

Wallace III

April 10, 1941

Dear Mr. Wallace:

I shall be very pleased to come to your conference at the May-Adams House on Saturday, May 3rd. Thank you for inviting me.

Sincerely yours,

Winfield W. Riefler

Henry A. Wallace, Esq.
Wardman Park Hotel
Washington, D. C.

HENRY A. WALLACE
WARDMAN PARK HOTEL
WASHINGTON, D.C.

April 9, 1941

Dear Mr. Riefler:

Sooner or later, the day will come when something will have to be said about the concrete aims of our national effort. This day may not come for several years. On the other hand it may come much earlier. It occurs to me that it might be a good idea for a few of us to spend an evening together having a private and off-the-record talk regarding this matter.

I imagine you would agree with me that when aims are finally stated they should:

- (1) Reflect the responsible opinion of both parties and the various regions of the country.
- (2) Result from prolonged consultation rather than momentary judgment.
- (3) Represent commitments which it seems reasonable to suppose the United States might be specifically willing to undertake and carry through over a period of years.

I am writing to invite you and the others on the attached list to meet me in Washington on Saturday, May 3, for an informal conversation along these lines. We will meet at 5 o'clock at the Hay Adams House, have supper there and talk for the rest of the evening.

Obviously, the purpose of this conversation is not to prepare a statement. The time has not come for that. The value of our being together will consist in the exchange of views and the discovery of the direction in which our minds are moving.

Sincerely yours,

Mr. Winfield W. Riefler
Institute for Advanced Study
Princeton, New Jersey

H A Wallace

Hamilton Fish Armstrong
Council on Foreign Relations
45 East 65th Street
New York, New York

Dr. Isaiah Bowman
Oak Place
Baltimore, Maryland

David Cushman Coyle
1719 H Street, N. W.
Washington, D. C.

Allen W. Dulles
48 Wall Street
New York, New York

Major George Fielding Eliot
19 East 88th Street
New York, New York

Mark Ethridge
Courier Journal
Louisville, Kentucky

Alvin H. Hansen
Graduate School of Public
Administration
Harvard University
Cambridge, Massachusetts

Stacy May
4949 Hillbrook Lane
Washington, D. C.

Francis P. Miller
Council on Foreign Relations
45 East 65th Street
New York, New York

Paul Scott Mowrer
Chicago Daily News
Chicago, Illinois

Charlton Ogburn
Union Trust Building
Washington, D. C.

Winfield W. Riefler
Institute for Advanced Study
Princeton, New Jersey

Whitney H. Shepardson
213 East 61st Street
New York, New York

Charles P. Taft
Dixie Terminal Building
Cincinnati, Ohio

Jacob Viner
University of Chicago
Chicago, Illinois

W. W. Waymack
Register and Tribune
Des Moines, Iowa

M. L. Wilson
14 Rosemary Lane
Chevy Chase, Maryland

Helen Hill Miller - Secretary
National Policy Committee
1202 National Press Building
Washington, D. C.

Mr. Morris Ernst
Greenbaum, Wolff and Ernst
285 Madison Avenue
New York, New York

June 21, 1941

Honorable Henry A. Wallace
Wardman Park Hotel
Washington, D. C.

Dear Mr. Wallace:

Thank you very much for your invitation to reconvene our
group on Saturday, July 13th. I shall plan to be present.

Sincerely,

Winfield W. Riefler

HENRY A. WALLACE
WARDMAN PARK HOTEL
WASHINGTON, D.C.

June 20, 1941

Dear Mr. Riefler:

A number of the men who attended our dinner on May 3 have suggested the desirability of a further conversation, so I am writing to ask the group to reconvene on Saturday, July 12.

In order to focus our talk, the enclosed agenda has been prepared.

As before, we will meet at five o'clock (Eastern Standard Time) in the same room at the Hay-Adams House.

Sincerely,

H A Wallace

Mr. Winfield W. Riefler
Institute for Advanced Study
Princeton, New Jersey

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JULY 12

Assumptions:

1. That we are talking chiefly about the second of the three periods mentioned on May 3--namely the period of post war transition.
2. That the instrument of order during this transition period will be an American-British agreement.

1. Given these assumptions what should be the wartime relationship between the United States and the British Commonwealth? Possible alternatives are:

- a) Associated powers (as in 1917-19)
- b) A defensive alliance
- c) Step by step joint action accompanied by the creation of joint agencies to express common objectives, and to employ their force to realize these objectives
 - (1) What are the principal objectives?
 - (2) What agencies are required?

2. What steps might be taken now to organize an American-British trade area including:

- a) Removal of trade restrictions within the area
- b) Agreement upon a common area financial policy
- c) Disposition of surplus raw materials

3. If the United States and the British Commonwealth undertake a post-war program of joint action, what kind of permanent governmental procedures are required to carry out such a program? What kind of American governmental procedures? What kind of American-British governmental procedures?

4. What steps could the United States and the British Commonwealth take now, at the peace settlement, and during the transition period after the war to pave the way for a world-wide system of collective security?

**OFFICE OF THE VICE PRESIDENT
WASHINGTON**

July 23, 1941


Mr. Winfield Riefler
Princeton University
Princeton, New Jersey

Dear Mr. Riefler:

The Vice President is going to New York on Friday afternoon of this week, and he has a matter which he is very anxious to talk over with you. He wonders if it would be possible for you to ride with him from Trenton to New York on the train.

He is leaving Washington at 2 P.M. on the Pennsylvania Railroad, train No. 170, which stops at Trenton, New Jersey at 4:49 P. M., E. S. T. Mr. Wallace will be in car No. 702, drawing room A. If it is possible for you to make this trip with the Vice President, will you please wire us confirmation, so that he will know whether to expect you at Trenton.

Sincerely yours,


Mary Huss
Personal Secretary to
The Vice President

VICE PRESIDENT'S OFFICE

July 24, 1941

Secretary to
Mr. Winfield Riefler

Here is a copy of the letter sent to Mr. Riefler this morning. Just thought you might like to have this for your information.

When you see him in New York Monday, you might want to bring this up if, by chance, the original did not reach him.



Mary Huss
Personal Secretary to
The Vice President

July 24, 1941

**AIR MAIL
SPECIAL DELIVERY**

**Mr. Winfield Riefler
Orleans, Massachusetts**

Dear Mr. Riefler:

I am writing you at the suggestion of the Vice President. He has a matter which he is very anxious to discuss with you, and endeavored to get in touch with you at Princeton yesterday but found that you were away from the University for a few days.

It is our understanding now that you will be in Washington on next Thursday. Since Mr. Wallace is leaving the city Wednesday night, and since he would like very much to have this discussion with you before he goes, he wonders if it will be possible for you to come to Washington on Wednesday.

We will be very glad to hear from you at your earliest convenience as to whether you can come at that time.

Sincerely yours,

**Mary Huse
Personal Secretary to
The Vice President**

October 2, 1941

Honorable Henry A. Wallace
The Vice President of the United States
Washington, D. C.

My dear Mr. Vice President:

Enclosed you will find a preliminary draft of a program to stimulate international investment in underdeveloped regions. It represents a further elaboration of the ideas about which we talked last Summer. I am very anxious to have your reactions.

The program proposed is novel in many respects. It envisages a complete reversal of the trends that have come increasingly to dominate the international economic scene since 1914. How utterly essential it is to reverse these trends is symbolized nowhere so strikingly as in the huge stocks of gold which this country owns at the present time. To an important degree, this gold has come to us, not to go to work, but in search of safety.

In a very fundamental sense, the program proposes to put this gold to work. It seeks to restore security to investment abroad, provided, first, that it is genuine investment, i.e., equity investment prepared to take economic risks, and provided, secondly, that it is investment that accepts its social responsibilities.

The program is designed, particularly, to stimulate investment in the underdeveloped regions of the world. These regions today are characterized all too frequently by over-population, and are cursed with persistent under-employment, malnutrition and poverty. Yet often they are rich in resources and lack mainly enterprise and investment to solve their problems. This program should create the conditions necessary to permit our enterprise and skill, and our huge latent power to invest, to go to work in these regions.

Personally, I can conceive of no more appropriate task to which to dedicate our gold.

Very sincerely yours,

Winfield W. Riefler

October 4, 1941

Mr. Milo Perkins, Executive Director
Economic Defense Board
Washington, D. C.

Dear Mr. Perkins:

Enclosed you will find a preliminary draft of a proposal to stimulate international investment. I am sending a second copy by this same mail to the Vice President.

I would appreciate it very much if you could find time to read the manuscript in detail and advise me of your reactions. If the manuscript is acceptable as a basic working document, subject to subsequent modification and elaboration, I would like to have it mimeographed immediately so that we will have copies to submit to the various consultants.

I have not shown this draft to anyone as yet. During this next week I plan to hold extensive conferences on it with certain of my colleagues here at the Institute for Advanced Study, including certain of the League of Nations experts, and also with certain of my research associates of the National Bureau of Economic Research. The program in general terms is also due for discussion on Saturday, October 11th, among the Economic and Financial Group at the Council on Foreign Relations.

