Juridical constraints on monetary sovereignty: implications for international economic law

by

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DECLARATION

Student number: **3314-839-2**

I declare that **"Juridical constraints on monetary sovereignty: implications for international economic law"** is my own work and that all the sources that I have used or quoted have been indicated and acknowledged by means of complete references.

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09 April 2015

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DEDICATION

To my father Siphiwo Ndlovu and my mother Sibonile Khabo-Ndlovu, my wife Basikana Debra and children Mbongeleni and Phumlo Crystal Ndlovu.

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ABBREVIATIONS

ASCM	Agreement of Subsidies and Countervailing Measures
BIT	Bilateral Investment Treaty
EMU	European Monetary Union
ESCB	European System of Central Banks
FTA	Free Trade Agreement
FET	Fair and Equitable Treatment
ICSID	International Centre for the Settlement of Investments Disputes
IIA	International Investment Agreement
IMF	International Monetary Fund
GATT	General Agreement on Tariffs and Trade
GATS	General Agreement on Trade in Services
MCP	Multiple Currency Practice
SADC	Southern African Development Community
MST	Minimum Standard of Treatment
TFEU	Treaty for the Functioning of the European Union
TNCs	Transnational Corporations
UN	United Nations
UNICITRAL	United Nations Commission on International Trade Law

ABSTRACT

Money is a public good. The regulation of its creation, supply and distribution is of national and international interest. Monetary stability is an important regulatory goal conducted through an interaction of economic, political, religious factors as well as legislative action. The state plays an intermediary role, bridging domestic interests and international interests. Increasing interdependence between national economic systems and international obligations sometimes leads to the manipulation of systems as well as currency wars. Regulation is done through co-operative international action since domestic regulators are no longer sufficiently equipped to do so. Resultantly, there is an emergence of new structural paradigms to deal with it. Meanwhile, states still enjoy certain residual competences of sovereignty. Numerous legal factors act as constraints on sovereignty with far reaching implications on states' regulatory space. In light of the divergence of regulatory objectives, there is an apparent need to balance municipal with international interests on the regulation of the monetary system.

KEY TERMS

Monetary sovereignty, international economic law, juridical constraints, regulation, trade liberalisation, capital flows, controls, restrictions, currency, manipulation, monetary power.

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CHAPTER 1

1. MONETARY SOVEREIGNTY AS AN ESTABLISHED RIGHT OF A STATE

1.1. INTRODUCTION

The role of the state in the minting and coinage of currency is an age old tradition among states. National legislation defines legal tender, determines what chattels constitute money and also determines the monetary standard upon which that money is to be based. This power of the state to define money is the basis for the dominance of the state theory of money. Other theories such as social and institutional origions of money also seem to have gained popularity in recent times.[1] As monetary systems have evolved from commodity based standards such as precious metals to fiat standards, the monetary power of the state has become even more apparent.

Monetary sovereignty[2] still remains an important attribute of statehood as the state occupies a relatively unlimited position regarding the formulation of monetary law and policies. It is noteworthy, however, that this type of sovereignty stems from the general sovereignty of the state, an attribute which assigns exclusive control to a particular state to determine matters within a particular territory.[3] Mutual respect of each other's sovereignty is the basis of international co-operation between states. Although international co-operation is based on a number of principles, that of "sovereign equality" of nations[4] plays a highly important function. It is the first to be stated in Article 2 of the United Nations Charter, an indication that its significance is highly regarded in international law.

The application of the principle of 'sovereign equality" of nations creates a complex scenario, particularly with regards to questions on how national interests are to be balanced with the demands steming from a state's international legal obligations. There is no other area in

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[1] Proctor C *Mann on the Legal Aspect of Money* 7th Edition 2012 at 40 notes that a strict adherence to the state theory of money is no longer tenable as there now exist institutional and other forms of money.

[2] Treves T "Monetary Sovereignty Today" in Giovanoli M (ed) *International Monetary Law: Issues for the New Millenium* 2000 at 111-118. Treves perceives monetary sovereignty as inclusive of the power to define a monetary unit, to define notes and coins in multiples of that unit and to require that payments in such notes and coins be accepted as legal tender at nominal value.

[3] Jackson JH "Sovereignty:Outdated Concept or New Approaches" in Shan W, Simmons P and Singh D (eds) *Redefining Sovereignty in International Economic Law* 2008 at 10 says that in light of the recent developments in international relations, the state no longer wields exclusive power which traditionally would include the power to chop off heads or to even violate virgins.

[4] See Article 2(1) of UN charter and Article 4 of the SADC Charter which deal with principles. The latter reads; SADC and its Members shall act in accordance with the following princples: a) sovereign equlaity of all Members States.

which upholding national sovereign prerogatives openly clashes with the principle of free trade than in the area of monetary law. States do sometimes enact legislation which is adverse to the interests of foreign individuals.

By virtue of the above stated facts, the powers and responsibilities of the state entity are of great interest to one attempting to obtain an indepth understanding of public international law of money. As the bearer of sovereign power regarding money, the state enjoys a priviledged international law position which makes the regulation of its conduct somehow problematic. Understanding the functional role of national sovereignty within the legal order is a necessary requirement for the proper appreciation of the legal matters pertinent to cross border trade, investment and other economic activities. While a state's exercise of political sovereignty rarely raises problematic questions except in cases of excessive abuse of such power, the exercise of sovereignty with regards to monetary power does from time to time give rise to critical questions that tend to have far reaching implications on international economic relations.

As monetary sovereignty is a public international law principle which basically means that every state has the right to determine its own monetary matters within its territory[5], disputes surrounding the implications of its application have been brought for adjudication before both domestic[6] and international courts[7] and tribunals. The reasoning of the courts in these cases seems to indicate that monetary sovereignty is an established right in international law.[8] Be that as it may, a unilateral exercise of such state power still gives rise to conditions that make the pursuit of international economic activities difficult.

1.2. CURRENT CONCERNS REGARDING MONETARY SOVEREIGNTY

One of the areas of great importance in international economic law is the interconnection between the monetary systems and other economic activities of states. While monetary sovereignty is an important attribute of statehood, it currently stands in jeopardy in light of the increasing inclination towards globalisation. To uphold and defend it is to overthrow the pillars of modern economic relations. Payment for goods purchased would become impossible if states were to unilaterally impose and adhere to rigid exchange controls and

[5] Mann FA *The Legal Aspect of Money* 5th Edition 1992 at 461.
[6] *Norman v Baltimore & 0hio Railroad.,* 294 US 240 (1935).
[7] *France v Kingdom of the Serbs, Croats, and Slovenes* Judgment, (1929) PCIJ Series A no 20, ICGJ 260 (PCIJ 1929), 12th July 1929, Permanent Court of International Justice and *France v Brazil* Judgment, (1929) PCIJ Series A no 21, ICGJ 261 (PCIJ 1929), 12th July 1929, Permanent Court of International Justice (PCIJ).
[8] *Ibid*.

restriction policies as they please. No wonder, in an effort to prevent states from arbitrarily imposing restrictions on certain monetary transactions, Article VII (3)b of the IMF is designed to limit the member states' powers to impose any controls unless the adoption of such controls is done in pursuance of formal declarations (made after a properly conducted investigation) of the scarcity of the currency of the state concerned.[9]

For the sake of promoting free international enterprise, municipal monetary laws must of necessity be bought into conformity with the demands of international economic interaction so as to inspire the development of complimentary relationships among states. Unilateral state action is often characterised by protectionist measures which create numerous problems for cross-border economic interaction. Adoption of the "race to the bottom"[10] strategies, competitive depreciation as well as exchange rate manipulation often lead to friction among states as is apparent in the case of the US-Sino relations. It is alleged that the People's Republic of China engages in deliberate currency manipulations through maintaining an undervalued Renminbi (RMB), the official currency of China, whose unit is the Yuan, against the US Dollar. This has led to a "currency war"[11] and a diplomatic tension between the USA and China in recent years. The latter has been accused of adopting monetary policies that allegedly exert undue pressure on the US economy.[12] In light of the emergent "competitive regulation"[13] whereby states attempt to exploit loopholes in other states' regulatory systems for their own advantage, it turns out that co-operation remains the best option in order for international economic interaction to be mutually enriching.

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[9] See IMF Article VII:3(b) which deals with the issue of exchange controls.

[10] See Jackson JH "Global Economics and International Economic Law" (1998) 1 *Journal of International Economic Law* 1-23 at 22 who notes that governments do sometimes set lower standards of regulation so as to attract economic activity in their own societies. For example, a lower tax rate for businesses makes it more attractive to invest in that country than investing in states where taxes are high.

[11] Copelovitch MS & Pevehouse JC "Currency Wars by other Means: Exchange Rates and GATT/WTO Dispute Initiation" (2011) *University of of Wisconsin, Department of Political Science, Working Paper (Unpublished).* Available at https://ncgg.princeton.edu/IPES/2010/papers/F220_paper3.pdf . Last accessed on 14 January 2015. See also Cline WR and Williamson J (2010) "Currency Wars?" *Peterson Institute for International Economics Policy Brief Number PB 10 - 26* at 5 who acknowledge the existence of the war and explain why "… many countries, especially those not fully developed, desire to protect their export sector …" Some states, including Brazil, China, India, Indonesia, Israel, Japan, Korea, Malaysia, the Philippines, Singapore, South Africa, Switzerland, Taiwan, and Thailand seem to participate in some kind of exchange market interventions.

[12] Jung H "Tackling Currency Manipulation with International Law: Why and How Currency Manipulation should be Adjudicated?" (2012) 9 (2) *Manchester Journal of International Economic Law* 184-200.

[13] Jackson J H "Global Economics and International Economic Law" (1998) 1 *Journal of International Economic Law* at 14. Also Trachtman JP "Regulatory Competition and Regulatory Jurisdiction" (2000) *Journal of International Economic Law* 331-348 at 339.

