or long-term lending."[196] This concern over the liquidity requirement also reflected the fact that the Bank had limited reserves. At the end of March 1984, the Bank had book assets of $41.2 billion.[197] Two years later, BIS assets had risen to $51.5 billion.[198] If the Bank's holdings were in gold

188. *Id.* at 182.
189. *Id.*
190. *Id.* at 185.
191. Wall St. J., Dec. 15, 1982, at 35, col. 2.
192. *See supra* note 134 and accompanying text.
193. *See supra* notes 123-29 and accompanying text.
194. Wall St. J., June 14, 1983, at 40, col. 3.
195. *See* BIS Statutes, *supra* note 36, art. 26; *supra* note 71 and accompanying text.
196. BIS Fifty-fourth Ann. Rep. 152 (1984).
197. *Id.* at Balance Sheet and Profit and Loss Account. This figure ranks the BIS as the forty-sixth largest bank by assets, as of 1984. For this calculation, the Swiss gold franc was valued at U.S. $1.94.
198. BIS Fifty-fourth Ann. Rep. Balance Sheet and Profit and Loss Account (1986).

valued at market rates, its reserves and capital would exceed $3 billion.[199] But the Bank's reserves were not liquid. Thus, there was an effective limit on lending, a limit that the Bank apparently approached in 1983.

Many of the loans in 1982 and 1983, particularly those to Brazil and Mexico, were tantamount to credits to sovereign governments in violation of the Bank's statutes.[200] Since the Bank was free to invest in treasury bills,[201] this restriction was really observed in the breach. Nevertheless, it was manifest that the BIS was engaging in the business of sovereign lending, no matter how short-term or how much-needed.

Factors outside the Bank's statutes also influenced BIS lending. There was resistance when the Bank lent to non-members, which included virtually any non-European debtor nation.[202] While the statutes make no distinction between states whose central banks are subscribers to BIS shares and those that are not, the BIS Board obviously represents the interests of the members. Although the Bank's decision-making to date has not been tainted by European provincialism, it would not be surprising if member central banks were given priority for aid. For instance, Hungary, Portugal, and Yugoslavia all received substantial assistance in 1982 despite the fact that their financial condition was less severe than the Latin American debtors.

Finally, the Bank has conceded that the IMF is in a better position to promote structural adjustment and provide financial support for stabilization programs in developing nations.[203] The IMF has a comparative advantage in its ability to impose and manage conditionality.[204] This function, after all, was not contemplated by the founders of the BIS. The stringent foreign management of the German economy after World War I, required by the very terms of the reparations clauses of the Versailles Treaty and the later Dawes Plan,[205] was utterly discredited by the Young Plan. The Bank had no power to impose conditionality on Germany. The essential provision of the statutes giving central banks the power to veto BIS operations within their nation,[206] even those pursuant to an international settlement to which they have acceded, bars any form of conditionality. Also, as a practical matter, the Bank's small staff could not adequately oversee any such reforms.[207]

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199. *See* ECONOMIST, *supra* note 4, at 50. In contrast, as of 1984, Chase Manhattan Bank had capital and reserves totalling $3.6 billion. This figure has likely increased as Chase adopted the policy of increasing stated capital to cover likely debt defaults and write-downs. The BIS still compares favorably with Chase in this regard since its internal reserves have never been disclosed. *Id.*

200. *See* BIS Statutes, *supra* note 36, art. 25, para. c.

201. *See supra* notes 68-69 and accompanying text.

202. For a list of member central banks of the BIS, see H. SCHLOSS, *supra* note 11, at 143-44.

203. BIS Fifty-fourth Ann. Rep. 152 (1984).

204. *See* IMF Articles, *supra* note 104, art. 8.

205. *See supra* notes 6-13 and accompanying text.

206. BIS Statutes, *supra* note 36, arts. 20 & 23. *See also supra* note 39.

207. Wall St. J., Dec. 15, 1982, at 35, col. 2 (noting that the BIS has a 300 person staff, compared with the 2500 member staff of the Washington-based IMF).