These are my specific plans to date. Do you want to arrange for Mr. Ogburn to come. I would be pleased to have him at any time. Would you mind if I invited Thomas Blaisdell of the National Resources Board to come up and go over the program this week? He called me yesterday on the basis, I believe, of a conversation with you. I would rather like to have him. Finally, do you want me to come down to Washington for a discussion with you or with the Vice President. Wednesday would be best from my point of view, if you do.

Very sincerely yours,

Winfield W. Riefler

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A PROGRAM TO STIMULATE INTERNATIONAL INVESTMENT

Winfield W. Riefler
Princeton, New Jersey
October 4, 1941

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A Program to Stimulate International Investment

Purpose of the Program

It is the purpose of this program to demonstrate, concretely, a means by which the democracies can implement now the Peace Aim, "Freedom from Want." The program proposes, through the use of public guaranties, to establish a more just and more secure basis for the flow of international investment funds. It is designed

- A. To stimulate the investment of an adequate volume of equity funds in corporations operating across national boundaries;
- B. To provide particularly for the economic development of under-developed regions, e.g., the Caribbean, the Danube Valley, China, the Dutch East Indies, Latin America;
- C. To remove, on the one hand, the fear that native populations and resources will be subject to exploitation in the interests of capital investment, and, on the other hand, the apprehension that productive enterprises will be discriminated against or confiscated, once they have been successfully established;

The program contemplates a bold and imaginative stroke of economic statesmanship. From a political point of view it assumes

- A. The defeat of the Axis;
- B. A democratic solution of the political problem of international security based on a nucleus of British-American understanding;
- C. The adoption of policies designed to reverse the accentuated trend toward economic nationalism that dominated much of the pre-war scene.

If the general lines of the program are acceptable, steps should be inaugurated immediately toward its execution in order that it may be in full operation during the period of post-war reconstruction. The mechanism proposed has been designed to permit the utmost flexibility in meeting the strains that may develop at that time.

It should be noted that this program does not cover all phases of reconstruction investment problems. A supplementary memorandum, devoted particularly to publicly financed investment, including inter-governmental advances, is in course of preparation.

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2.

The Program

It is proposed

- A. That the governments of Great Britain and the United States undertake immediately by joint action to establish an International Development Authority; such Authority to be organized and to begin operations as soon as possible;
- B. That the International Development Authority be authorized to grant corporate charters to international enterprises -- private, public, or mixed -- that propose to engage in genuinely productive economic activities;
- C. That the area of investment of enterprises so incorporated be limited to countries that register their formal approval of this program and their desire to participate in its benefits;
- D. That the benefits of international incorporation be conferred only on enterprises that make adequate provision to meet the social obligations of enlightened management with respect to such matters as
 - (a) Working conditions
 - (b) Social insurance
 - (c) Housing
 - (d) Sanitation and other community facilities
 - (e) Participation, where possible, of local management and capital.
- E. That the International Development Authority receive a share of all profits accruing to enterprises to which it has issued charters of incorporation;

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- F. That provision be made that a further share of the profits of internationally incorporated enterprises accrue to the governments of the countries in which they operate;
- G. That the local governments exercising jurisdiction over internationally incorporated enterprises agree to refrain from all discrimination against the operations of these corporations by taxation, by administrative regulation, or otherwise;
- H. That the International Development Authority be authorized, subject to appropriate limitations, to commit itself to exchange its own debentures for the stock of all internationally incorporated enterprises at the option of the holder of such stock;
- I. That the World Court have legal jurisdiction over all disputes, suits, etc., arising out of the operations of this program, both with respect to the activities of the International Development Authority and with respect to enterprises to which it has issued charters of incorporation;
- J. That the Authority take all steps in its power to prepare for a quick expansion of activity as soon as a cessation of hostilities may permit.

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Discussion of Specific Details of Program

The discussion that follows is based on the assumption that the general program suggested above is sufficiently attractive to merit exploration. It covers specific details of the program, alternative methods of approach to certain of the problems raised, and appropriate procedures required to further its inauguration. In each section, specific notation is made of the problems which require decision.

The left hand margin of each page is available for notation and space is left below each query for answers. The discussion is organized according to the outline below.

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6.

A. Financial Inducements to Investment

To succeed, this program must induce investors, at a time when all economic horizons are obscure, to make plans to expand existing industries and to develop new industries outside of our borders. In particular, the inducement must be strong enough to encourage new ventures in the less fully developed regions of the world. It is important that these plans be matured rapidly so that active operations may be undertaken as soon as the state of hostilities permits. The financial inducement offered in this program consists of a positive guaranty to the investor that, at the worst, he will get his money back. It is proposed that this guaranty take the form of a commitment issued by the International Development Authority, in which the Authority undertakes to exchange its own debentures for shares of internationally incorporated enterprises at the option of the holder of those shares.

The exact nature of this guaranty, the terms in which the commitment to exchange is issued, will determine the success or failure of the program. The Authority must issue its commitment in specific form at the time it grants a charter of international incorporation to enterprises proposing to operate abroad. It must specify at that time the face value of the debentures which it commits itself to exchange for shares of the new enterprise as well as the maturity of such debentures and the rate of interest they will carry. Exactly how should the Authority determine the basis of exchange of these debentures? Should it be guided solely by the amount of the original investment represented by each share, or should it promise to take into account the book value of the stock at the time the option is exercised? Should it disregard or take into account dividends that may have been paid on such stock prior to its presentation for exchange? For how long should the commitment run? In what currency should it be written? How should stock issued at time of incorporation in exchange for promoters' services be treated? What treatment should be accorded to stock issued by the new corporation in exchange for concessions or for existing capital facilities? How would decision on these points be affected by current taxation practices?

The answers to these questions will determine the equity of the program as well as its success in providing incentives to invest, particularly incentives sufficiently powerful to motivate investment under present obscure conditions.

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7.

Suggestion - Commitment to Guarantee

Let decision on these details be guided, first, by the principle that the financial incentive provided by this program is an assurance to the investor that he will, at the worst, get his money back. It will provide no guarantee of profits, nor even of a minimum rate of return equivalent to that on government bonds. For income, the investor will have to look to the success of the venture in which he places his funds and for which he assumes the responsibilities of management. Let there be complete assurance, however, not only that the investor will get his money back, but also that he will get it back, with certain minor exceptions to be noted later, at his own option, at a time chosen by him, and for his own reasons -- either because he has another use for his funds, or because he no longer regards the venture as promising.

In accordance with this principle, let the International Development Authority, at the time it grants a charter of incorporation, ascertain what proportion of the equity represents solely a new investment of cash, or of liquid cash equivalent, what portion represents an exchange of stock in the new enterprise for existing values, such as franchises, productive equipment, real facilities, etc., and what portion represents payment for promoters' services. Let the charter of incorporation distinguish clearly between these three categories of stock and let this distinction be carried to the stock itself. This can be effected by the issuance of different kinds of stock, e.g., preferred and common, or by different classes of the same stock, e.g., Class A, Class B, Class C, all three classes being identical in their provisions other than those relating to the commitments which the International Development Authority may issue. With respect to stock issued for new cash, the Authority would know and require to be printed on each stock certificate of ownership, the pro-rata value of the cash investment represented by that share of stock. To this stock it would attach a commitment giving the owner the right to exchange the stock at his option for debentures of the Authority. The interest and maturity date to be carried by such debentures would be written into the commitment, the rate of interest being governed by current market rates of interest, and the maturity being established by the Authority to conform to its own operating requirements, i.e., it should avoid the possibility that its debentures will mature in too large amounts in any one year.

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The commitment would provide that the principal, or face value, of the debentures would vary according to the time when the option was exercised. It would be determined by subtracting from the figure shown on the stock as the amount of cash investment which it represented at the time of incorporation, all cash disbursements, in the form of dividends or otherwise, paid on such stock prior to the exercise of the option. In other words, the guaranty of the Authority would be for a sum equal to original investment less dividends paid. Non-cash dividends or disbursements would be forbidden except with the consent of the Authority. In granting such consent, the Authority would determine the cash value to be imputed to such dividends on the exercise of the guaranty.

The commitment to exchange stock for debentures of the Authority would not start until one year had elapsed from the time when the commitment was issued. In the case of successful enterprises, the commitment would be ended whenever dividends and other cash disbursements on the stock had equalled the original cash investment. In the case of unsuccessful enterprises in which dividends did not equal original investment, the commitment would terminate at the end of twenty years. Any stock not exchanged by that time for debentures of the Authority would lose the right to exchange.

Let stock representing solely sponsors' or promoters' equity carry no guaranty. In ventures of the type here envisaged, the promotional activity of sponsors is frequently remunerated by the assignment of a portion of the equity stock of the new enterprise. While this practice may be a source of abuse, it may also be entirely justified. It may constitute, in fact, an excellent device for the sharing of future profits between those, on the one hand, who have the vision, imagination, and managerial ability to develop new ventures, and those, on the other, who are passive except for the provision of investment funds. The Authority will, of course, scrutinize and pass on such issues of stock before it grants a charter of incorporation. When it permits such issues, it should insist that they be differentiated from issues for cash, and that they carry no guaranty commitment.