One other subject that has generated great attention concerns the liberalisation of capital movements.[14] While states have the competence to determine the external value of their currencies through the development of exchange rate policies, the power of a state to regulate money outside its borders remains a tricky matter. The growth of global financial markets and the emergence of offshore markets have made the task even more cumbersome. In the words of Cohen,

> "The functional domain of each money no longer corresponds precisely to the formal jurisdiction of its issuing authority. Currencies have become increasingly deterritorialized, their circulation determined not by law or politics but by the preferences of market agents.[15]

In light of the above, Jackson is not far from the truth when he notes that "the actual circumstances of the "globalized market" impose realistic constraints on the unilateral exercise of "sovereignty."[16] The Brettonwoods monetary system operated with the effect of stabilising the global monetary system. Its collapse on 15 August 1971[17] resulted in the adoption of floating exchange arrangements thereby compromising the desired stability. As manipulative state conduct became the order of the day, some states began to maintain artficially undervalued currencies with the attendant effect of distorted trade balances.

The problem is further compounded by the fact that sovereign decisions in one state usually have adverse consequences outside its own boundaries. An unfettered right of monetary sovereignty is no longer justifiable in an open globalised market but rather runs contrary to the objectives of free trade and capital liberalisation.[18] In light of the crystalisation of trends towards globalisation and mounting tension between national sovereignty on one hand and

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[14] Pasini FL "Movement of Capital and Trade in Services and Trade: Distinguishing Myth from Reality Regarding the GATS and the Liberalization of the Capital Account" (2012) 15 (2) *Journal of International Economic Law* 581-619. Viterbo A "Iceland's capital controls and the constraints imposed by the EEA agreement" (2011) *Capital Markets Law Journal,* 214-237 at 216. In 2008, Iceland introduced exchange restrictions in order to curb the flight of capital which was caused by the stress suffered by the Icelandic economy.

[15] Cohen BJ "The international Monetary System: Diffusion and Ambiguity" (2008) 84 (3) *International Affairs* at 455–470 at 463.

[16] Jackson JH "International Economic Law: Reflections on the Boileroom of International Relations" (1995) 10 (2) *American University International Law Review* 595-606 at 604.

[17] Lowenfield A F "The International Monetary System" (2010) 13 (3) *Journal of International Economic Law* 575-595 at 581.

[18] Article VI of the IMF which deals with purposes and aims of the organisation. Article XV of the GATT regulates exchange and trade measures by which states may frustrate GATT and IMF objectives respectively.

international trade objectives on the other,[19] the imposition of constraints on monetary sovereignty almost becomes compulsory.

Articles IV and VIII of the IMF, Article XV of the General Agreement on Tariffs and Trade (GATT) and Article XII of the General Agreement on Trade in Services (GATS) are very significant in regulating international economic activities. The extent to which these provisions constrain abitrariness in the formulation of sovereign decisions is, however, far from clear. There are other numerous instruments that are relevant in this regard. These include those from regional systems such as the European Monetary Union (EMU). The treaty establishing the European Communities as amended by the Maastricht Treaty[20] is an important regulatory regime from which guidance may be obtained as the need arises[21] in the regulation of monetary matters.

Since money is so central to trade between states[22], a legal framework that protects the monetary rights of participants in international commerce is imperative. The three dimensions to the economic relations between states namely trade, money and investment play a pivotal role in shaping interstate relations.[23] However, money plays the key role of a facilitator of trade in goods, trade in services, and foreign direct investments. Its central function in international commerce has been recognised by Booysen who refers to it as "one of the cornerstones of International trade law."[24]

The following statement echoes the importance of a harmonised monetary system.

> "Because a country cannot alter its international payments position without automatically causing an opposite change of equal magnitude in the payment positions of the rest of the world, one country's pursuit of its macro-economic goals inevitably influences how well other countries attain their goals."[25]

States therefore need to co-operate in the formulation of monetary law so as to stabilise the international monetary system.

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[19] Bagwell K and Staiger RW "National Sovereignty in an Interdependent World." (2004) *National Bureau of Economic Research Paper Series 10249* at 1.

[20] The treaty regulates the restrictions on capital movements between EMU members and third states. Article 73(b) deals with the prohibition of capital movements between states. It is a tenable submission that a prohibition on the restrictions of capital movements is in itself a constraint on the sovereignty of the state to deal with capital movements into and out of its territory.

[21] Booysen H "The Monetary Constitution of the Future Euro and its International Effect" (1996) 29 (2) *The Comparative and International Law Journal of Southern Africa* 112-129 at 118.

[22] Antonio Sáinz de Vicuña "Legal consequences of a single currency" in Giovanoli M (ed) *International* law: *Issues for the New Millenium* 2000 at 161.

[23] Lastra RM *Legal foundations of International Monetary Stability* 2006 at 346.

[24] Booysen H *Principles of International Trade Law as a Monistic System* 2003 at 318.

[25] Krugman PR and Obstfeld M. *International Economics; Theory and Policy* 2006 at 487.

1.3. INTERNATIONAL MONETARY CO-OPERATION

Due to the apparent importance of economic interaction, states have drifted closer towards monetary co-operation in recent decades.[26] As already mentioned above, the IMF has been functional in this arena since the ratification of its charter in 1945. Other initiatives have also been adopted, leading to the emergence of monetary unions, amid calls for the creation of a more harmonised international monetary and financial architecture.[27] All these efforts are designed to usher in a measure of certainty in international monetary law for the sake of the protection of trade and other public goods.[28] The EMU has also integrated national currencies in a manner that has had a dramatic impact on global monetary relations while the Southern African Development Community (SADC) has launched a regional integration strategy and the agenda for the formation of a monetary union.[29] It can be argued that these initiatives stem from a realisation that exclusive municipal control of monetary law is no longer compatible with the current developments in international commerce. Inevitably, the sovereign monetary powers of states have undergone curtailment. States have surrendered some of the attributes of their power through participation in treaty regimes such as the IMF,[30] the EMU, and other monetary unions.

1.4. THE IMPORTANCE OF CONSTRAINTS ON MONETARY SOVEREIGNTY

States sometimes undertake certain acts in violation of international law. Examples of such acts are the manipulation of exchange rates and the imposition of exchange restrictions contrary to IMF Articles. They do this in order "to gain unfair competitive advantage over other states"[31] and such action is an affront to international law particularly if undertaken in violation of treaty obligations. Market intervention strategies that violate international obligations cause a serious disruption of cross border economic activities.

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[26] The EMU has emerged as a leading example of regional monetary co-operation creating a single currency since 1999. Its performance has seen mixed outcomes. Lauded as an intelligent innovation at its birth, the first one and a half decades of its existence have raised more questions than answers with regards the feasibility of a universal currency.

[27] Giovanoli M (ed) "A New Architecture for the Global Financial Market: Legal Aspects of International Financial Standard Setting" in Giovanoli M *International Monetary Law: Issues for the New Millenium* 2000 3-59 at 4.

[28] Viterbo A *International Economic Law and Monetary Measures: Limitations to State Sovereignty and Dispute Settlement* 2012 at 10.

[29] SADC Regional Indicative Strategic Development Plan Desk Assessment 2005 – 2010 Report November 2011 at 29 refers to plans for a regional Monetary Union by 2016 and an Economic Union, with a single currency by 2018.

[30] IMF Article VIII (2) deals with "Avoidance of restrictions on current payments." It further reads; (a) Subject to the provisions of Article VII:3(b) and Article XIV:2, no member shall, without the approval of the Fund, impose restrictions on the making of payments and transfers for current international transactions."

[31] Gold J *Legal Effects of Fluctuating Exchange Rates* 1990 at 10.

Constraints on sovereignty assume factual as well as legal dimensions[32]. Factual constraints occur mostly due to concessions and co-operation based on political considerations, market changes as well as trade usages. Legal constraints, on the other hand, are different from factual ones. Unlike the constraints which emanate from political factors, economic developments and market forces in operation,[33] legal or juridical constraints occur in terms of state law, international law obligations that come about in terms of multilateral or bilateral agreements or in terms of customary public international law norms. The sovereign state has legally ceded some of its traditional elements of control to other role players such as the international organisations.[34]

The rate of the *de jure* shift of monetary power from the state to international organisations has however been slower than that of the *de facto* shift of power due to political and economic factors. Factually, the state is no longer able to keep pace with all activities connected with its currency[35] and yet the law does not fully address the mismatch.

Juridical constraints are important in that they force each state to operate in terms of international expectations instead of pursuing selfish and protectionist policies. They constrain the power of the state and ensure legal protection for the benefit of other parties.

1.5. CHAPTER BREAKDOWN

This work is broken down into six chapters as outlined below.

Now that the introductory work has been covered in this chapter, chapter 2 considers the conduct of the state in the exercise of its monetary sovereignty including how state power is occasionally wielded in a manner that is adverse to the interests of other states and private parties.

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[32] Lastra RM *Legal Foundations of International Monetary Stability* 2006 at 26. Also Jackson JH "Sovereignty:Outdated concept or New Approaches" in Shan W, Simmons P and Singh D (eds) *Redefining Sovereignty in International Economic Law* 2008 at 10. Jackson writes that the sovereignty debate refers to the allocation of power, particularly government legal decision-making power.

[33] Zimmermann CD "The Concept of Monetary Sovereignty Revisited" (2013) 24 *Journal of International Economic Law* 797–818 at 800 suggests that there are "factual constraints brought about by economic globalization and the increasing integration of financial markets…"

[34] Multilateral legal regimes such as the IMFsystem, have usurped some of the powers traditionally reserved for the state. In terms of Article IV:2 (a) of the IMF a member state must notify the organisation of its intention to adjust its exchange arrangements. Bilateral Investment Treaties also do sometimes contain clauses that limit the powers of the state as far as monetary sovereignty is concerned.

[35] Cohen BJ "The international monetary system: Diffusion and Ambiguity" (2008) 84 (3) *International Affairs.* at 455–470 at 463.

In chapter 3, an appraisal of the theoretical matters regarding monetary sovereignty is given elaboration. Its contours and scope are discussed in the section of the work which also unveils the effects of these incidences on international law. An exploration is made of the law regarding exchange rate determination, exchange controls and capital controls and how they are being employed in the contemporary monetary system. It also discusses the complimentary relationship between national and international legal instruments.

In chapter 4, the reasons and methods of constraining state power are given attention and the chapter also examines the effects of the IMF, the World Trade Organization (WTO), Bilateral Investment Treaties (BITs) and regional agreement provisions on the monetary power of the state. The application of legal provisions that constrain monetary sovereignty is also discussed.

In chapter 5, the study focuses on the implications that the constraints on monetary sovereignty have on the broader body of international law. It also explores the effects of the constraints on the application of international economic law. It explores concrete examples of factual situations in which monetary sovereignty has openly clashed with other legally protectable interests as well as some tentative solutions to these clashes.