Therefore, instead of preempting the IMF's authority by directly offering bridging loans, the Bank has worked to increase the IMF's resources so that the IMF could provide the aid needed in emergency situations. Preparatory to the eighth review of IMF quotas, the BIS and ten central banks made available to the IMF in 1981 a stand-by facility of 675 million special drawing rights (SDRs).[208] Under the General Arrangements to Borrow (GABs), the Group of Ten central banks established a line of credit on behalf of the IMF in the early 1970s.[209] In 1984, after negotiations between the BIS and the IMF, this line was increased from SDR 6.4 billion to nearly SDR 17 billion.[210] The BIS later staked, with seventeen central banks, an additional SDR 2.5 billion.[211]

Despite all formal limitations and policy objections to becoming the "lender of last resort," however, the BIS can still play a crucial role in offering bridge loans. Though the IMF now certainly has the resources to provide short-term financing if needed to avert a collapse of the international financial system, the question remains whether it could react quickly enough in a crisis. The BIS's 1982 policy of offering bridge loans was necessitated by the urgency of the situation. In this sense, the "lender of last resort" was merely the shortest of short-term creditors. As long as negotiations between the debtor nation and the IMF proceeded constructively, there was a view to "the end of the bridge" and no danger that the Bank could be used as a way to circumvent IMF conditionality.[212] Similarly, as long as IMF conditionality is not circumvented and the BIS's three criterion for lending (short duration, solid collateral, and automatic repayment) are satisfied, financial prudence should not bar the offering of BIS bridging loans in a future crisis.

D. The United States and Japan in the Bank's Future

The factor which may most decisively limit the BIS' potential role in resolving the debt crisis is purely institutional—the lack of formal participation by the central banks of Japan and the United States. Reconsideration of the Bank's lending practices and promotion of its position as a trustee in new restructuring arrangements require close coordination between all central banks. These initiatives might flounder if the central banks of the world's two most dynamic economies and most expansive lending reserves do not have confidence in BIS operations.

Under the statutes, both Japan and the United States were assigned seats on the Bank's Board.[213] Japan took its place in the institution, only to forfeit

208. BIS Fifty-fourth Ann. Rep. 152 (1984). Special Drawing Rights are the IMF unit of account, the value of which fluctuates but approximates the U.S. dollar.
209. M. De Vries, *supra* note 166, at 118-19. *See also supra* note 149.
210. M. De Vries, *supra* note 166, at 191-92.
211. BIS Fifty-fourth Ann. Rep. 152 (1984).
212. Editorial, *Hands off the BIS*, Euromoney, July 1984, at 5.
213. BIS Statutes, *supra* note 36, art. 28.

it after the Second World War.[214] The United States declined to participate from the outset,[215] and its shares were distributed to a consortium of leading banks and the public.[216] The Federal Reserve Board considered joining the Bank in the 1950s. Favorable action was impossible owing to fears that "joining the BIS might be construed as an expression of preference over the International Monetary Fund,"[217] and that it was undesirable to participate in certain financial operations then undertaken by the Bank, particularly the trade in gold.[218]

In 1983, Congress ordered a new study of possible United States' participation in the BIS.[219] The report which followed indicated that there was "no urgent need to change the current relationship" between the Bank and the United States.[220] The reasons offered were wholly inadequate and, in some instances, disingenuous. For example, the report noted that the BIS Statutes would have to be amended to accommodate the United States' participation and that this might raise the specter of wholesale reforms in the legal authority of the Bank.[221] However, since the statutes have been changed for technical reasons in the past, it is unlikely that any change to articles nine and twenty-eight will require much debate to allow the Chairman of the Federal Reserve Board and his designate to assume their seats.[222]

A more significant concern raised by the Report is that it may be inappropriate for the United States to become party to the financial operations of an institution whose capital is partly privately-held.[223] The irony of this argument is notable since it was precisely because of the United States' declining to take a role in the Young Plan, and in the subsequent founding of the BIS, that its subscription of shares was offered to a consortium of commercial banks and later to the public. But ownership of shares does not entitle any non-governmental entity to a say in the operations of the Bank.[224] There could thus be no risk of a conflict of interest with private parties.

The Report also contended that "greater involvement in some of the operational aspects of the BIS . . . could result in the Federal Reserve having to

214. *See supra* note 38.

215. *See supra* note 34.

216. *See supra* note 37.

217. U.S. SECRETARY OF THE TREASURY, CHAIRMAN OF THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, AND U.S. SECRETARY OF STATE, UNITED STATES MEMBERSHIP IN THE BANK FOR INTERNATIONAL SETTLEMENTS, Report to Congress, Nov. 30, 1984, at 13 [hereinafter Report to Congress] (available from the U.S. Department of the Treasury Library).

218. *Id.* at 13-14.

219. *See* Act of Nov. 30, 1983, Pub. L. No. 98-181, Title VIII, § 813, 97 Stat. 1276 (codified at 22 U.S.C.A. §§ 286b-2(b)(1) (West Supp. 1987)).