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A case intermediate between these two will arise in the case of stock issued in exchange for existing real values. Few enterprises applying for international incorporation, probably, will represent 100 per cent new cash investment. Usually, they will plan to acquire existing facilities of some sort needed in the further development of the business. Frequently, payment for these acquisitions will take the form, in whole or in part, of exchange of stock in the new enterprise for the facilities acquired. This device may, in fact, be one of the ways in which the new internationally incorporated ventures carry out the requirement of the program that local management and local capital, whenever possible, be associated with these new ventures. The value to be placed on such acquisitions, however, presents certain problems. Since they are usually special purpose facilities, their liquidation value as ascertained under bankruptcy proceedings would be very low. As going concerns, on the other hand, their value for the new enterprise may be very high. Clearly this higher value might properly be the basis for the exchange of the facilities for the stock of the new enterprise.

Should stock received in exchange for existing real values be eligible for guaranty by the Authority? Clearly many cases will arise in which the Authority will decide against any guaranty for stock falling within this category, on the grounds that the sole purpose of the guaranty is to induce new investment. There may well be cases, however, where the Authority will wish to extend its guaranty, cases, for example, where the existing real values are idle and will not be risked in productive use unless some guaranty is forthcoming. In such cases, should the Authority issue a commitment to exchange debentures at the original book value at which these facilities are acquired by the new corporation, or should the commitment be for a lesser amount nearer to the liquidation value of these facilities?

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These questions will have to be decided by the Authority case by case. In general, however, it can be said that commitments issued in cases of this kind should be for something less than book value. This would be necessary to avoid one possibility of abuse of the guaranties issued by the Authority, namely, that they would be used to provide an indirect cash market at high levels for existing facilities. Since owners of these facilities would be able at the end of a year to exchange their stock for marketable debentures of the International Development Authority, the commitment value placed on these facilities cannot be so high as to furnish the equivalent of a favorable cash market. To avoid such problems, let the Authority place an original guaranty value on stock of this character that is sufficiently below its par value to prevent abuse. In all other respects, let such stock be treated in exactly the same manner as stock representing cash investment. For example, the actual face value of debentures which the Authority committed itself to issue in exchange for such stock would be determined by subtracting from its original guaranty value all dividends and cash disbursements which it had received prior to its presentation for exchange for debentures.

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Suggestion - Taxation

The treatment outlined above will require some modification in taxation policies with respect to disbursements on shares of internationally incorporated enterprises. According to present practice in the United States, dividends on shares in all corporate enterprises are treated as income, subject to the income tax. Under the new graduated rates now in effect, such taxation absorbs a very considerable portion of dividends except in the case of taxpayers falling in the very low taxable income brackets. In the case of internationally incorporated enterprises, consequently, the value of the commitments issued by the Authority would be nullified to the extent that taxes were levied on dividends received while the commitment remained outstanding.

To meet this difficulty, let the income tax base be modified to provide that dividends paid on shares with respect to which commitments of the International Development Authority are outstanding, be considered capital repayments so long as such commitments are in effect. This would mean in practice that disbursements on that portion of the stock of internationally incorporated enterprises that represented real investment would be free from taxation until such disbursements equalled the original investment. This procedure should not involve serious administrative difficulties. The shares of internationally incorporated enterprises would be distinguished into classes in accordance with the value and nature of the commitment which the Authority had issued with respect to each. Shares representing promoters' equity would not be affected and dividends on such shares would be fully subject to income taxation as at present. Classes of shares on which commitments had been issued by the Authority, on the other hand, would have printed on their face the original amount of that commitment. The cash disbursements made on such shares would, of course, be a matter of public record. The current value of the commitment, therefore, would be readily ascertainable as the positive difference between these two sums. On this basis, the marketability of the shares would be preserved, since any potential

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buyer would know exactly the current value of the commitment that attached to the stock and the status of dividends from such stock for tax purposes. Once dividends on such stock equalled the original cash actually invested in such new enterprises, or, in the case of shares issued in exchange for existing facilities, equalled the guaranty value placed on such shares by the Authority, further dividend disbursements would be subject to full taxation as at present. This modification would preserve the value of the Authority's commitment, namely, that it guaranteed to the investor the full return of his original investment at a zero rate of interest. It would, also, probably constitute an inducement to investors to undertake investment in enterprises chartered by the Authority

Should this modification be adopted, it would necessitate a corresponding modification in the capital gains tax in this country. At present the capital gains tax is levied on the excess, if any, of the amount for which stock is sold as compared with the amount for which it was purchased. Intervening dividend disbursements are not considered. To prevent the modifications suggested above from leading to tax evasion, it would be necessary, in the case of shares with respect to which commitments of the Authority were outstanding, to provide that on sale of such stock the capital gains tax be levied on a basis that takes account of the full amount by which its selling price exceeds the guaranty commitment of the Authority on the date of sale.

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13.

Comment

This novel procedure has been worked out to meet the specific problem posed by the nature of the guaranties proposed in this program. It is not out of line, however, with basic economic principles. From a theoretical point of view, economists have long recognized that equity investments lose all stated cash value as soon as they are made. Once cash is invested in fixed plant and equipment, its value represents a capitalization of the value of the services which that fixed capital is expected to produce. The investor, in other words, exchanges a current cash value for a series of expected future cash returns. These may take the form either of dividends or of cash received on sale of the equity. Cash receipts on either or both of these accounts, moreover, may be negligible. Given these basic conditions, it might perhaps be wiser for investors to consider their first dividends not as income but as repayments of the principal which they had ventured. They would then treat as income only those receipts which accrued to them after their cash returns had equalled their original investment. Considered from this point of view, such income receipts might, of course, include cash received on the sale of their investments.

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14.

Query

- (a) What detailed adjustments would have to be made in the American tax laws to carry out this suggested procedure?
- (b) What adjustments would have to be made in the British tax laws to accomplish a result comparable to that suggested for the United States?
- (c) In what currency should debentures be issued? A strict construction of the guiding principle, namely, that the investor should be assured that he would get his investment back and nothing more, would require that the debentures of the Authority issued in exchange for stock be in the same currency as the cash investment originally represented by such stock. Investors, of course, would prefer that the debentures be issued in the strongest currency -- at present, dollars. In these days of fluctuating exchanges and blocked currencies, the issuance of debentures in dollars, where desired, would provide a powerful inducement for foreign owners of foreign facilities to seek American capital to expand their enterprises. Would it or would it not be wise to give the Authority discretion to depart in this instance from a strict construction of the primary guiding principle advanced above and permit commitments to be issued in dollars, on occasion, without regard to the currency of original investment?

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15.

B. Determination of Social Standards with Respect to

- (a) Working Conditions
- (b) Social Insurance
- (c) Housing
- (d) Sanitation and other community facilities.

One of the worst indictments of large scale industry is that, due to the separation of management and ownership, the managers of large enterprises may seek to maximize profits at the expense of decent wages and working conditions for their employees. The implications of this indictment have especial significance in connection with a program such as the one which is here proposed, for this program plans definitely to stimulate the investment of American funds in underdeveloped areas, many of which are remote geographically from this country. It plans to make British and American skill and management techniques available for the development of the resources of these areas and thus contribute to a solution of their pressing economic problems. These skills and techniques, however, would be definitely associated with the management of these enterprises, while their ownership would inevitably, in a great number of cases, be vested in residents of this country or of Great Britain. Taking into account the primitive conditions that exist in many regions where investment will take place, there would ordinarily be a distinct danger that some of the enterprises stimulated by a program such as is here proposed would become identified with all of the abuses of "absentee ownership." It is to preclude this possibility that the program stipulates, as a condition prerequisite to international incorporation by the International Development Authority, assurance that such corporations are aware of their social responsibilities and will conform to modern standards of enlightened management with respect to working conditions (including remuneration), the social insurances, housing, sanitation, and other community facilities. That these standards can be met has been amply demonstrated in the past and is being demonstrated now in the foreign operations of a very great number of existing large scale enterprises.

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16.

How can this prerequisite be effectuated? Are there standards with respect to these social aspects of investment that can be stated in literal form, embodied as it were in an enforceable contract? Are they universally applicable or must they be individually adapted to each community? How can they be enforced? These are perplexing questions which require extensive discussion in the course of preparation of this program.

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17.

Suggestion

Let one of the Directors of the Authority be definitely chosen from the group that has been associated with the International Labour Office, for this office has devoted more attention to a study of these problems than any other. Such an appointment would introduce into the inner mechanism of the Authority a deep concern for and an intimate familiarity with the whole area of industrial standards.

Let the Draft Conventions prepared by the International Labour Office be analyzed from the point of view of the problems here posed. They represent the fruits of years of conference and study devoted specifically to the problem of introducing and enforcing higher industrial standards with respect to social conditions on an international basis. Many of these Conventions may not be directly applicable to the problems at hand, since they were prepared with a different purpose in mind, i.e., they were prepared primarily for the purpose of leveling up social standards in the more advanced industrial countries. Even though these Conventions may be subject to this criticism, it should be possible to adapt them to the requirements of this program.

Finally, let the Authority maintain current contact with enlightened managements that are facing successfully the problems of meeting decent working standards, especially those managements that are operating under primitive conditions. The Authority will be able to secure a detailed understanding of the problems involved and the techniques that have proved most successful in their solution.