Chapter 6 deals with the concluding remarks, assesses the extent of the legal constraints that are applicable to monetary sovereignty, and also makes relevant recommendations.

CHAPTER 2

2. THE CONDUCT OF STATE IN MONETARY MATTERS

2.1. INTRODUCTION

There have been some changes in state's role of regulating monetary law in recent decades. This chapter explores those changes and the responses that have been adopted to address them. The position of the state as the centre for monetary regulation in international monetary law continues to be questioned. Yet in spite of the assaults on its dominance, the state's position still remains central and pivotal. An adaptation to the resultant changes has tended to tour various routes, none of which has brought about any fundamental changes to the monetary system.

This chapter begins by exploring the concept of global monetary stability in light of the theory of 'global public goods.' The theory originates from the economic sciences discipline but has in recent years found its way into the legal discipline. It has been useful in enhancing an understanding of the policy choices of states and also to bridge the conceptual gap between the disciplines of law and economics. Building upon the assumption that the law does not regulate in a vacuum, but rather enjoys a complimentary relationship with rules of economics, monetary law is placed in context as an interdependent public good the regulation of which imports the imperative of international co-operation. An enquiry is then made into the applicability of the classical Westphalian perceptions of international law under the present circumstances of globalisation. These perceptions refer to a prohibition[36] on the conduct of states that international law;

> "leaves them [states] in … a wide measure of discretion which is only limited in certain cases by prohibitive rules; as regards other cases, every state remains free to adopt the principles which it regards as best and most suitable."[37]

The public choices at the disposal of the international community receive attention and are evaluated in terms of how they can best be exercised in the design of the most effective system.

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[36] The Westphalian model of international law, as explained in the Case of the *SS 'Lotus'* (*France V Turkey)* Publications of the Permanent Court of International Justice Series A.-No. 70 September 7th, 1927 at 18 holds that the state "may not exercise its power in any form in the territory of another State. In this sense jurisdiction is certainly territorial; it cannot be exercised by a State outside its territory except by virtue of a permissive rule derived from international custom or from a convention."

[37] *Id.* at 20. See also Jackson J H "Sovereignty: Outdated Concept or New Approaches" Shan W, Simmons P and Singh D *Redefining Sovereignty in International Law* 2008 at 8-9.

The chapter also exposes the abuses of power that have come about as a result of the unqualified and slavish application of the Westphalian model of international law. The next step is a discussion of how Westphalian regulatory models are out of step with the current maze of interstate relations and patterns of international economic interaction. An exploration of some emergent *'structural paradigms'* of international economic law also comes in tandem as do the evaluations of the foundational principles upon which a legitimate international monetary system may be built. These various paradigms are examined for their merits together with the prevailing criticisms against each one of them. In conclusion, the chapter cites the apparent strengths and weaknesses of the paradigms explored.

2.2. MONETARY STABILITY AS A 'GLOBAL PUBLIC GOOD'

A stable monetary system is an essential ingredient for any economic system. It has been argued that "… a stable currency is one of our most valuable public goods, comparable to well-functioning systems of law, public order or public finance and taxation."[38] Currency is an intergral part of the monetary system and it plays a very important function of facilitating economic activities. The stability of the global monetary system translates to international economic stability, a condition that has been elusive in recent years.[39] The central function that money plays in economic activities makes the regulation of its supply and provision very important. Monetary stabillity is a global monetary good the supply of which is beneficial to all those involved in the global economic system. Questions therefore arise regarding who should regulate the supply of this all important public good. Should regulation take place at the level of the state or at international law level? The public choices that have to be made in respect of this question must take into account numerous considerations some of which are discussed below.

[38] Baltensperger E & Cottier T "The Role of the International Law in Monetary Affairs" (2010) 13 (3) *Journal of International Economic Law* 911–937 at 911.

[39] As recently as 2007, a gobal financial crisis with far reaching effects affected financial systems of almost all the states. It began in the last quarter of 2007. What may have begun as the burst of the housing mortgage bubble in the USA soon spread into other financial centres and led to a solvency / capital crisis and a subsequent run by financial institutions on other financial institutions. The effect was felt right across the global economic spectrum, affecting the economic activities of many nations. States adopted various responses to the crisis some of which generated more problems. The bail out strategies on the Too Big To Fail (TBTF) institutions were adopted and this method exacebated the problem in that it resulted in a snowballing sovereign debt. By the year 2014, some European nations such as Greece and Italy were still sitting with huge and menacing sovereign debts. Rickards J *Currency Wars: The Making of the Next Global Crisis* 2011 at 114. Stiglitz JE "Too Big to Fail Banks" *Carnegie Council for Ethics in International Affairs.* Available at https://www.youtube.com/watch?v=EV2Pn6gMhVQ (Accessed on 15 February 2015). See also Petersmann EU "JIEL Debate: Methodological Pluralism and its Criticism in International Economic Law Research" (2012) 15 (4) *Journal of International Economic Law* 921-970 at 951. Lastra RM & Wood G "The Crisis of 2007–09: Nature, Causes, and Reactions" (2010 13(3) *Journal of International Economic Law* 531–550.

In order to fully appreciate the importance of global monetary stability, it is very important to place it within the framework of 'global public goods' and then to define what 'global public goods' are. One definition states that "Transnational public goods are those with benefits and costs that reach beyond one country and in some cases beyond one generation."[40] Trachtman indicates that they are goods that are "non-excludable and non-rival."[41] Goods are said to be 'non-rival' when their consumption by one person does not diminish the ability of others to also enjoy the same benefit. The term 'non-excludable' means that those paying for the supply of the good "cannot keep a non-payer from consuming the good's benefits."[42] The systemic importance of monetary stability as well as the risk of contagion import upon its regulation an imperative of international co-operation.

Given that there are different types of global public goods, the methods used to supply each type have to accord with the nature of each good in question. The *'single effort global public goods'* such as scientific inventions do not require the co-operation of all the nations but only the effort of those directly involved, while the 'weakest link goods' such as prevention of the spread of diseases require the collective action of all states so as to effectively control epidemics. There are also what are called 'interdependent aggregate global public goods' whose supply requires collective action to effectively and efficiently supply them. Such goods are 'interdependent' in nature in that what happens in one state has an effect on other states. The goods have an 'aggregate' nature in that their supply requires the collective participation of all the states.[43]

Global monetary stability is one of the "interdependent aggregate public goods"[44] the supply of which invites 'collective action' of all states and Petersmann states that these goods are best supplied by a 'summation process'[45] of numerous institutions and levels. The globalisation of markets accounts for the transformation of what used to be national goods into global public goods.[46] This observation casts a dark shadow over the validity of the obiter

[40] Sandler T "Assessing the Optimal Provision of Public Goods: In Search of the Holy Grail" in Kaul I & Conceição P *Providing Global Public Goods: Managing Globalization* 2006 at 131. Sandler goes on to add concerning this type of goods that "If this reach is worldwide, the goods are global public goods."
[41] Trachtman JP "The International Law of Financial Crisis: Spillovers, Subsidiarity, Fragmentation and Cooperation" (2010) 13 (3) *Journal of International Economic Law*) 719–742 at 721.
[42] Sandler T "Assessing the Optimal Provision of Public Goods: In Search of the Holy Grail" in Kaul I & Conceição P *Providing Global Public Goods: Managing Globalization* 2006 at 132.
[43] Petersmann EU "JIEL Debate: Methodological Pluralism and its Critics in International Law Research" (2012) 15 (4) *Journal of International Economic Law* 921-970 at 930. The author gives an enlightened exposition of the various types of 'global public goods' as well as the mode of supply of the goods in a discourse that lays a solid foundation for the 'Multi-level governance' of 'interdependent aggregate global goods.' The elegant discourse shows how what he terms the summation process is the most appropriate method of governing the global monetary system.
[44] Petersmann EU *supra* at 932.
[45] Petersmann EU *supra* at 950.
[46] Petersmann EU *supra* at 947.

made by the Court of International Justice on the Serbian loans case in 1929[47] to the effect that monetary sovereignty is an unchalleged given. A lot has changed since the court ruling. Closer market intergration means that national economies no longer operate with the same degree of autonomy which they had in 1929. How then can the contours of monetary sovereignty as they stood in 1929 remain the same after eight decades? The law certainly needs to adapt to the developments that occur across the various sectors of society. The 'horizontal and vertical dependencies' of nations and institutions make it "highly impossible for one state to effectively regulate the supply of such goods.[48] The 'jurisdictional exclusivity'[49] of yesteryears certainly needs to give way to 'inclusivity'.

The co-operation of all states, particularly those with vastly sized economies of systemically significant stature, is an imperative of the modern international monetary legal system. This is the most effective way to temper the adverse effects of the negative externalities[50] of national economic policies. The negative spillovers, that have potential to cause global instability can best be avoided through co-operation in monetary regulation. In light of this, the state law must no longer be isolated but rather must be woven into the fabric of the international legal system in such a way as to facilitate co-operative action in the search for solutions to cross-border problems. Co-operation and removal of information assymetries are the prerequisites for proactive action.

2.3. REGULATORY BURDENS UPON THE STATE

The state has numerous responsibilities towards its citizens as well as other states. One of its paramount responsibilities is to govern the territory as effectively as it possibly can. It has to ensure the welfare of its constituents who otherwise have the corresponding right to demand political, social and economic stability, as well as peace and security.

The decisions of the state are informed by a combination of economic, political, ideological and religious considerations. The forces from these spheres of a nation's life determine the policy choices of the state as well as how these factors are employed to achieve the desired

[47] *France v Kingdom of the Serbs, Croats, and Slovenes* Judgment, (1929) PCIJ Series A no 20, ICGJ 260 (PCIJ 1929), 12th July 1929, Permanent Court of International Justice and *France v Brazil* Judgment, (1929) PCIJ Series A no 21, ICGJ 261 (PCIJ 1929), 12th July 1929, Permanent Court of International Justice (PCIJ).
[48] Petersmann EU "JIEL Debate: Methodological Pluralism and its Critics in International Law Research" (2012) 15 (4) *Journal of International Economic Law* 921-970 at 947.
[49] Jurisdictional exclusivity refers to the jurisdiction priviledge of a state to regulate within its territory without interference from outside forces.
[50] Joel Trachtman "The International Law of Financial Crisis: Spillovers, Subsidiarity, Fragmentation and Cooperation" (2010) 13 (3) *Journal of International Economic Law* at 721-722.

objectives. Domestic political considerations[51] play a decisive function in shaping these choices as does "… a country's level of economic development ..[…]…capacity and desire to adopt and maintain particular monetary regimes."[52] States sometimes place a high premium on nationalism. Russel observes how nationalistic governments are less inclined to intergrate themselves into the international economic system[53] due to their inclination towards protection of patriotic agendas.

