Floating Currencies, SDRs, and Gold

Further Legal Developments

Introduction

The changes that have occurred in international monetary arrangements in the period since August 15, 1971 have provoked novel problems of international and domestic monetary law. It is useful to recall briefly some of the main events:

(1) From August 15, 1971 to December 18, 1971, following the declaration by the President of the United States that holdings of U.S. dollars by the monetary authorities of other countries would not be converted by the United States, many currencies, including the U.S. dollar, floated independently. Although the par value system established by the original Articles of Agreement of the International Monetary Fund still remained in force legally, the system was not in operation. The decision of the Fund of December 18, 1971[1] that accompanied the Smithsonian agreement attempted to introduce an orderly system of relationships among the currencies of all members of the Fund on the basis of par values and "central rates" coupled with margins for exchange transactions that were wider than those permitted by the Articles. Central rates were defined directly or indirectly in terms of gold. The maintenance by members of central rates, whether with or without the wider margins included in the decision, or the maintenance of par values and wider margins in accordance with the decision, did not bring these practices into conformity with the Articles. Conformity required that exchange transactions be conducted within margins around parities that were consistent with the Articles. In short, the exchange arrangements defined by the decision, although designed to achieve maximum stability, were nevertheless extralegal.[2]

(2) In March 1973, the objective of the Smithsonian agreement of fixed relationships among all currencies was abandoned by members of the Fund. On November 7, 1973, the Fund adopted a revised decision on central rates and wider margins that was based on the pattern of the

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original decision, except that the revision permitted the establishment of a central rate defined in such a way that it might be impossible to relate it to gold.[3]

(3) On June 13, 1974, the Fund adopted a decision that became effective on July 1, 1974, under which the special drawing right (SDR) is valued on the basis of a "basket" of 16 currencies.[4] The decision is reproduced in Appendix A. This method of valuation was adopted for the purposes of operations and transactions in SDRs conducted through the Special Drawing Account of the Fund. The SDR is defined in terms of gold in the Articles.[5] The valuation was deemed, therefore, to define gold value, and it was applied in the operations and transactions conducted through the Fund's General Account as well.[6] In this way, the SDR as defined according to the new method of valuation became the unit of account of the Fund for all practical purposes in the application of the Articles. The Fund's decision on its use of the SDR as the unit of account is reproduced in Appendix B.

(4) On April 30, 1976, the Board of Governors of the Fund approved the draft of a comprehensive second amendment of the Articles that had been prepared by the Executive Directors. The proposed second amendment will take effect when accepted by three fifths of the members of the Fund representing four fifths of the total voting power of all members.[7]

Pamphlet No. 19[8] in this series surveyed certain legal developments that had occurred already or that seemed imminent as a result of the transition from the Bretton Woods system of par values based on gold as the common denominator to the arrangements that will be governed by the second amendment of the Articles. The present pamphlet discusses further developments in the complicated process of change that will undoubtedly continue for some time to come.

The canvas is a broad one, and a pointillist technique must be employed. Nevertheless, a clear picture is emerging. Units of account in treaties and in the domestic legal provisions that give effect to them are ceasing to be based on gold. As a result, gold is rapidly losing one of its traditional monetary functions and the SDR is undertaking much of this function. Members are applying diverse exchange arrangements. Some currencies are floating independently while others are pegged to particular currencies or to combinations of them. The par values of currencies established under the Articles will be abrogated for the

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purposes of the Articles when the second amendment becomes effective.[9] The courts must decide what effect to give to par values or to gold-value clauses when referred to in contracts or legal instruments. They must also decide whether to modify established legal principles because of the new conditions. Courts are disposed to find practical solutions for all these problems.

Floating Currencies

Effects on New Legislation

The proposed second amendment of the Articles of Agreement is responsible for three classes of legislation that members of the Fund have adopted or are in the process of adopting. The first and most obvious class is legislation that amends the member's Bretton Woods legislation in order to authorize the member to accept the proposed second amendment of the Articles and to enable it to perform its obligations under the Articles when amended. The second class also is legislation that was to be expected. It consists of measures to modify or abrogate the domestic law by or under which a par value for the member's currency is established. The third class consists of a variety of measures that are considered necessary or desirable because of the changes introduced by the other two kinds of legislation. For example, the amendment of the Bretton Woods Agreements Act of the United States,[10] which is to take effect on the occasion of the proposed second amendment of the Articles, has modified the Gold Reserve Act of 1934 (31 U.S.C. 405b).[11]

The 1934 statute, which is entitled "An Act to protect the currency of the United States, to provide for the better use of the monetary gold stock of the United States, and for other purposes," dealt, among other topics, with the Exchange Stabilization Fund, and provided in Section 10(a) as follows:

> For the purpose of stabilizing the exchange value of the dollar, the Secretary of the Treasury, with the approval of the President, directly or through such agencies as he may designate, is authorized, for the account of the fund established in this section, to deal in gold and foreign exchange and such other instruments of credit and securities as he may deem necessary to carry out the purpose of this section. An annual audit of such fund shall be made and a report thereof submitted to the President.[12]

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