In developing standards, it is essential that the Authority avoid the danger that they become a concealed form of economic nationalism. That is, they should not be drawn up nor should they be administered in such a way as to prevent new investment in new areas and thus protect the vested interests of the more fortunate industrialized regions.

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18.

Query

Are there other sources of experience on the problem of industrial standards that can be tapped by the Authority?

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19.

C. Position of the World Court

It is an underlying conception of this program that corporations engaged primarily in international economic activities will function more effectively for the general welfare if they derive their corporate powers from an international body and are subject to the jurisdiction of an international court. It is believed that in this way the operations of large-scale international industry can be subjected to governmental restraints without taint of intervention, imperialism, and economic nationalism that has beclouded this relationship hitherto.

In the absence of international political institutions, and particularly, of a system of international courts to which to appeal, large-scale international economic activities are bound to be surrounded with suspicion and friction. Foreign officers of state, particularly of powerful states, have frequently adopted the policy of pushing the interests of their nations without regard to the interests of other parties. When they have, on the other hand, at times adopted a policy of hands off, there have been numerous instances when the interests of their nationals have been unjustly disregarded. There have been cases where international corporations have meddled in local politics in foreign countries and then called on their governments for help when parties they had been opposing gained control. There have been other instances when international corporations, because they failed to secure effective representation on their behalf from their own government, have sought to preserve themselves from discrimination by embarking into local political activities. These various sources of friction and trouble reflect mainly one great lack, i.e., the absence of any international source of corporate authority and the correlative absence of a system of international courts. Without international courts of appeal to exercise judicial review of the thousands of situations when international economic activities clash, there cannot help but be friction and trouble.

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It is contemplated in this program that the World Court will perform this essential function. It would be the court of jurisdiction over such cases, for example, as disputes over the powers assumed by the Authority invoking a review of the legal acts under which the Authority was established; disputes concerning the activities of corporations incorporated by the Authority to determine whether they had or had not exceeded the limits of their corporate powers; disputes concerning the accounting practices adopted by corporations holding international charters, in determining net income and thus the share of their profits that accrued to the Authority and to the governments of the states in which they operated; disputes with respect to the value of property held by corporations and the amount of compensation due thereon when such property was taken over by public authorities under their powers of eminent domain, and finally, disputes with respect to the interpretation of discrimination, determining whether or not a given administrative act of a local government constituted an act of discrimination with respect to an internationally incorporated enterprise. It should be realized that these problems of discrimination will doubtless be the most difficult for the Court to decide. They will come nearer to involving national prestige than any other questions, and will seem to approach more closely to an infringement of local sovereignty. It is hoped that the benefits of the whole program undertaken by the Authority will be sufficient to induce states to make this concession.

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Query

Is the World Court now capable of assuming the important functions suggested in this program? If not, how should it be reorganized?

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22.

D. Problems of Definition

1. Enterprises Eligible for International Incorporation

This program is directed specifically toward stimulating a flow of investment out of creditor countries into underdeveloped regions. A new corporation organized by American capital to develop the steel industry in Brazil would constitute a perfect example of the type of enterprise in terms of which the program has been conceived. In actual operation, however, a great proportion of the applications will fail to conform so closely to the type of investment visualized. It is essential to explore these possible variations in advance in order to state with greater exactitude what may or may not constitute an eligible application.

(1) Productive Enterprises

One range of problems will center around the definition of the phrase "productive enterprise," since to be eligible for international incorporation, applicants must propose to engage in "productive enterprise." Just what is meant by "productive enterprise?"

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Suggestion

Productive enterprise clearly envisages an operation in which, if it is successful, receipts will more than cover costs of operation. It also envisages an operation in which the investment of capital is a major rather than an incidental element and in which success is dependent to a considerable extent on qualities of management. Such enterprises would ordinarily be privately owned, but there is no reason to prevent their being publicly owned, or enjoying a mixed ownership. Enterprises that propose to engage in extractive operations, in large scale agricultural and raw material production, in processing, or in manufacture, clearly fall within the scope of the operation here envisaged. Investment trusts holding assets in the form of foreign securities clearly fall outside. In between these extremes there are a variety of cases requiring consideration, such as

- (a) Merchandising enterprises in wholesale and retail trade;
- (b) Radio chains, movie chains, local advertising agencies;
- (c) Insurance companies, banks, and finance companies;
- (d) Transportation enterprises, railroads, bus and truck companies, aviation lines, and water shipping services;
- (e) Self-liquidating public works, dock and harbor facilities, toll bridges.

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24.

Query

Should an attempt be made to write specific requirements covering types of eligible operations in the legal charter of the Authority, or should these problems be left to the administrative discretion of the Authority itself?

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25.

(2) "Economically Sound."

Other difficult problems of definition will center around the phrase "economically sound." What sort of operations should be defined as "sound?"

Suggestion

The phrase "economically sound" should not be defined narrowly in the sense of a "sure" venture. It is the purpose of this program to encourage investors to take risks. The program would be defeated if charters of incorporation were limited to ventures whose successful operation could be taken for granted. The phrase should be defined, on the other hand, so as to exclude "wild cat" ventures, to say nothing of downright frauds. There should be a fair chance of success, tested from the point of view of profitable operations. The successful outcome of the venture must also promise to be good on balance for the country in which the investment is located and also for the world in general. It should promise greater employment, or more abundant goods and services to its locality. It should not too greatly disrupt or bring chaos into the world markets (as would happen, for example, in the case of further investment in sugar or coffee plantations.)

"Economically sound," as used in this program, should also be defined from the point of view of the economic needs and the balance of payments of the country in which the investment takes place. A venture which had the effect of causing an outflow of exchange would be "economically sound" in the case of the United States, but "unsound" in the case of Brazil. The Authority should always appraise the effect of proposed ventures upon the balance of payments and the position of the exchanges, giving preference in each area to enterprises which tended to restore balance to these positions.

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26.

(3) Role of existing international enterprises

In many cases applicants for international incorporation under the program will not constitute wholly "new" enterprises. Part of a venture applying for incorporation may be new in the sense that the investment of new capital is involved, but part of it may be old in the sense that the venture includes the acquisition of certain existing facilities and may take the form of a merger of these facilities into the new corporation. A sharp line distinguishing between new capital and existing investment is clearly required with respect to commitments which the Authority may make with respect to its guaranties. This problem has already been discussed earlier in this memorandum. The question at issue here is whether there need be so sharp a line with respect to the granting of an international charter of incorporation.

Such a charter imposes on corporations definite responsibilities with respect to their social policies, but it also confers privileges by removing jurisdiction over certain of their problems from a local authority to that of the International Development Authority and to the World Court. It might even come about, should the program prove exceptionally successful in its legal aspects, that many of the large existing international corporations would eventually apply to the Authority for charters of international incorporation without seeking financial guaranties of any kind.

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27.

Query

Should existing international corporations that fall clearly within the scope of the program in all respects except that they are not new and do not seek guaranties, be permitted to apply for charters of international incorporation?

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28.

(4) What constitutes an international enterprise?

An enterprise wholly owned within one country, the capital of which is wholly invested within the same country, would clearly fall outside the definition of an "international enterprise." All other ventures might conceivably be so defined.

Suggestion

Let an international enterprise be defined as one in which (1) less than 75 per cent of the total capital is invested in a single State, and (2) less than 75 per cent of the ownership of the enterprise is held by citizens of the same State.

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29.

2. Profit-Sharing

The program requires that internationally incorporated enterprises shall share a portion of their profits with the governments of the countries in which funds are invested and a further portion with the International Development Authority itself. The share of profits accruing to the International Development Authority may be considered as partaking of the nature of a fee or insurance charge to reimburse the Authority for the commitments to guarantee which it assumes. The income accruing from this source would help to make the Authority self-sustaining in the long run. The other share of profits, accruing to the governments of countries in which funds are invested, have a different purpose. Their function is (1) to assure local governments that investment in their areas will not only improve their general economic situation, but also help directly to relieve their local fiscal problems, (2) to interest local governments in the success of internationally incorporated ventures by assuring direct participation in their profits. This direct sharing of profits is designed to be a substitute for certain kinds of local taxation. It will approximate, in effect, taxes on corporate net income as they are applied in the United States. Various questions arise with respect to the rates of these two shares. They require much more extensive detailed study than it has yet been possible to make and are listed below for further canvass and research. Many of them raise intricate questions quite similar to those involved in problems of double taxation.

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Query

- (a) What limit should be placed on the total of the two types of profit sharing combined, i.e., to look at the same question from the investment point of view, what is the aggregate proportion of net income that should accrue to investors to provide inducement for investment in a wide range of foreign enterprises -- 50 per cent, 60 per cent, 70 per cent?

- (b) What should be the specific share of profits accruing to the International Development Authority?

- (c) When an internationally incorporated enterprise operates in more than one country, e.g., in the case of a shipping line or airplane service, how will the respective shares of the different countries be determined?

- (d) Should the net income of internationally incorporated enterprises be exempt from taxation in Great Britain and the United States? Would they be so exempt without specific amendments to the current tax laws?

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- (e) To what extent can these profit sharing provisions be made a substitute for other types of local taxation? To what extent should the Authority insist that they be substituted before issuing a commitment to guarantee?

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321.