Considering that the state formulates monetary law, its role in defining money remains a matter of great significance. Since the collapse of the Bretton Woods system and the disppearance of commodity standards, almost all national currencies are of a non-convertible nature based on 'fiat' rather than commodity standards. Until then, currencies were convertible in the sense that bank notes could be redeemed for *specie* or a commodity of appropriate value. Gold and silver were the popular monetary commodities but have since been demonetised. Nowadays each currency obtains its legal status from the authority of the one issuing the it. The word 'fiat'[54] means 'decree' or 'proclamation.' It is the power of proclamation by a state which gives monetary character to the paper. There is absolutely nothing of intrinsic value in the paper that could for instance give greater value to a Pound Sterling as compared to the US dollar. Neither, comparing the US$1 with a US$10, is there any unique and perculiar intrinsic quality in one paper granting it more value than the other. Instead, the quality and the size of the paper may be the same such that only the figure super-scribed on the face of each note serves as the distinguishing factor.

The state pursues the goal of sustaining the internal and the external value of the currency. A crucial factor regarding the value of the currency is the national economic policies of the issuing state. Sound economic policies have a tendency to secure stability whilst unsound policies lead to the opposite result. The value of money is at the heart of economic stability, which happens to be one of the basic requirements for the security of any state. When a country's economy fails to guarantee economic security for its citizens, this may result in widespread social unrest or even a political revolution.[55] The state pursues macro-economic

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[51] Russel J "Trading Sovereignty for Stability? The Political Economy of Monetary Intergration" (2011) 37 *Review of International Studies* 673-690 at 674.
[52] *Id* at 681.
[53] *Id* at 681.
[54] Knapp GF *The State Theory of Money* 1924 at 30. Validity is assigned to money by means of a 'proclamation' by the authorities of the state. Value is not intrinsic on the substance that makes the money but is derived from the proclamation or the decree made. See also Acocella N *Economic Policy in The Age of Globalisation* 2005 footnote 9 at 254.
[55] The Arab spring that swept across North Africa as from 2011 was triggered by economic hardships under a dictatorship. Mohammed Bouazizi, a street vendor in Tunisia doused himself with fuel and set himself on fire in front of a governement building. The incident sparked a series of revolts which subsequently led to the ousting of the head of state in Tunisia and inspired revolutions in Egypt,

stability with unremitting vehemence as a way of preserving its sovereign status. It meets these obligations through the maintainance of a balance of payment equilibrium, exchange rate stability as well as price stability. It employs many other monetary policy instruments in order to achieve its goals.

The goal of price stability has in recent years emerged as one of the priority monetary stability goals among many states[56] and this goal also finds expression both in national as well as international legal instruments. An example of a national legal instrument that cites price stability as a monetary policy goal is the Bank of England Act of 1998. It reads;

> "In relation to monetary policy, the objectives of the Bank of England shall be (a) to maintain price stability, and (b) … to support the economic policy of Her Majesty's Government, including its objectives for growth and employment.[57]

The Treaty on the Functioning of the European Union (TFEU) is a highly significant international legal instrument espousing the goal of price stability. Article 127 of TFEU stipulates that 'The primary objective of the European System of Central Banks … (ESCB) shall be to maintain price stability" and to "… support the general economic policies in the Union with a view to contributing to the achievement of the objectives of the Union …"[58]

The South African Reserve Bank[59] also strongly pursues the goal of monetary stability. National legislation is invariably employed as a tool in the furtherance of the broader agenda of economic stability. It appears to have become a prevalent assumption that price stability is an important policy goal to be pursued by the members of the EMU. Monetary stability refers to "the absence of erratic or unanticipated movements in the level of prices through inflation or through deflation."[60]

States sometimes maintain monetary stability by controlling inflation. Care needs be exercised in the use of instruments designed to control inflation. A slavish pursuit of stability in the goods prices has in some instances resulted in a complete overshadowing of the

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Yemen and Libya. http://global.britannica.com/EBchecked/topic/1753077/Mohamed-Bouazizi Accessed on 09 November 2014.

[56] Lastra RM *Legal Foundations of International Monetary Stability* 2006 at 35.

[57] Section 11 of the Bank of England Act 1998.

[58] Article 127 of the Treaty on the Functioning of the European Union (TFEU).

[59] South African Reserve Bank website reads "The primary objective of monetary policy in South Africa is to achieve and maintain price stability in the interest of sustainable and balanced economic development and growth." Price stability reduces uncertainty in the economy and, therefore, provides a favourable environment for growth and employment creation. Available at http://www.resbank.co.za/MonetaryPolicy/Pages/MonetaryPolicy-Home.aspx (Accessed on 09 November 2014).

[60] Lastra RM *Legal Foundations of International Monetary Stability* 2006 at 36.

debilitating market behaviour regarding the financial asset markets.[61] The adoption of inflation targets becomes a potentially distabilising factor unless there is a rational harmonisation of inflation indeces between those that are based on price adjustments for consumer goods and those based on asset price adjustments.[62]

As is apparent from the discussion above, the goal of monetary stability is met through the employment of numerous economic instruments, principles and policies, an exercise which requires a high degree of skill. Monetary economics, a branch of economics dealing with matters such as the supply, quantity of money, the relationships between money and growth and between money and employment plays a highly influential function in influencing the choice and the deployment of these intruments. Law as a discipline is neither competent nor sufficiently equipped to prescribe the choice of these instruments. The ideas of economists do sometimes find their way into the law[63] though it remains clear that law-making is not simply an enactment of economic theory into law. This remains so in spite of the fact that law-making does substantially leans on assumptions and commonly held notions of economic theory.

The Keynesian theory[64] dominated economic thinking for many years such that even legislators were informed in their reasoning by the dominant thoughts of the day. The adoption of the gold standard by England in the 19th century and the demonetisation of silver were directly attributable to the ideas of the British economist Ricardo[65]. His arguments in the years preceding the adoption of the gold standard in 1821 clearly pointed towards the economic importance of gold. Because legislators are not necessarily economists, they may

[61] Stiglitz JE *The Stiglitz Report:Reforming The International Monetary and Financial Systems in the Wake of the Global Crisis* 2010 at 38. According to the report, the inflation indeces used were based on consumer goods and overlooked the price adjustments regarding other asssts.
[62] Lastra RM *supra* at 35-36.
[63] The Washington Consensus exercised a great deal of influence on monetary and financial law formulated after 1989. Begining with the paper by Williamson J who coined the phrase, the neo-liberal principles of market fundamentalism gained popularity. See Stiglitz JE *The Stiglitz Report:Reforming The International Monetary and Financial Systems in the Wake of the Global Crisis* 2010 at 21 and 59 who notes that these ideas were very influential in promoting non-regulation of the financial markets. Such non-regulation, based on the assumptions that markets have an innate ability to self-correct were responsible for the global crisis that began in 2007. See also Sornarajah M "The Neo-Liberal Agenda in Investment: Its Rise, Retreat and Impact on State Sovereignty" in Shan W, Simmons P and Singh D *Redefining Sovereignty in International Law* 2008 at 199.
[64] The Keynesian theory, an expression of the ideas of John M Keynes was based on the assumptions of the efficacy of closer and stronger state intervention in the economy through guidelines and financing of public projects. The 'General theory', as it was called, emphasised the role of the state in fixing macro-economic behaviour of the essential variables such as interest rates as well as supply and demand for money through systematic interventions. Monetary and fiscal policies were viewed as important factors in the overal performance of the economy. Refer to Cord R *Reintepreting the Keynesian Revolution* 2013 at 6. See also Blinder AS "Keynesian Economics" in *The Concise Encyclopedia of Economics* http://www.econlib.org/library/Enc/KeynesianEconomics.html Accessed on 17 July 2014.
[65] Friedman M *Money Mischief; Episodes in Monetary History* 1994 at 152-154.

be influenced by the dominant economic views. In the post-1960s period, the quantity theory of money became very influential following the writings of a prominent economist of the time, Friedman.[66]

The monetary economics discipline thus seems to occupy a very central function in prescribing the course for monetary legislation. Stiglitz and Greenwald opine that:

> "A central reason for interest in monetary theory is that monetary policy remains one of the most effective means by which the government can control the level of the economy's activity, at least at certain times."[67]

The state is more than willing in most cases, therefore, to resort to prevailing eceonomic principles and to enact laws that promote what is believed to be sound economic theory. It is economic theory that defines what stability is as well as the required circumstances in which growth and employment may best be achieved. The choice and the deployment of appropriate policy instruments therefore belongs in the province of economics rather than law.

The state also finds itself saddled with an unenviable duty to prevent systemic failure of the financial sector as a way to ensure stability of the macro-economic environment. By virture of the inter-connection among institutions, the soundness of each institution is a matter that the state pursues with uncompromised diligence. A state may employ austerity measures during episodes of economic hardships so as to mitigate the effects of instability. It is significant to note that the focus of the law differs greatly from the pre-occupations of economics and politics. The law deals with the regulation of human and economic relations. Its focus is on rights and obligations. Legal subjects incur rights and obligations by their conduct. Economic relations and processes may benefit from the observance of these rights and obligations. It is important at the same time to note that legal objectives go beyond the mere facilitation of economic efficacy. Economic theory on the other hand is concerned with the efficacy of economic activity, the efficiency of markets, factors influencing outputs as well as the employment of the factors of production.

The choices that the state makes regarding its monetary law are also influenced by the prevailing ideological considerations. When communism took a hold of Russia, the state adopted state-centred economic polices which did not give room to private enterprise. The

[66] Friedman M *A Program For MonetaryStability* 1959 at 89 states that "The stock of money therefore seems to me the relevant magnitude in terms of which to formulate monetary rules and behavior …" The quantity rules of money gained a great deal of influence in guiding monetary policy for several decades following Friedman's writings.