220. Report to Congress, *supra* note 217, at 2. *See also An Aloof Role at Basel Bank*, N.Y. Times, Jan. 7, 1985, at D2, col. 1 (summarizing this Report to Congress).

221. Report to Congress, *supra* note 217, at 16.

222. *See supra* note 38.

223. Report to Congress, *supra* note 217, at 15.

224. BIS Statutes, *supra* note 36, art. 15.

defend some of the activities of the BIS about which the United States may have reservations."[225] If this statement is a reference to BIS policies that may negatively affect U.S. fiscal or monetary policy, then it is completely unfounded. Any member nation of the Bank has the power to veto BIS operations affecting its accounts or financial position.[226] The Federal Reserve's policies could not possibly be embarrassed by the Bank. Indeed, the concern of having to defend international banking action is better reserved for the organs of the United Nations system, including the IMF and World Bank, than for the nearly depoliticized BIS.

Moreover, the BIS Board's decision-making procedure should be quite attractive to the United States. Although a simple majority is required for many decisions,[227] and a two-thirds vote for important matters,[228] the Board, in reality, operates by consensus, which means any member can block an undesired course of action.[229] This method of taking decisions may prove to be more durable than the weighted-voting system in the IMF and World Bank, which has recently come under increasing scrutiny and criticism.[230]

The United States' final reason for not taking its place on the BIS Board is that it would not really increase U.S. influence with the institution.[231] The United States indeed now participates informally in the work of the BIS. Federal Reserve representatives are observers at the annual business meetings, and attend the regular sessions of the Group of Ten.[232] However, it is the Board that sets policy for the Bank and, more importantly, guides the operations that would be most essential in any intervention for resolving a debt crisis. The Board's approval would be necessary for any extension of emergency credits or for the assumption of a trustee role in an international settlement, the two options for Bank activism discussed above. Though the United States may be able to indirectly influence BIS decision-making, they cannot claim to have any significant or direct impact without assuming a seat on the Board.

The Federal Reserve's participation on the BIS Board would allow the United States to influence directly the work of the Bank in formulating plans for managing the next phase of the debt crisis. This might involve launching lifeboat operations of short-term lending, when IMF resources are limited or are unavailable to a debtor nation facing imminent default. Although the Bank, as an inherently conservative institution, would obviously prefer involvement in long-term solutions to the debt problem, it cannot overlook its

225. Report to Congress, *supra* note 217, at 15.

226. *See* BIS Statutes, *supra* note 36, art. 30. *See also supra* note 39 and accompanying text.

227. BIS Statutes, *supra* note 36, art. 34.

228. *Id.* arts. 9 (increasing or reducing capital), 22, para. L (establishing own agency) and 59 (requirements for amending statutes).

229. Report to Congress, *supra* note 217, at 6.

230. *See* F. LISTER, DECISION-MAKING STRATEGIES FOR INTERNATIONAL ORGANIZATIONS: THE IMF MODEL 111-19 (1984).

231. Report to Congress, *supra* note 217, at 15.

232. *Id.* at 6. *See also* ECONOMIST, *supra* note 4, at 50.

role as the lender of last resort under the conditions described above. United States and, perhaps more importantly, Japanese official involvement in these lending operations would be essential for their success. The promising avenues of debt restructuring that the Bank might pursue likewise depend on the agreement of commercial creditors in the United States and Japan. The resistance of these creditors may only be overcome by their central banks' participation on the BIS Board.

CONCLUSION

The Bank for International Settlements has the capacity to play a significant role in today's debt crisis. It can continue to foster central bank cooperation. It can undertake new trustee functions, including the conversion of sovereign debt into commercial equity. It can become a type of "lender of last resort" if it works with the IMF and follows BIS lending guidelines. Admittedly, no single international financial institution will be able to develop the wide-ranging consensus and commitment of resources needed to avoid a financial apocalypse. But the BIS has proven that it is able to take a role in the process, a role that will emphasize both short-term stability and aversion of default while also planning for the next stage of restructuring. After all, the Bank was born in the darkest years of international banking and was an essential instrument of what was then considered to be the most radical and innovative debt restructuring plan ever. Even though debt moratoriums and global war intervened, the Bank effectively managed to retire Germany's reparation debt.

The United States should reconsider its past decisions and assume a place of responsibility with the Bank. With the support of the most interested and capable central banks, the BIS may well be the first institution to take the decisive steps towards resolving today's debt travails.