3. Local participation, discrimination and confiscation

The benefits of the program here proposed should be open to all countries in need of foreign investment provided the governing authorities of those countries express formally their approval of the program, their desire to participate in its benefits, and their agreement to observe its responsibilities. These responsibilities are of two kinds, (1) an agreement to refrain from discrimination against internationally incorporated enterprises, and (2) an agreement to accept the jurisdiction of the World Court on all cases involving disputes with respect to the operations of the Authority, or of enterprises incorporated by the Authority, and also, with respect to whether a specific act of local administration does or does not constitute discrimination.

The manner in which these agreements are registered must be left to experts on international law. There is one question of policy, however, that will require general consideration before specific details can be worked out by these experts. Should the International Development Authority be required to secure the formal approval of the local government of a country before it incorporates an individual enterprise proposing to invest in that country? In most cases, of course, the local government will be informed of proposed ventures. In many cases, in fact, these ventures will have been promoted by them. In all cases, it would be highly desirable that proposed ventures be welcomed by the country in which they propose to operate. A specific requirement that formal approval be given, however, might in some cases permit blackmail tactics or tend to lead to bribery of local officials.

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33-

Query

Should the legal documents establishing this program provide a valuation formula, such as original investment cost, or replacement value, to guide the Court in determining the amount and form of compensation due to owners whose property may subsequently be taken over by local governments under powers of eminent domain? Should the determination of the method of valuation as well as the amount of such compensation be assigned specifically to the jurisdiction of the World Court?

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E. Problems of Organization

1. Organized by Whom?

The proposed International Development Authority would clearly constitute a joint international agency. It would not, however, constitute a joint agency comparable to the International Labour Office, where all member states occupy the same legal position. The functions of the International Development Authority differ radically as between states governing economically developed regions, on the one hand, and states governing economically underdeveloped regions, on the other. It is the purpose of the International Development Authority, by means of guarantees, to stimulate a flow of developmental capital out of territories governed by the former into those governed by the latter. The task of establishing the Authority and of providing the funds to guarantee its operations, therefore, would seem to pertain solely to the creditor powers. States hoping to benefit from an inflow of guaranteed funds, on the other hand, would be asked to register a formal declaration of their desire to participate in the benefits of the program and of their willingness to conform to its responsibilities.

Suggestion

It is suggested that, in the beginning at least, the International Development Authority be organized as a joint agency by the governments of Great Britain and the United States. Once it is organized, invitations should be extended to all favorably disposed states to take such formal action as may be necessary to permit their countries to participate in the benefits of the program. This procedure would follow exactly the spirit and letter of Point IV of the Churchill-Roosevelt joint declaration where they pledged Great Britain and the United States to make every effort to give all states equal access to the trade and raw materials of the world.

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35.

Query

(a) Should sponsorship of the plan be limited permanently to Great Britain and the United States, or should other creditor countries be asked to join -- Holland, or (after the war) France or Germany?

(b) Should the roster of debtor countries invited to adhere to the program and to share in its benefits be limited in any way, as for example, to democracies, or to non-Axis affiliated states?

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2. In what amount should funds be allocated to the Authority?

Two primary considerations govern the amount of funds needed by the Authority to fulfill its functions. First of all, the funds under its control must be large enough in amount to provide income for operating expenses and to meet all possible losses resulting from the extension of its guaranties. Assuming proper organization and sound administration, a total allocation of \$1,000,000,000 would be ample from this point of view. It would provide income far in excess of operating costs, which after a preliminary period would probably be more than covered out of profit sharing receipts. It would also provide a more than adequate capital cushion for the guaranties, particularly so in view of the nature of the commitments assumed in these guaranties, which take the form of an exchange of debentures for equity, and in view of the value of the property acquired by the Authority whenever the guaranties might be invoked. A second and more important consideration, however, is that the funds under the control of the Authority must appear to the investor to be fully ample to meet all possible contingencies. This consideration will require a materially larger volume of funds, since investors, particularly in the early period of post-war operation, will be hesitant -- the atmosphere will still be permeated by a feeling of general insecurity, the Authority will be new and untested, there will be no record of experience to indicate to the investor the specific character of risks it is assuming through its guaranties, and there will be no indication of how large in the aggregate these guaranties may come to be. Domestically, a situation such as this could be met as it has been met in the case of the debentures of the Federal Housing Administration, by having the debentures of the Authority guaranteed by the Treasury. In the case of a joint international agency, such as is here envisaged, this device could, of course, be adopted, but it might lead under certain circumstances to friction between two governments. It would be preferable, therefore, to provide a larger guaranty fund.

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37.

Suggestion

It is suggested that the International Development Authority be allocated a total sum of \$4,000,000,000, equivalent at current exchange to £1,000,000,000. Of this amount, one-half, or \$2,000,000,000, would be subscribed by the United States government, either directly by the Treasury, or through the Reconstruction Finance Corporation. The other half, or £500,000,000, would be subscribed by the British government or by one of its agencies. Of the amount so subscribed, 5 per cent would be paid in the form of Treasury securities at the time of organization of the Authority. This means that the United States government would turn over to the Authority, Treasury bonds with a face value of \$100,000,000, while the British Government would turn over £25,000,000 in British Treasury bonds. The Directors of the Authority would be empowered to call on the two governments jointly for the remainder of the subscription in each provided (1) that the amount called for was needed to meet maturing debentures issued as a result of commitments to guarantee, and (2) that such calls were limited in any one year to not more than \$100,000,000 or £25,000,000 respectively in the case of the two Treasuries. It is suggested, finally, that the Directors of the Authority be required to allocate out of funds on hand or subject to call, reserves against guaranty commitments at the time the commitments are made. These allocated reserves might be for the full amount of the guarantee assumed or for a proportion of such guarantee. In either case, the Directors would be required to announce beforehand the amount of reserves they were establishing and the policies by which they would be governed in maintaining them.

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This procedure would appear to be sufficiently flexible to meet the exigencies of the situation. The Authority would have ample income from the Treasury securities which it received at the time of organization to meet current organizational and operating expenses, even though these might well be heavy, involving as they would costly preliminary investigations in different regions of the world. The Directors of the Authority would also be able to adapt their reserve policy to a developing situation. In the early stages of operation, they would be able to assure investor confidence by allocating reserves equal to the total amounts of investments guaranteed. Later, when they had established investor confidence on the basis of a period of experience, they would be in a position to reduce the proportions so allocated. The only calls made during the period of war financing would be limited to amounts equivalent to \$100,000,000 each. These sums, moreover, would not involve a current cash drain on the Treasuries (except for the interest involved) since they would be paid in the form of bonds. Should the program work out on a normally successful basis, its self-financing characteristics might obviate the necessity of any further calls on the two Treasuries whatever. Should it not be entirely self-financing, i.e., should losses run higher than receipts, the amounts called from the two Treasuries would be moderate in amount (not over \$100,000,000 each) in any one year. This provision would constitute a real protection to the Treasuries and would not hamper the Authority, since it would make good on its guaranties by a tender of debentures, the maturities of which could be so spaced that no more than a specified amount fell due in any one year. It should be noted, finally, that this financial set-up makes no current draft on resources -- financial or real -- needed for the effective prosecution of the war.

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39.

Query

(a) With respect to the above suggestions

- (1) Is a total allocation of \$4,000,000,000 sufficient for the Authority?**

- (2) Should it be allocated equally between Great Britain and the United States on the basis of the current rate of exchange?**

- (3) Would the immediate subscription of \$100,000,000 in United States Treasury securities and £25,000,000 in British Treasury securities provide sufficient cash in the form of interest to meet organizational and operating expenses of the Authority?**

- (4) Are the proposed limitations on future calls adequate to protect the two Treasuries?**

- (5) Are the proposed provisions with respect to allocated reserves adequate to assure investor confidence and to maintain the solvency of the International Development Authority?**

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49.

(b) Should the interest rates on the deposited securities be the same for the two countries, or should they reflect the market rates currently being paid on new long-term issues?

(c) What arrangements should be made about free exchange — should both countries agree not to restrict the conversion of exchange held by the Authority?

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41.

3. Board of Directors - Composition

The composition and method of selection of the Board of Directors for the proposed Authority presents several knotty problems. (a) The Authority itself would constitute an utterly new type of international agency for which there are no precedents. It would be charged with stimulating new investment throughout the international field, particularly into areas where economic opportunities are promising but political and social obstacles are acute. It would be responsible for the guidance of that investment according to the highest standards of social usefulness and of enlightened management. All of these considerations dictate a Board of Directors composed of far-sighted individuals with sound social instincts capable of executing a program requiring a high degree of political insight, as well as economic statesmanship. They also imply a large measure of initiative for the Board of Directors. It must have freedom of action, if it is to carry out the ideals implied in its mandate. (b) The fact that the Authority would be established by two governments as powerful as those of Great Britain and the United States and that it would develop its leadership on the basis of powers delegated jointly by these two powers would indicate that it should be so established that neither government alone could control its operations. (c) The responsibility of the Authority for social developments in smaller countries together with the influence it would be able to exert on their growth would point to the desirability of having place on the Board for citizens of states other than Great Britain and the United States. It would be difficult for the Authority to retain the confidence of the smaller countries, if the Board were composed solely of representatives of these two creditor states. (d) To do its work honestly and to retain the confidence of investors and of the populations of underdeveloped regions, the Board would have to be free from the exertion of pressure by interested political groups. (e) In contrast to these considerations, all of which point toward a Board of Directors free from control of the sponsoring governments, the Board would have to be thoroughly and directly responsible to these governments in a financial sense -- the volume of funds allocated to its control would be too great to permit it to operate without surveillance. (f) Finally, the Board would have to be relatively small. It could not function responsibly or effectively if it were unwieldy in size.