[67] Stiglitz JE &Greenwald B *Towards a New Paradigm in Monetary Economics* 2003 at 154.

accession of Fidel Castro in Cuba in the late 1950s saw a nationalisation of foreign owned monetary assets, a move that brought a serious diplomatic rift between Cuba and other states.[68] In terms of the law enacted at the time, refered to as Law 891,[69] national banks in Cuba were nationalised, thereby affecting countless foreign nationals in a case which amounted to property expropriation. A diplomatic fall-out occurred between the USA and Cuba. Under the guidance of Enersto Guevara, Cuba drifted away from the geo-political relations with the Americas and instead forged closer ties with the USSR and the rest of the Communist bloc. The USA retaliated by imposing a trade embargo[70] and promulgating laws which resulted in the freezing of Cuban assets falling within the jurisdictional control the USA at the time.[71] The developments cited above in relation to Cuba's decisions reveal the extent to which ideological and political factors can wield such a gross influence on a state and even determine the legislative course it takes.

Another determinant of a state's policy choice concerns theories of justice. As explained below, the "Washington Consensus" influenced thinking as from 1989 and caused some sweeping changes on the Latin American and African national economies. The IMF and the World Bank were able, through the principle of conditionality, to prescribe monetary and other various economic measures to the least developed countries (LDCs) in a typical bullying fashion. Principles such as privatisation, trade liberalisation and capital liberalisation, attributable to what Williamson proposed in his ground breaking paper that gave birth to what came to be known as the "Washington Consensus,"[72] became the guiding principles in policy formulation.

Much debate has taken place regarding the influence that the Washington Consensus had on the monetary policies of the LDCs. Whether or not it brought about any developments to those places is a question yet to be answered. Sornarajah opines that the 'Washington Consensus' was a neo-liberal initiative that was detrimental to the economic interests and the welfare of the less powerfull states.[73] Williamson[74] denies the imputation that it is an

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[68] *Nielson v Secretary of Treasury* 1970 54 *International Law Reports* 534.

[69] Travieso-Diaz MF "Alternative Recommendations for Dealing with Expropriated US Property in Post-Castro Cuba" (2002) *Association for the Study of the Cuban Economy* 101-115 at 104.

[70] *Id.* at 102.

[71] The Cuban asset control regulations adopted by the USA were a response to the nationalisation of US assets in Cuba. Such a move resulted in legal battles brought before the municipal courts in the USA as some private individuals who had claims against the frozen properties took action to recover the said properties. The *Nielsen v Secretary of the Treasury* 1970 54 *International Law Reports* 534 is an example of the case in which the freezing of Cuban properties through a retaliatory US legislation became subject of a major legal challenge.

[72] Williamson J "The Washington Consensus as Policy Prescription for Development" (2004) *Institute for International Economics* at 1-2.

[73] Sornarajah M "Mutations of Neo-Liberalism in International Investment Law" (2011) *Trade Law and Development* at 212. At footnote 22, Sornarajah talks of the "Washington Consensus" as an alleged conspiracy between the White House, the IMF and the World Bank and attributes its growth in

advancement of a neo-liberal agenda. Whatever the justification of the 'Consensus' is, the policies of numerous states were certainly shaped by its ideological foundations as they were exported to the LCDs through the application IMF conditionality principle. This refers to conditions which states have to meet in order to qualify for IMF financial assistance and their discussion is out side the scope of this study.

Even if they sometimes sound highly cogent, political ideologies do not always sustain a viable economic system whereas rational decision does. Even though monetary phenomena such as inflation, deflation, and depression are ideologically neutral, they may be manipulated by a state in such a way as to produce a certain policy outcome

Another factor that has a telling impact on global monetary relations is religion, an example of which is the Islamic religion giving birth to an Isamic monetary system. It is a unique model which draws its rationale from the deeply entrenched religious foundations of its proponents. To the extent that this system holds sway in so many countries which constitute a substantial portion of the global system, it can be conclusively stated that, as a result, the formation of a fully intergrated global monetary system shall for the forseeable future remain a pipe dream.

It is in light of states' regulatory burdens that the study turns to review the developments which have occurred in international monetary relations. The next section is devoted to the changes to regulatory approaches.

2.4. RE-THINKING THE STATE'S POSITION BEYOND WESTPHALIA

Until the outbreak of the First World War, monetary regulation was the preserve of the individual states. The whole international monetary system was anchored on national rules[75] rather than on any international treaty. The system lacked any centralised coordination. That was the era of the gold standard, a very stable system in which states adopted the gold standard in alignment to the hegemonic influence of the British monetary system. The system was spontaneous rather than coordinated. The outbreak of the First World War marked an end of the gold standard as states printed paper money to finance the budgetary deficits resulting from the increased demands of war. The end of the war in 1918 saw some

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popularity to the election of neo-liberals like Thatcher, Reagan and Kohl as leaders of the developed world.

[74] Williamson J "The Washington Consensus as Policy Prescription for Development" in a Lecture delivered at the World Bank as part of a series (2004) '"Practitioners of Development". Available at www.iie.com/publications/papers/williamson0204.pdf (Accessed 04 January 2015).

[75] Simmons BA "The Legalization of International Monetary Affairs" (2000) 54 (3) *International Organisation* 573-602 at 575.

attempts to return to the pre-war monetary system without success. The foundations of the pre-war gold anchor had already been grossly shaken.[76]

National economies were hit by hitherto unprecedented hyper-inflation. The level of inflation experienced by Germany revealed the weaknesses of the recently adopted fiat standards. The Genoa conference convened in 1922 was meant, among other things, to curb the challenges of the new system but it did not bear fruit. States continued to act unilaterally with regards to monetary issues. The inter-war years were characterised by highly volatile economic conditions. The Great depression of the 1920s to 1930s brought great pressure to bear upon national economies. The outbreak of the Second World War is to a great extent attributable to the economic challenges of the time. The Bretton Woods system emerged after World War II as the first attempt to build a truly international monetary system and marked the emergence of the "public international law of money."[77] The Bretton Woods system was based on a *par value* system whereby the US dollar was convertible to gold at a rate of $35/oz (thirty five dollars per ounce).

That system remained very stable until 1971 when the USA "declared the end of the convertibility."[78] Since then, floating exchange rates replaced the *par value* system. The IMF made ammendments to its Articles on the realisation of the need to adapt the law to the demands of the time. The adoption of flexible and floating exchange rate arrangements resulted in a potentially chaotic situation. As each state received the freedom to pick and choose its own policy from a catalogue of alternatives, an opportunity was created for currency manipulations leading to misalignments and distorted patterns.[79] States also carried out market intervention activities to either undervalue their own currencies or adopted measures to feign balance of payment equilibrium. The European monetary system developed in a way that brought harmonised exhange rate patterns among its member states in a typical 'snake in the channel'[80] fashion while laying the foundation for the EMU.

Even in the days following the collapse of the Bretton Woods system, states did not readily yield to the temptation to act in isolation. It was in those years immediately after the collapse

[76] Rickards J *Currency Wars: The Making of the Next Global Crisis* 2011 at 61.
[77] Simmons B A *supra* at 577.
[78] Thorstensen V, Ramos D and Muller C "The 'Missing link' Between the WTO and the IMF" (2013) 16 (2) *Journal of International Economic Law* 353–381 at 360.
[79] The currency war between the USA and China has been raging on for over a deacade. The allegation made by the USA is that the RMB, the Chinese currency is grossly undervalued to the extent that it allegedly causes serious distortions in the economic relations of the two nations. See Miranda J "Currency undervaluation as a violation of GATT Article XV(4)" in Evenett S J (ed) *The US-Sino Currency Dispute: New Insights from Economics, A VoxEU.org Report* 2010 at 125.
[80] Giavazzi F & Giovannini A "Can the European Monetary System be Copied Outside Europe? Lessons from Ten Years of Monetary Policy Coordination in Europe" (1990) *International Policy Coordination and Exchange Rate Fluctuations* at 247.

of the Bretton Woods system that Britain, in 1979,[81] repealed the law on exchange controls, signifying a significant opening up of the markets to foreign participants. Since then, national economies have continued to drift closer towards one another in a manner that has brought greater levels of intergration.

The prevalence of national monetary policies that produce adverse externalities on other economies has necessitated concerted action among states.[82] The state is no longer an isolated and ultimate authority whose decisions are beyond scrutiny. Current international architecture positions most states such that they have to give account both within and without their borders.[83] In the post-westphalian global order, "… the state will have an intermediary role between international and domestic concerns …"[84] Apparently the emerging architecture is is a fundmanental shift from the erstwhile configurations of the international legal framework. The intermediary function is exercised between the state's citizenship on the one hand and other functionaries in the international community on the other.[85] As Viterbo notes[86], the intermediary state will operate with a double-pronged focus. Its conduct in the formulation of internationally negotiated policies while pushing for the incorporation of domestic preferences within the international legal framework forms one of the two legs. The other is that the state also bears the responsibility to implement the internationally negotiated policies in the domestic legal order thereby making it imperative to view the conduct of the state as that of a bridge over various interest formations.[87]

However, even after the obvious shift from the formations based on 'jurisdictional exclusivity', the distinction between domestic and international affairs still remains relevant.[88] The question whether the state will cease to have relevance in the new configurations of power is answered in the negative. The states will remain key players in the multi-level structure. Concurring with Marks, Hooghe and Blank, Aalberts uses the following words to explain how the multi-level approach reconciles the demands of the state with those of the international community:

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[81] Mann FA *The Legal Aspect of Money* 1992 5th Edition at 361.
[82] Trachtman J "The International Law of Financial Crisis: Spillovers, Subsidiarity, Fragmentation and Cooperation" (2010) 13 (3) *Journal of International Economic Law* 719–742 at 728.
[83] Pasini FL ""Movement of Capital and Trade in Services: Distinguishing Myth from Reality Regarding the GATS and the Liberation of the Capital Account" (2012) 15 (2) *Journal of International Economic Law* 581-619 at 598. Pasini states how a state limits its policy space and becomes subject to GATS discipline when it liberalises its capital account.
[84] Viterbo A *International Economic Law And Monetary Measures: Limitations to States' Sovereignty and Dispute Settlement* 2012 at 18.
[85] Kaul I "The Rise of the Intermediary State" in Kaul I and Conceição P *"The New Public Finance: Responding to Global Challenges"* 2006 at 73.
[86] Viterbo A *supra* at 19.
[87] Viterbo A *supra* at 19.
[88] Aalberts TE "The Future of Sovereignty in Multilevel Governance Europe – A Constructivist Reading" (2004) 42 (1) *Journal of Common Market Studies* at 24.