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42.

Suggestion

It is suggested that the number of Directors be fixed at nine, that three of these Directors be appointed by the government of Great Britain, three by the government of the United States, and that the remaining three be appointed in the first instance, i.e., at the time of organization, by the heads of the two governments in joint consultation, and thereafter, by the Board of Directors itself. It is further suggested that each government inform the other government of its prospective appointees, in time for that government to register such comments as it may wish to make with respect to their fitness for the position. It should be understood that the three members at large, i.e., the three appointed in the first instance by the heads of the two states acting jointly and thereafter by the Board itself, should bring to the Board a thoroughly international point of view gained on the basis of intimate contact with international problems and with social and economic problems, particularly those of small and relatively less developed countries. Because of the rapid shift in conditions, it would be dangerous to specify too directly in advance the background and contacts required for candidates for these positions. Under present conditions, however, it would be wholly appropriate if these three appointees were chosen from a group composed of individuals who had been closely identified with the work of such organizations as the International Labour Office, or that of the League of Nations, either in connection with its economic and financial services or its mandate services, or of individuals in current intimate contact with specific developments in colonial areas, or in other underdeveloped regions. Such a group would constitute a guaranty to smaller states that the legitimate interest of these states as well as those of the creditor powers would have a hearing in the Authority. It would probably be a mistake to appoint nationals of countries hoping to benefit greatly from investments guaranteed by the Authority, since this might engender too great jealousy on the part of other small states.

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43.

Query

(a) Is nine an appropriate number for the Board of Directors, i.e., is it small enough to function effectively as a Board and at the same time large enough to insure that the very important responsibilities delegated to the Authority do not depend for their observance on a single appointee who may fail to cope with them?

(b) Is the distribution of the nine, i.e., three American members, three British members and three members at large correct? Will it give adequate expression (1) to the very direct interests of Great Britain and the United States -- the two countries that are advancing the guaranties, (2) to the welfare of the regions in which investment takes place, and (3) to the broad consideration of international economic policy underlying the whole program?

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44.

(c) How can the legal documents establishing the Authority indicate the type of person required for members at large without becoming so specific as to make him a representative of a special interest or of an organization that may not continue to exist?

(d) Should some provision be made for the Board to inform international organizations of prospective selectees for members at large, giving them opportunity to make comments similar to those permitted to each government with respect to appointees of the other government? If so, how would these organizations be named? Is not the whole development of international agencies too embryonic still to make this procedure feasible?

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45.

4. Board of Directors - Term of Office

There is no great importance attaching to any specific term of office, say of five years as compared with seven. It is important, however, that a definite term be decided upon, that that term be so fixed as to guarantee rotation on the Board, and that the term of government members be longer in general than five years so that no single administration in either country will have an opportunity to influence unduly the composition of the Board. It is also important that the original members of the Board have long enough terms to insure an adequate initial job of organization.

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Suggestion

Let the term of office for government Board members be six years, each government making an appointment on alternate years, provided that in setting up the Authority, rotation of government members does not start until the fourth year. Let the term of office of members at large be three years, rotation not to start until three years after organization. Let vacancies due to resignation or death be filled on an interim basis by appointment in the same manner as the original appointment. At organization, Great Britain and the United States would establish by lot the country whose appointee would be first subject to rotation. Under this plan, rotation of term would follow the pattern set forth in the following table. The shorter term for members at large is possibly justified by the fact that personnel is more fluid in this field. The reason for a three year term is (1) that it is divisible into six; and (2) that members at large would be appointed alternatively, first coincidentally with a British member and next with an American member. The following table assumes that the draw established the United States as the country to rotate its appointees first, and also, that the program was inaugurated in 1942.

| <u>Years of New Appointments</u> | <u>British Member</u> | <u>American Member</u> | <u>Members at Large</u> | <u>Total Appointees in Year</u> |
|----------------------------------|------------------------------------------------------|-------------------------------------------------------|------------------------------------------------------|---------------------------------|
| 1942 | (1 for 5 yrs.) 3 (1 for 7 yrs.) (1 for 9 yrs.) | (1 for 11 yrs.) 3 (1 for 6 yrs.) (1 for 8 yrs.) | (1 for 3 yrs.) 2 (1 for 5 yrs.) (1 for 7 yrs.) | 9 |
| 1943 | none | none | none | none |
| 1944 | none | none | none | none |
| 1945 | none | none | 1 for 3 yrs. | 1 |
| 1946 | none | 1 for 6 yrs. | none | 1 |
| 1947 | 1 for 6 yrs. | none | 1 for 3 yrs. | 2 |
| 1948 | none | 1 for 6 yrs. | none | 1 |
| 1949 | 1 for 6 yrs. | none | 1 for 3 yrs. | 2 |
| 1950 | none | 1 for 6 yrs. | none | 1 |
| 1951 | 1 for 6 yrs. | none | 1 for 3 yrs. | 2 |
| 1952 | none | 1 for 6 yrs. | none | 1 |
| 1953 | 1 for 6 yrs. | none | 1 for 3 yrs. | 2 |

etc.

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47.

Query

(a) Is six years satisfactory for government members?

(b) Is three years justified for members at large?

(c) Is it intelligent to defer the beginning of rotation until the third year in order to insure a stable Board to organize the Authority?

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48.

5. Board of Directors - Personnel Requirements

Responsibility for the development of broad policies of the International Development Authority will rest in the Board of Directors. Responsibility for the execution of these policies will rest in the executive organization which the Board of Directors sets up. Clearly, the Board should be given wide freedom with respect to the personnel and to the methods of organization of the executive agency which it creates. The variety of problems that may be faced are too numerous to permit specification in advance with respect to these matters. But what of the Board of Directors itself? What kind of individuals should it have? How detailed should their functions be? Should they be full-time or part-time?

In general full-time Boards of Directors become involved in the minutiae of operations and tend to interfere with good administrative management. This should certainly be avoided in the International Development Authority. At the same time, the work of the Board itself, merely from the point of view of policy determination, will make fairly heavy drafts on the time of its members. It will probably be necessary to establish two main centers of operation for the Board, one in Washington and one in London. It would be well if the Board met alternately in each place. With the development of aviation, this procedure would not be as time consuming as it would have been hitherto, but it will nevertheless still require a considerable amount of time. The Board members, in addition, should be in fairly close contact with industrial sentiments in the two countries, and, also, with conditions in various parts of the world where investment undertakings are in operation.

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Suggestion

Let the legal documents establishing the Authority be silent on the question of full-time membership. This will give the authorities responsible for appointing members maximum freedom in locating individuals with the requisite background, experience and current contacts needed. This will make it possible in certain instances to secure Board members of high calibre who otherwise would not be available. At the same time, there must be assurance that Board members will devote the time necessary to the job and there must be compensation adequate to meet the conditions imposed by this situation.

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Query

(a) Should the enabling legislation be silent on the question of full-time service for the Board members, but specific on the requirement of ample time to perform the functions imposed?

(b) Should compensation be specified, and if so, how?

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6. Legal Framework

The legal framework required to establish the contemplated program raises questions which only the specialist can answer. They are listed below.

Query

(a) How can an international agency such as the International Development Authority be created. Could it be established by Treaty between the United States and Great Britain?

(b) How would the necessary funds be turned over to the Authority? Would this require a full appropriation bill in the United States?

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- (c) How would other countries benefitting from the program arrange their formal participation and express their adherence to the responsibilities imposed?
- (d) What legal steps are necessary to secure to the World Court jurisdiction over disputes arising in the course of operation of the Program?
- (e) How could the program be amended as time passes and poses new problems?

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F. Problems of Operation**1. Establishment of the Administrative Organization**

The kind of administrative organization needed to effectuate the policies of the Authority will necessarily be governed by the tasks it will be called upon to perform. It is assumed in this discussion that the Authority is established jointly by Great Britain and the United States while the war is still in progress. Under these conditions, the economic resources available for current investment in undeveloped regions will be distinctly limited. So long as the war continues, the organization would be chiefly concerned with making adequate preparation for active operation on the termination of hostilities. It would have to arrange (a) for the appointment of executive officers, (b) for the establishment of executive headquarters, (c) for the formal participation in the program of states desiring to participate in its benefits, and (d) for the granting of certificates of international incorporation to as many worthwhile projects as possible with the object of setting the stage for a large outflow of developmental capital immediately on the cessation of hostilities. It should be noted that this activity would provide valuable estimates of the volume of such investment that might be expected. Such estimates would be highly useful in the general formulation of post-war reconstruction plans.

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Suggestion

It has already been suggested that the International Development Authority have two headquarters, one in Washington and one in London. This suggestion is directly contrary to the general rule of sound organization. It seems to be imperative in this case, however, since the Authority will need to operate in close contact with both American and British investors, if it is to be in a position to stimulate a maximum flow of investment, and also, if it is to be able to act quickly and intelligently on plans submitted to it for approval. Experience has shown that it would not be wise to have a single headquarters equally removed from both important centers of operation. Something similar to this was done in the case of the Bank of International Settlements which located its headquarters at Basle in order to escape the possibility of over-dominance by reason of too great proximity to London, Paris, or Berlin. The result was that the Bank was isolated at the start from the organizations with which it was supposed to work. In the case of the Authority, it is essential that it should not be isolated from the centers of investment activity.

This being the case, it would be preferable to face the problems of organization imposed by the creation of two headquarters.

The problem of securing formal adherence to the program on the part of countries desiring to participate in its benefits would probably fall on the Directors as well as the Administrative Staff. Extensive travel on the part of both might be necessary to arrange the details of the program with countries planning to participate.

Once the organization was selected, headquarters established, and the formal adherence of participating countries arranged, the Authority would concentrate on the problem of passing on applications for incorporation. This would involve a considerable amount of staff work, including field surveys to establish the conformity of applications with the requirements of the program. It would be necessary, for example, to establish criteria for economic soundness, social standards, etc. The problems involved in establishing such criteria have already been considered in other sections of this memorandum.

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Query

Should definite provision be made, as suggested, for two headquarters -- one in Washington and one in London?

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2. Going-Concern Functions

After cessation of hostilities, the Authority would face new problems as a going concern. In addition to organizing itself effectively to stimulate applications for international incorporation and to pass on such applications when received, it would have to establish an accounting section to receive reports from corporations to which it had granted charters, to scrutinize these accounts in order to determine net income subject to profit-sharing under the program, and to establish the amount of the commitment outstanding under the guarantees which the Authority had issued.

These commitments would probably not come into action for some years. When they did come, the Authority might find that it was the dominant holder of the equity in the case of some of the less successful of the enterprises incorporated under it. In this event, the Authority would have to staff itself to deal directly with problems of management.

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3. Powers of the International Development Authority

This outline of problems involved in organization and operation suggests some of the powers that the Authority must have in order to function effectively. A tentative list, to be amplified as a result of discussion of the program, is presented below.

- (1) To organize, establish headquarters, engage personnel;
- (2) To grant charters of international incorporation;
- (3) To issue commitments to exchange debentures for the stock of internationally incorporated enterprises;
- (4) To sue and be sued;
- (5) To receive and hold funds (in cash or prime obligations), to issue debentures, and to hold, manage or sell properties received as a result of guaranty commitments;
- (6) To allocate reserves against guaranty commitments;
- (7) To make investigations -- economic, social, engineering, etc. -- in connection with the granting of certificates of incorporation;
- (8) To deal directly with governments with respect to the responsibilities delegated to the Authority;
- (9) To receive reports from internationally chartered corporations;
- (10) To have access to the accounts of internationally chartered corporations for the purpose of determining amounts due under guaranty commitments, net income subject to profit-sharing, etc.

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Query

(a) What should be the exact power with respect to the accounts of internationally incorporated enterprises?

(b) What other powers should be added to the above?

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Background and Conclusions

This program has been designed specifically to stimulate international investment in new ventures to develop the underdeveloped regions of the world. Because of the high risks inevitably associated with new ventures, investment of this character preferably takes the form of equities. In the century that preceded the first World War, such investment spread the benefits of the Industrial Revolution far beyond the boundaries of Europe and succeeded in knitting the economic activities of a large part of the globe into a single fabric.

Also, during that century, there appeared a reaction against international equity investment, known popularly as the "reaction against imperialism." This was due basically to a variety of frictions and abuses rather than to any one cause. There was sharp criticism, for example, of the practice of powerful creditor countries of seeking special privileges abroad for the trade and capital of their nationals. Such practices constituted specific examples, in the pre-1914 period, of tendencies toward economic nationalism that have become increasingly dominant during the last decade. In recent years such tendencies have been particularly conspicuous in the international economic policies pursued by the Axis powers. Criticism also developed when the governments of creditor countries intervened in smaller countries to enforce recognition of contractual rights held by their nationals against such contingencies as default or confiscation. Finally, the resistance of certain large internationally financed corporations

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to regulation of their activities by local governments, and especially their active participation in local politics to prevent the passage of social legislation, aroused widespread resentment within the creditor democracies as well as in the countries directly affected.

Partly as a result of this reaction and partly in consequence of the unstable character of the whole Versailles settlement, genuine equity investment, specifically investment in underdeveloped areas, diminished in importance during the reconstruction that followed the First World War. Other types of international capital flows, however, increased. There were, for example, huge flows of investment funds across national boundaries that came to be known as "hot money." These flows were not directed toward new areas or new resources in need of development. They came generally to countries already highly developed in search of speculative gain or in flight from confiscation. There was also, for a time in the twenties, a large countervailing flow of capital funds out of creditor countries, in the form of bond debt contracted by governments or by institutions guaranteed by governments. The economic effectiveness of many of these loans was limited, especially so in the case of loans that were floated, directly or indirectly, to provide service for war debts and reparations. There were also, of course, many loans not connected with the reparation and war debt situation, particularly loans in Latin America. Even in these cases, however, international capital investment tended to take the form of publicly guaranteed bonds because of a preference on the part of investors for this type of security.

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The small volume of international equity investment that did occur in the interval between the wars was confined largely to the development of very low-cost mineral resources and to the establishment of branch plants within tariff-protected areas. Altogether, there was little investment devoted to the general development of underdeveloped regions. Opportunities for such enterprises had been sharply diminished by the growth of economic nationalism, with its disruption of the channels of trade, and such opportunities as remained tended to be left untouched, unless the potentialities were especially impressive. With declining confidence that their governments would intervene in their behalf, investors have hesitated to assume the hazard of direct operations in these areas. By 1939, the general imposition of exchange controls, the prevalence of defaults, certain outstanding cases of confiscation, together with the general insecurity engendered by the encroachments of the Axis powers, had produced a situation of almost complete stagnation in the international capital markets. Such movements of capital as still took place consisted either of "hot money" coming to the United States where it was not needed, or of political loans, extended by governments, to secure friends or to buttress allies in the impending conflict. The desirability of directing an adequate flow of equity capital to the underdeveloped regions of the world was freely admitted within the democracies, but the outlook appeared hopeless.

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The Current Problem

Developments since 1939 have emphasized the need for a complete re-appraisal of this problem, particularly as it affects the international exchange position of both Great Britain and the United States. It is now apparent that capital funds in some form or other must be made widely available at the close of hostilities. Economic developments during the war, including the pressing needs of the imperilled democracies for supplies and munitions of war, have brought about a universal shortage in dollar exchange and in assets convertible into dollar exchange. The pressure of this situation is being eased currently through the operations of the Lend-Lease program, but the fundamental lack of balance in the international exchange position remains, and must be faced in any program that is directed toward the formulation of post-war reconstruction policies.

Should the United States fail to take measures adequate to induce an outflow of capital funds at the close of hostilities, the councils of post-war reconstruction will be haunted by a persistent shortage of dollar exchange. The structure of the American economy is still one in which the value of its export commodities normally exceeds in the aggregate the value of imports accepted in exchange. At the cessation of hostilities, the present abnormal export demand for American munitions (financed now through Lend-Lease) will cease, but the American economy will still need its export outlets and Europe will still need American supplies in large volume, particularly feedstuffs, raw materials, and productive equipment required to

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reconstruct industry to a peace-time basis. The outside world, however, will not have sufficient means to pay for these exports. The imports of the United States alone will not supply a sufficient volume of dollar exchange. Foreign holdings of liquid cash assets and capital assets convertible into dollar exchange by sale in the United States have already been drastically drawn down and will no longer be available in sufficient quantities to meet the situation. This position does not need extensive amplification. It is amply illustrated by the present concentration of the World's gold.

A gradual reduction of American tariff barriers under a revival of the Trade Agreements Program will constitute an essential element in developing a more balanced trading position between the United States and the outside world, but it will not be sufficient in the immediate post-war period when industry abroad will be still disorganized. It is in awareness of this impending situation that many observers throughout the world are forecasting as inevitable a continuation of exchange controls in the period immediately following the war, together with a further development of commercial policies along bilateral lines, despite the fact that such developments would run directly contrary to the fundamental commercial policies of the government of the United States.

Alternative Approaches to the Problem of Capital Outlays

Broadly speaking, a supply of dollar exchange sufficient to avert a crisis in the immediate post-war period can be provided through operations in the capital markets by any one of three methods of approach. First, the United States government can continue to raise funds in the American market on its

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own credit and can then advance these funds directly or indirectly to foreign governments. This is the method that gave rise to the inter-allied debts in the last war. It is also the method that is being used at the present time, in the form of advances to governments in South America and elsewhere through the Reconstruction Finance Corporation. Second, foreign governments or foreign industries can obtain dollar resources by floating loans in the American market. This is the procedure that was followed in the 1920's. It is generally agreed that a resumption of lending of this type would not take place in the absence of powerful public guaranties. Finally, the supply of dollar exchange can be augmented as a result of direct equity investment operations of the type discussed in this program. To be effective, these operations, also, would require public guaranties.