> "As such multilevel governance seems to challenge both the external anarchy and the internal hierarchy element of the Westphalian principle. At the same time multilevel governance theorists in fact do not dispose of states – quite the opposite, as they argue that states will not only remain players, but even key actors in European politics."[89]

The 'jurisdictional exclusivity' of the state as regards internal domestic matters has fallen into the abyss of the yesteryears. The state's "exclusive political authority within its geographic boundaries based on territorial and policymaking sovereignty,"[90] has been greatly eroded. Kaul plausibly develops the concept of the intermediary state in the context of public finance in such an enlightening manner that the application of the same model to the state conduct in monetary affairs should not seem like a far-fetched adventure. The current state cannot ignore the "ever denser network of external expectations,"[91] but has to blend those policy choices that have origins in the domestic arena with those of international origin so as to bring about mutual and aggregate benefits.

Yet, in spite of all these seeming encroachments, the state's regulatory machinery still remains the mainstay of monetary law. Jackson approporiately advances the view that it is not time to "dismiss the nation-state yet" adding that it "can be an important check on the misuse of power at an international or muliti-lateral level."[92] The only important point to watch is how state and international institutions interact to bring about the desired outcomes. The notion of 'shared sovereignty' has taken centre stage. From an analytical perspective therefore, it appears that the multi-level governance can help to mitigate the adverse effects of restrictive exchange controls, exchange rate misalignments, restrictions of inflows and outflows of capital between states. This would be achieved by placing great emphasis on collective engagement and maximising synergies between state actors.

As the interdependence between national economies has become comprehensive, it is apparent that the unilateral regulation of the monetary system is no longer feasible. Connally's comment regarding the global importance of the US dollar in 1971 when he said, "It may be our currency, but it's your problem…,"[93] shows how the mutual dependence of

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[89] *Id*. at 25.
[90] Kaul I *supra* at 73.
[91] Kaul I *supra* at 73.
[92] Jackson JH "An Interview with John H Jackson: Shaping International Economic Law" (1997) 5 (1) *The Journal of the International Institute* http://quod.lib.umich.edu/j/jii/4750978.0005.102/--interview-with-john-h-jackson-shaping-international-economic?rgn=main;view=fulltext (Accessed on 18 January 2015.)
[93] This remark was made by John B Connally who was US Secretary of treasury at the time that President Nixon announced the end of the convertibility of the US dollar to gold in 1971, thereby marking an end of the post war monetary stability. He made the remark to his European counterparts.

monetary systems had already become a living reality then. More than ever before, this interdependence has become a deeply ingrained phenomenon. The Sino-US "currency debate"[94] is a sign that Chinese policy will no longer be the exclusive concern of Beijing. Instead, a change of policy in that country is likely to trigger some corresponding action in Washington or elsewhere in the world. The occassional reversion, by states, to national regulatory machinery in times of crisis, in a typical protectionist style threatens co-operation and subsequently brings the whole monetary system into jeorpady. Currency manipulations, exchange rate misalignments, and restrictions on capital inflows and outfows require collective action at all times. Developing a bridge between international and domestic spheres will go a long way in establishing the necessary conditions for stability.

2.5. CHOICES AND PERSPECTIVES IN SEARCH OF AN EFFECTIVE REGULATORY SYSTEM

The current global monetary system is characterised by disjointed regulatory regimes, ranging from state regulators to regional as well as global multilateral institutions. This raises problems of norm conflict. The methods by which states integrate themselves into the international monetary system are numerous and therefore carrying out the task may be problematic. One choice is for the state to align itself with a hegemonic currency such as the British Pound Sterling, the Euro or the US dollar which would serve as a reserve currency for the state concerned. Another choice is "dollarisation," whereby a state adopts the currency of another and uses it as its own. There is also the option of a "multilateral intergration" arrangement such as membership to a monetary union as well as a "go it alone approach." [95] The adoption of each choice tends to be a function of both domestic and international considerations.

In the case of 'dollarisation', the state forfeits its monetary power and subordinates its monetary policy to that of the state whose currency it adopts. Examples of dollarisation include Zimbabwe[96] and El Savador. A monetary union, an example of which is the EMU, is

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A quote given in Zimmermann CD "Exchange Rate Misalignment and International Law" (2012) *Graduate Institute Centre for Trade and Economic Integration* at 2.

[94] Jung H "Tackling Currency Manipulation with International Law: Why and How Currency Manipulation should be Adjudicated?" (2012) 9 (2) *Manchester Journal of International Economic Law* 184-200.

[95] Russel J "Trading Sovereignty fo Stability? The Political Economy of Monetary Intergration" (2011) 37 *Review of International Studies* 673-690 at 675.

[96] Zimbabwe adopted foreign currencies as legal tender after a protracted economic downturn and an inflation rate of an unprecedented proportion. Domestic economic problems which saw the collapse of the industrial and the agricultural sectors of the national economy resulted in massive human suffering and the people stopped using the Zimbabwe dollar as a store of value long before the official announcement by the Minister of Finance in March 2009. By January 2014, the multiple currency

an institution in terms of which several states integrate their monetary systems into one system. Monetary sovereignty is pulled together and the monetary union exercises it on behalf of member states. There is yet another possible arrangement called a currency board in terms of which the state anchores its currency to a relatively more stable currency. The challenge for the subordinate currency is that it becomes susceptible to the macro-economic pressures experienced by the major currency.

From 1989 to 2002, Argentina operated a currency board in terms of which the Peso was anchored on fixed parity to the US Dollar. When the Argentine national economy got severely strained at the beginning of the current millenium, the state abondoned the anchor and undertook a 'pesification' of all monetary obligations. The state's unfavourable balance of payment position was responsible for the abondonment of the currency board arrangement by 2002.[97]

Given the states' freedom to design their monetary systems, the global system evidently operates without uniformity. Arguably there are some "long-standing structural weaknesses of our international monetary arrangements"[98] that need to be addressed to bring stability to the system. Some of the most difficult choices concern the question of how to allocate authority between national and global functionaries. Largely, states adopt choices that are aimed at bringing about maximum benefits for their constituencies while international law institutions pursue interests that seek to benefit the larger global community.

Faced with such difficult challenges in balancing divergent policy preferences, international co-operation presents itself as the most reasonable choice. The Rapport Camdesus succintly captures the pursuits of the international monetary law in saying:

> "The international monetary system to which we aspire is one that … maintains freedom of trade and current payments and that allows sharing more widely the benefits of financial globalization, appropriately regulated. It is a system where all countries recognize their stake in global stability and accept that near-term national objectives may, if needed, be constrained by the global interest."[99]

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regime included the Botswana Pula, British Sterling Pound, Euro, South African rand, US dollar, Australian dollar, Chinese Yuan, Indian Rupee and Japanese Yen. (Source Monetary Policy Statement issued in terms of the Reserve Bank of Zimbabwe Act Chapter 22:15, Section 46 (January 2014) by CL Dhliwayo, acting governor at 55).

[97] Lowenfield AF "The International Monetary System: A look over Seven Decades" (2010) 13 (3) *Journal of International Economic Law* 575–595 at 593.

[98] Camdessus M *et al* "Reform of the International Monetary System: A Cooperative Approach for the Twenty First Century" *A Royal Palaise Initiative* 2011 at 2. Available at http://global-currencies.org/smi/gb/telechar/news/Rapport_Camdessus.pdf (Accessed on 05 January 2015).

[99] *Id* at 17.

The choice, therefore, is between assigning decision-making functions to national institutions and assigning the competences to the international level to be carried out by international institutions. It is a difficult one to make because of political and other interests that states must compromise in the process. It juxtaposes centripetal and centrifugal forces in a heavily contested tug of war.[100] The centripetal or 'centralisation' theories are based on the belief that the state needs to sacrifice its own policy preferences in favour of the international preferences. This view erronoeusly assumes that there are some 'neutral international preferences' out there which exist independently of any national influences. Such a view disregards the fact that all choices carry some subjective tastes and self-interests of their proponents.

Theories regarding the relationship between municipal and international law determine how the municipal and the international legal regimes interact to regulate the legal relationships. They determine how international legal norms are assimilated into municipal law. The dominant theories are monism and dualism. Monism means that municipal and international law belong to the same legal system and "... municipal courts are obliged to apply rules without any need for an act of adoption by the courts or transformation by the legislature"[101] Their sources are the same. Once a norm attains the status of law in terms of international law, it becomes unnecessary to take any other municipal steps to give the norm the status of law in the municipal legal system. The doctrine of dualism on the other hand holds that "… international law and domestic law are two legal systems independent of each other."[102] This therefore necessitates a procedure by the state to assimilate international treaties into the domestic system. Without such processes, the treaty cannot enjoy the force of law in the domestic sphere.[103] This artificial divide between 'municipal' and the 'international' law poses serious challenges on the implementation of international law in the municipal legal landscape. It also justifies a denial of rights and legal standing to private indivduals and non-state actors. Cottier argues that, "while international law affects people, they often cannot

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[100] Franck TM "The Centripede and the Centrifuge: Principles for the Centralisation and Decentralisation of Governance" in Broude T and Shany Y *The Shifting Allocation of Authority in International Law* 2008 at 19-20.
[101] Dugard J *International Law: A South African Persepctive* 4th Edition 2012 at 42.
[102] Wallace R M M and Holliday A *Nutshells International Law* 2006 at 32. See also Dugard J *supra* at 42. See also Starke J G "Monism and Dualism in the Theory of International Law" in *Year Book of International Law* 66 1936 at 73.
[103] The Republic of South Africa is an example of a state which applies a dualist approach. In terms of Section 231 (2)-(4) of the Constitution of the Republic of South Africa of 1996, the approval of parliament is required before the treaty can have a binding effect upon the state. It must be tabled before parliament and its provisions must be consistent with the constitution. This last requirement which puts the treaty in subjection to the constitution renders international law subordinate to municipal law.

invoke it or rely upon it."[104] This is a strange scenario and it is out of step with the pervasive discourse of human rights.

Due to the perception of municipal and international law as different legal systems, a risk of improperly regulated commons becomes a menacing reality. The argument that national and international law are founded on completely different principles is often employed to bolster the notion that 'internationalisation' of decision-making is not consistent with international legality. It is viewed with disdain, much as it is argued that there are countless and 'deep-rooted' cultural, religious, linguistic and other differences between the peoples.[105] It is ironic, however, that diversity is not a feature that is is exclusive to international communities but it is also a feature of domestic communities. As regards this 'diversity' argument, Cottier's well considered observation is that, "disagreement is not unique to international relations and law…"[106]

As already stated, the view regarding the internationalisation of decision making holds that the state must take a back seat while an international institution such as the IMF or another with overall and sweeping jurisdiction must exercise law making functions. These laws would then bind all the states the way municipal law binds all citizens. In the absence of an international legislature endowed with compulsory law making functions, it is hard to imagine how the 'centralisation' would operate. Whether decision-making would take place at the level of an institution that has a universal outreach such as the UN, the IMF or at regional level such as the EU, the North American Free Trade Agreement (NAFTA) or the SADC, there stands a very crippling criticism against this proposition. International institutions suffer from a 'congenital defect' of a 'democratic deficit' because their decisions emanate from state representatives who are not elected representatives of the people.[107] The legitimacy of their decisions is questionable in the absence of a people-driven mandate. This amounts to a drifting away from democracry to 'technocracy' whereby the technically minded elite become the decision makers. It sounds like a lousy suggestion that unelected elites such as economists, lawyers, banking specialists and scholars, among others, should usurp the priviledges of the people.

[104] Cottier T "Multilayered Governance, Pluralism and Moral Conflict" (2008) *Swiss National Centre of Competence in Research Working Paper No 2008/*23 at 3.
[105] *Id* at 5.
[106] *Id* at 10.
[107] Paulus AL "Subsidiarity, Fragmentation and Democracy: Towards the Demise of General International Law?" in Broude T & Shay Y *The Shifting Allocation of Authority in International Law* 2008 at 193.

Making choices in this area is a formidable task and Russel captures the complexity so accurately in saying, "But to understand the international side of monetary relations, one must look to domestic political structures, histories and politics."[108]

2.6. PRINCIPLES AND PROCESSES IN DECISION MAKING

Sound principles such as democracy and subsidiarity are the cornerstones of reasonable decision-making. With regards to the subsidiarity principle, it has been said, "The principle of subsidiarity stands out for the proposition that normative, political and legal decisions should be taken by the competent authority that is closest to where the impact of the decision will be felt."[109] When one considers that decisions touching on monetary regulation are in their nature technical, it is however debatable that the popular views of common masses who lack technical understanding of monetary dynamics should at all be esteemed when it comes to taking decisions on these matters. Without seeking to disregard and undermine the democratic rights of the citizens of nations, it is important to be mindful of the fact that the foundational principles relevant to the regulation of one branch of law differ in a fundmamental way from those applicable in another. Democratic representation, equality and justice are certainly the most applicable principles as regards the protection of human rights and access to clean water. In cases where monetary regulation is the subject of consideration, the principles of stability and peaceful relations between the concerned parties tend to be foundational.[110] Considerations of alternative principles other than democracy seem logical.

As a way of limiting the areas of contention in decision-making, an emphasis on processes rather than outcomes seems to be the sensible option. Among those legal scholars who uphold the importance of structures and procedures is Cottier who argues in favour of 'shared processes and structures of decision-making'.[111] This creates an even-handed ground for consensus building among the numerous interest groups. These shared values, principles, structures and procedures in decision-making help to moderate some of the contestations that arise in relation to content based decision-making approaches which

[108] Russel J "Trading Sovereignty fo Stability? The Political Economy of Monetary Intergration" (2011) (37) *Review of International Studies* 673-690 at 689.
[109] Broude T & Shay Y *The Shifting Allocation of Authority in International Law* 2008 at 6. The principle has application in the TFEU as ammended by the Treaty of Lisbon (Preamble Articles 5, 9 and 12).
[110] Baltensperger E & Cottier T "The Role of International Law in Monetary Affairs" (2010) 13 (3) *Journal of International Economic Law* 911–937 at 929.
[111] Cottier T "Multilayered Governance, Pluralism and Moral Conflict" (2008) *Swiss National Centre of Competence in Research* at 49.

emphasise the contestable theoretical issues.[112] Another proponent of 'process based' rather than 'outcome based' decision-making governance is Franck who proposes the adoption of neutral principles to serve as the guide posts to the processes adopted.[113] The application of these principles is meant to serve as the starting point for any assessment of the legitimacy of the decision taken.

In reconciling the clash between domestic and international law,[114] appropriate choices must show regard to these principles and processes. Issues regarding how international objectives get to be incorporated into national law should consider the nature of the issue at hand, the persons who will be affected by the decisions, as well as the legitimacy of the decision in light of the competence of the concerned institution. To cure the defects of an institution's decision, a turn to the 'subsidiarity' principle may, notwithstanding its own 'inherent weaknesses',[115] turn out to be the best option.

The principle of subsidiarity[116] is a very useful approach in light of the formulation of appropriate decisions. In other words, if there are numerous centres of decision-making all of which may be positioned to carry out a decision regarding a particular matter, the one closest to those affected by the decision may be the best one to make the decision. As already argued above, however, monetary decisions are of such a technical nature that a balancing of the principles of democracy and subsidiarity seems the most appropriate way to handle them.

2.7. PARADIGMS AND STRUCTURAL DESIGNS IN INTERNATIONAL LAW

The question regarding the allocation of authority is very pivotal to the design of an efficient international monetary law framework. Due to globalisation there have been intrusive regulatory demands upon the competences of the state. The absence of a unified global governance structure leads to a lack of co-ordination of the major economic and financial matters in areas such as exchange rate determination. As already discussed above, states

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[112] *Ibid.*

[113] Franck TM "Centrifuge and Centripede: Principles for the Centralisation and Decentralisation of Governance" in Broude T & Shay Y *The Shifting Allocation of Authority in International Law* 2008 at 26-27.

[114] Paulus AL "Subsidiarity, Fragmentation and Democracy: Towards the Demise of General International Law?" in Broude T & Shay Y *The Shifting Allocation of Authority in International Law* 2008 at 201.

[115] *Id* at 206.

[116] Broude T & Shany Y *The Shifting Allocation of Authority in International Law* 2008 at 6 posit that "The principle of subsidiarity stands out for the proposition that normative, political and legal decisions should be taken by the competent authority that is closest to where the impact of the decision will be most felt."

sometimes engage in manipulative exchange arrangements in order to attain balance of payment equilibrium. This may lead to distorted exchange rates as well as currency misalignments. The potential synergies of national complimentarity somehow get lost in the fray of protectionism and self-seeking policy agendas.

A theory of 'multi-layered governance' has developed in response to the competition between global and municipal institutions.[117] Domestic or national law making bodies no longer enjoy exclusive priviledges in law making but are rather augmented in their function by the contributions of other national as well as international institutions. The multiple institutions, state agencies and international regulatory regimes interact in a complimentary fashion. In terms of the multi-level governance model, decision-making competencies are shared by actors at different levels and institutions. One of the contempory scholars of the structural evolution of the international law framework acknowledges the "... emerging system of multilayered governance by which different regulatory levels interact in a mutually supportive, or sometimes conflicting, manner."[118] He further explains hows these multiple layers of governance have developed across the wide spectrum of "local, sub-national, regional and global levels."[119]

A thorough consideration of the emerging institutional relationships reveals the credibility of what Petersmann has observed as regards the changes that have become the defining pursuits of the contemporary legal age. The 'vertical' as well as 'horizontal interdependencies'[120] among state and non-state entities require an inclusive approach rather than fragmented and piece-meal solutions. While states could have in the past enjoyed exclusive legislative powers within their jurisdictions, the fact that global monetary stability now requires co-operation makes it imperative to work together. As such, numerous paradigms of international law have emerged, which view the state not as the central regulator of monetary law, but more as one among multiple centres from which monetary law is being dispensed.

These structural configurations can conveniently be described as either vertical or horizontal in nature. The relationship between the IMF and member states connotes a vertical interaction. This, however, is not a perfectly vertical configuration in that the IMF lakes absolute coercive command upon the state. Yet, to the extent that the IMF law binds the

[117] Garcia FJ & Ciko L "Theories of Justice and International Economic Law" (2011) *Boston Research Paper 252* at 5.
[118] Cottier T "Multilayered Governance, Pluralism and Moral Conflict" (2008) *Swiss National Centre of Competence in Research Working Paper No 2008/*23 at 3.
[119] *Id* at 4.
[120] Petersmann EU "JIEL Debate: Methodological Pluralism and its Criticism in International Economic Law Research" (2012) 15 (4) *Journal of International Economic Law* 921–970 at 950.

member state, it is not a misplaced proposition that the state stands in a relatively subordinate level to the international institution. The Articles of the IMF do have a defining power on the monetary law of the state hence a vertical relationship is discernible between them. The same argument can also be advanced in defining the relationship between the WTO and the contracting powers. The emergence of the WTO law towards the end of the last millenium was seen as the emergence of the "WTO Constitutionalism."[121] The constitutionalisation of international law has been discussed in recent years by among others Petersmann[122] amid an argument that the constitutional pattern is not yet fully developed.

While the interaction between international organisations and their members may be seen to be fashioned in a vertical pattern, the same cannot be said regarding the various multilateral bodies. The WTO and the IMF legal regimes are independent of each other. They regulate international economic interaction in completely divergent spheres. Each one makes its own decisions based on its own rules, processes and pursuits. The fact that the state finds itself having to fulfill obligations in terms of a mandate assigned to it by its own 'democratic constituents' as well as the varied international bodies to which it owes allegiance by virtue of membership puts it in a rather precarious position. No wonder the averment of Pulkowski that contemporary international law 'resembles a dense web of detailed prescriptions in almost any conceivable subject'[123] has merit.

International monetary law is certainly no exception as it is characterised by a plurality of institutions and centres of control. A horizontal relationship is clearly discernible when one takes a look at their patterns of interaction. The states act in the capacities of co-equal sovereigns, in a fashion that is typical of Westphalian patterns of international law. Under such a configuration, the state retains the traditional elements of monetary sovereignty. The state is the centre of monetary power and regulates its monetary affairs with little inhibition. However, the demands of 'collective action', particularly because of globalisation and the interdependent nature of monetary regulation force the state to act differently. Since monetary problems can no longer be contained within national frontiers,[124] internationalisation of decision-making has become the innevitable panacea to the global challenges.