Any one of these three methods of providing capital will meet the short-run requirements of the situation, that is, it will avert an acute shortage of dollar exchange and the unfavorable repercussions that may be expected to ensue from that shortage. Any one of these methods, in fact, will produce a favorable environment for a time, no matter how ill-considered it may be from a longer point of view. This was demonstrated specifically during the 1920's. Between 1924, when the Dawes Plan was inaugurated, and 1930, when the Bank for International Settlements was established, the second of these three methods was adopted. Intensive efforts were devoted to the creation of conditions favorable to a resumption of international

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movements of investment funds, but this movement consisted of loans, particularly loans to governments. In terms of the volume of funds involved, these efforts were highly successful -- probably too successful -- since there is grave doubt whether the receiving countries really needed or had productive use for the large bodies of funds which were made available to them in the capital markets of the United States and Great Britain during those years. In terms of their purely short-run economic and political effect, these movements of funds were also highly successful. They allayed political unrest; they served temporarily to balance the international accounts of creditor as well as debtor countries; they permitted the stabilization of currencies; and they were accompanied by a rise to new high levels in the standard of living for the common people of many countries. On the other hand, they were equally destabilizing in their longer-term political and economic effects. Some of the reasons for this ultimate failure grew out of the precarious nature of the peace that was established at the close of the last war and such reasons may not present themselves again. Others, as will be indicated in the subsequent discussion, are always likely to recur when international government debt is incurred in too large volume.

Although, as the broad program of post-war reconstruction develops, there will be need for a continuation of direct inter-governmental loans, every effort should be made to avoid too great reliance on this form of international capital outlay. The feeding of the people of Great Britain, for example, is becoming increasingly dependent on American supplies received through the operations of Lend-Lease. Such supplies will probably have to be

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continued for a time after the cessation of hostilities. Loans from the Reconstruction Finance Corporation to Latin America and other foreign governments will also probably continue in some volume. In fact, plans for the construction of international public works to aid in providing employment during the period of post-war readjustment will inevitably involve a continuation of inter-governmental loans in some magnitude.

Strenuous efforts should be made, however, to keep the total volume of such loans at a minimum. Inter-governmental debts, by their nature, are apt to become sources of friction. They make the economic prosperity and the welfare of presumably independent states increasingly dependent upon the good will and benevolence of the governments of the lending states. Should anything happen to change that good will, or should internal political developments in the lending countries be reflected in a change of attitude toward inter-governmental loans, the governments of debtor countries will be forced into drastic economic readjustments for which they may be ill-prepared. Should such readjustments take the form of economic and political nationalism, or of general defaults, as they did in the 1930's, the whole fabric of international security may be strained.

Most inter-governmental loans, and all international long-term loans, suffer also from the basic defect that they are extremely vulnerable to default during period of depression. This is particularly true of loans contracted by countries or nationals of countries dependent largely for their existence on the export of raw materials. When the volume of international long-term debt is large, consequently, there is introduced a basic

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element of instability into the economic framework that makes that framework susceptible to collapse under even moderately adverse circumstances. This vulnerability arises, first, from the fact that the service on loans is determined according to a contractual rate of interest. This service is payable in the same sum in periods of depression as in prosperity, despite the fact that the exchange available to the borrowing country out of which to pay the service may vary widely as between these periods. In fact, borrowing countries dependent on raw material exports may have very little exchange out of which to maintain debt service in periods of depression. Under these circumstances, such countries usually attempt at first to maintain their national credit by various measures calculated to diminish their demands for foreign exchange. They raise tariffs, impose rigid tariff quotas, institute exchange controls, or undertake a broad program incorporating all of these devices and many more. These are the devices of economic nationalism. Even when they succeed in averting debt default, they accomplish their end by a diminution in the aggregate volume of international trade. In their short-run effects, therefore, the use of these devices is destabilizing in that they tend to accentuate the depth of depressions. In the longer run, it is often found that the imposition of controls of this type develops a heritage of vested interests which require the retention of controls long after the occasion for their use has passed.

Default is

Default is always a serious matter and involves at best a loss of credit standing on the part of the party in default. When foreign investment obligations consist of public bonds rather than private obligations, default involves the whole credit of the government concerned. It is for this reason that

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governments frequently adopt such rigorous measures to avert default. When, in spite of these measures, default takes place, the credit of the whole country is ruined. Under these circumstances the administration of the country in question, or, as frequently happens, a new administration may undertake to rationalise the default by suggesting that the obligations were not morally binding. Anti-foreign agitation sometimes develops. Foreign property may be confiscated. This sometimes proceeds to the point where the resumption of debt service is politically difficult or even impossible, even when exchange has again become available for debt service as a result of industrial revival.

International movements of capital funds in the form of equity investment are free from these particular defects. The problem with respect to equity funds, as has already been noted, is found in the fears that may be engendered -- fear on the part of weaker states that the economic power of large and dominant countries will be used, not for their development, but for their exploitation and domination, and fear on the part of investors that the success of enterprises on which they risk their funds will be frustrated by administrative discrimination, or that the enterprises will be confiscated if they are successful.

It has been the primary purpose of this program, by removing these two fears, to provide once more for a large-scale development of equity investment. With these grounds for apprehension eliminated, the transfer of funds arising

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out of genuine equity investment can do much more than provide merely for greater exchange flexibility in the current balance of international accounts. It can constitute a dynamic force that spreads the initiative, enterprise, industrial techniques, and management skills of the more highly developed countries throughout the world. Because they consist of equities, the service on international capital obligations incurred through operations of this character can be deferred in depression. In fact they are more than likely to be deferred because profits are usually low at such times. These obligations, therefore, do not augment the cyclical vulnerability of smaller countries dependent for exchange largely on the export of one or two commodities. Again, because they are equities, these obligations do not endanger the national credit. If an enterprise is a failure, it is a private failure in which a specific group of investors have ventured and lost. Provided there was no administrative discrimination to cause the failure, no occasion for international recrimination is provided. Finally, because they are equities, they normally lead to more intimate understanding of international economic problems. The position of an investor venturing his funds in operations far from home is essentially different from that of a foreign bond holder. The former, if he follows his investment at all, must, as a matter of necessity, be brought into continuous contact with the currents and cross currents of world affairs in their political as well as in their economic aspects. He cannot remain as completely ignorant of impending strains as a

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bond holder who is suddenly awakened by a default to the fact that his coupons need no longer be clipped.

Conclusion

Should the program here described be adopted now while hostilities are still in progress, it will demonstrate concretely the determination of Great Britain and the United States to reverse the separatist trends of the past two decades; and their will to promote definite leadership in the construction of a new world order in which the economic advantages of the industrially more advanced states are made broadly available to the people of less advanced areas. It will constitute an example of what is meant by Point IV of the Churchill-Roosevelt Declaration that Great Britain and the United States

" . . . will endeavor, with due respect for their existing obligations, to further the enjoyment by all States, great or small, victor or vanquished, of access, on equal terms, to the trade and to the raw materials of the world which are needed for their economic prosperity;"

As a concrete example, it will bring to the minds of all men everywhere faith in the validity of that declaration.

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December 1, 1941

The Honorable Henry A. Wallace
The Vice President
Washington, D. C.

Dear Mr. Vice President:

I am ashamed to find that I failed to write you earlier about Stephen Raushenbush.

I have known Mr. Raushenbush intimately for years. We were boys in grammar school together and were close friends through high school, college and enlisted together in 1917. Since then our contacts have naturally been less numerous, but they have nevertheless been fairly continuous. I can vouch absolutely for his integrity. His judgment may have been wrong or open to dispute at times, but there is no question whatever of his sincerity, honesty and patriotism.

Very sincerely yours,

Winfield W. Riefler

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February 9, 1942

Honorable Henry A. Wallace
The Vice President
Washington, D. C.

Dear Mr. Vice President:

Thank you very much for your letter of February 6th. It encourages me greatly. You may rely upon it that I will be available to make any contribution I can to carrying out these plans.

I agree with you that the International Surplus Commodity Corporation would provide in effect a commodity dollar. In fact, it is the only type of commodity dollar that appears practical or realistic to me. From my conversations with Keynes, I think that he has the same general feeling.

Very sincerely yours,

Winfield W. Riefler

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**OFFICE OF THE VICE PRESIDENT
WASHINGTON**

February 6, 1942

Mr. Winfield W. Riefler
The Institute for Advanced Study
School of Economics and Politics
Princeton, New Jersey

Dear Mr. Riefler:

I agree wholeheartedly with you as to the great importance both of an International Surplus Commodity Corporation and an International Development Corporation. After reading the memorandum which grew out of the conference between you and Alvin Hansen, I asked Mr. Perkins to take up this problem with the various affected agencies so that I might talk the matter over with the President with some degree of assurance. I am glad you have been taking such a deep interest in this matter.

Sincerely yours,

H A Wallace

H. A. Wallace

P. S. It appears that Winston Churchill, when he was here, didn't indicate any particular interest in post-war economic planning. There was one exception, however: he did manifest interest in an International Commodity Dollar. An International Commodity Dollar would, of course, have a very real relationship to an International Commodity Corporation.