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[121] Charnovitz S "The WTO and the Rights of the Individual" at 13. Available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=282021 (Accessed on 05 January 2014).

[122] Petersmann EU "How to Promote the International Rule of Law" (1998) 1 *Journal of International Economic Law* 24-48 at 33.

[123] Pulkowski D "Structural Paradigms in International Law" in Broude T & Shay Y *The Shifting Allocation of Authority in International Law* 2008 at 51.

[124] Cohen BJ "The international Monetary System: Diffusion and Ambiguity" (2008) 84 (3) *International Affairs* at 455–470 at 463.

Pulkowski's three areas of concern[125] then spring to the foreground and the answers to his questions do serve as a starting point in the search for the most workable and effective way of allocating authority in international law. The first question regards whether international law is still based on state sovereignty. The second one regards how best to account for the involvement of non-state actors in decision-making processes and the last one is an interrogation of the relationships between the various 'functional subsystems' such as regional groupings, monetary unions, free-trade areas as well as multilateral subsystems that enjoy a universal outreach such as the UN and its agencies such as the IMF, the OECD, and many others. There are also some legal obligations created in terms of Bilateral Investment Treaties (BITs) which may also be applicable to a particular monetary law dispute

The answer to the first question is certainly negative as state sovereignty has evidently suffered much erosion.[126] The intermediary state certainly no longer enjoys that unfettered power to regulate without external influence. Even the coercive power has been extended to other centres. Arbitration tribunals such as the International Centre for Settlement of Investment Disputes (ICSID) do make binding decisions as do other tribunals that are set up in terms of international law. The decisions of the WTO's Dipute Settlement Body (DSB) are also very significant in the area of bringing about a solution to the disputes. Yet of course some of the major attributes of the state-centred international law such as the denial of legal personality and legal standing to private individuals and Non-Governmental Organisations (NGOs) remain very dominant.

The second and the third questions cannot be answered simplistically without infering the emergence of a multilayered pattern of governance and it is in light of them that this study turns to explore the 'structural paradigm'[127] of multilevel governance. The plurality of legal regimes, centres of monetary power and decision-making have generated the discourse of '*fragmentation'* of international law.[128] The state is a unique legal subsystem and so are the regional development groups, multilateral subsystems such as the Organisation for Economic Co-operation and Development (OECD) and the IMF. The proliferation of numerous legal regimes and subsystems enjoying overlapping functions subsequently engenders norm conflict, thereby creating a problem of interpretation. Once the state has become party to these subsystems through signing and ratifying their founding statutes, multiple centres of control emerge with regards to the affairs of that state.

[125] Pulkowski D *supra* at 51.
[126] Zimmermann CD "The Concept of MonetarySovereignty Revisited*"* (2013) 24 *The European Journal of International Law* 797–818 at 800.
[127] Pulkowski D *supra* at 51-77.
[128] Paulus LA "Subsidiarity, Fragmentation and Democracy: Towards the Demise of General International Law" in Broude T & Shay Y *The Shifting Allocation of Authority in International Law* 2008 at 197.

The intermediary state is, in terms of the emerging paradigms of international law, expected to play the bridging function among the differently placed institutions. It provides that necessary bridge between the domestic and internation legal regimes. At the municipal level, it balances the demands of the citizens with the demands of the international community. Taking into account that the welfare of the citizens in the remotest part of the least developed countries (LDCs) cannot be compared with those of the inhabitants of London, Berlin and New York, it follows that the state's legislative power must be carefully exercised to protect the weaker while at the same time protecting the welfare of the rich. Starting from the premise that global monetary stability is good for the rich and the poor alike, the state therefore walks the tight rope of keeping stability while also observing the preferences of the various interest groups. As an intermediary functionary and also by virtue of being in possession of the power of coercion, the state remains the focal point of international monetary regulation and its power to legislate is protected in terms of the principles of democracy and subsidiarity. In terms of democracy, the state is assumed to be a legitimate bearer of the mandate granted by its people.

It is one among several levels of governance. The decisions made by it have application not necessarily as absolute and unquestionable decrees but are rather evaluated within the context of the broader international framework. Since national constitutions have become "partial constitutions,"[129] recourse must always be had to the law of international systems particularly where the law of the state does not adequately address the matters concerned.

It is noteworthy that the 'muliti-level European governance' pattern cannot be simply extended to the global system without the risk of distortion,[130] whether as an interpretive model or as a new way of configuring relations. The diversified character of the nations of the world requires a measure of harmonisation in order to fully function as a fully intergrated system. Notwithstanding the diversity however, it is not altogether irrational to perceive the relations between nations as already exhibiting a tendency towards unified behaviour. Questions regarding allocations of competences among the various layers of a multi-level system echo with infinite resonance and as already noted in terms of the European example of multi-level governance, it always matters who does what.[131]

While the EU system has been evolving since its inception and has formed clearly demarcated formulas for 'competence allocation', the interaction that takes place at

[129] Petersmann EU "International Economic Law, 'Public Reason', and Multilevel Governance" (2011) 14 (1) *Journal of International Economic Law* 23–76 at 69.
[130] Wouters J & Ramopoulos T "The G-20 and Global Economic Governance: Lessons from Multi-Level European Governance?" (2012) 15 (3) *Journal of International Economic Law* 751-775 at 752.
[131] Wouters J and Ramopoulos T *supra* at 752-753.

international level is still a hybrid of 'state-centred' and 'multilayered' formations. It is altogether appropriate at this juncture to say that the 'multilayered governance' structural pattern is already in operation and the EU has taken it to an advanced stage.

One way of viewing the current global monetary system therefore is to see the IMF law as constituting a layer in which all members are represented, the OECD law as another as do the numerous regional monetary unions, the state, the agencies and organs of the state as well NGOs. It can aptly be perceived as a heterarchical structure consisting of the functional areas with complimentary roles towards each other. This mosaic of functional sites creates the uniquely complex network of legal relations. Even the state level exhibits these numerous functional sites. As Pulowski notes, "… state law has become a site for internal legal pluralism"[132] as various domestic sub-groups make decisions, thereby turning themselves into legal subsystems. The same legal pluralism is discernible in the context of the international legal system.

From the analysis of trends in recent years, state law is giving way to other regimes. Its functional frontiers are receeding. A new trend is drifting in while new power allocations are being forged.[133] New players[134] such as non-governmental organisations have sprung into relevance while the clamour for human rights also means that the individual citizen has gained great international recognition.[135] Various national and international legal regimes that regulate monetary matters are on the increase.[136] The problems that are most prominent have to do with the task of co-ordinating these functional areas and this comes largely because no single institution enjoys over-arching powers of command or compulsory jurisdiction.[137] The IMF which could have played that co-ordinating role has certainly not done so.[138]

What complicates the current relationships is the absence of a 'general international law'[139] which encompasses all areas of law. As a result, the law is compartmentalised into various functional areas and fragments. Decisions are taken within each compartment in a manner that sometimes has no regard for the other functional areas. Monetary matters are dealt with

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[132] Pulkowski D *supra* at 59.
[133] Domingo R "The Crisis of International Law" (2009) (42) *Vanderbilt Journal of Transnational Law* 1543-1593 at 1553.
[134] *Id* at 1554.
[135] *Id* at 1550.
[136] Institutions such as the IMF, OECD, GATT and GATS as well as BITs all exercise some regulatory influence with regards to monetary law. National institutions such as the central banks, business groupings and non-governmental organisations work together to shape the landscape.
[137] Camdessus M *et al* "Reform of the International Monetary System: A cooperative Approach for the Twent First Century" *The Palais-Royal Initiative* January 18th, 2011 at 4. Available at http://global-currencies.org/smi/gb/telechar/news/Rapport_Camdessus.pdf (Accessed on 05 January 2015).
[138] *Ibid.*
[139] Paulus AL *supra* at 196.

in a different way from trade, human rights or investment matters. The focus of monetary regulation has also shifted from 'territoriality to functionality'[140] in response to the emergence of private and public institutions.

With the emergence of multiple centres of monetary power, and as national public goods turn into global public goods, the international legal system needs to develop suitable 'competence allocation' patterns. The conclusive remarks of Petersmann succintly capture the importance of multilevel constitutionalism. He says:

> "Arguably, multilevel cosmopolitan constitutionalism offers more appropriate constitutional, legal, and democratic foundations for the collective supply of citizen-driven 'aggregate public goods' based on economic liberalism and cosmopolitan rights than state-centered 'legal nationalism' cultivating welfare-reducing border discrimination."[141]

Indeed, interdependent sectors, institutions and structures have become pervasive patterns. The multilevel structural paradigm would, more than any other, provide the appropriate environment for the delivery of a stable global monetary system.

2.8. CONCLUSIONS

This chapter revealed that money is a 'global public good' falling into the class of 'interdependent global public goods.' Its regulation in the current international legal framework can best be carried out by a fully co-operative international legal system rather than by individualistic and self-seeking state laws. Domestic regulators are no longer sufficiently enabled to carry out such functions hence the need for multi-functional, multi-sectoral, multi-regional, and internationally coordinated regulatory mechanisms. The state can no longer single handedly deal with this all important task for which high level co-ordination has been shown to be important. As Petersmann argues, the "collective supply of international public goods requires rules, institutions, and governance mechanisms going beyond those of the Westphalian system of 'international law among sovereign states'"[142]

The Westphalian system of international law, with its main attributes and ramifications is no longer sufficiently equipped to deal with the tasks before it. The intergrated international legal community can no longer be sufficiently serviced by out-dated patterns and models. The multilevel governance approach has become the most appropriate structural paradigm of

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[140] Paulus AL *supra* at 196.
[141] Petersmann EU "JIEL Debate: Methodological Pluralism and its Criticism in International Economic Law Research" (2012) 15 (4) *Journal of International Economic Law* 921-970 at 951.
[142] Petersmann EU "International Economic Law, 'Public Reason', and Multilevel Governance of Interdependent Public Goods" 2010 (2011) 14 (1) *Journal of International Economic Law*, 23–76 at 34.

international monetary regulation. Although the various layers and functional centres are more well developed in the European Community than elsewhere in the world, the principles already tried and tested in the Community can be extended to other centres and regions albeit with necessary modifications.

In the next chapter, the study discusses the theoretical matters regarding monetary sovereignty while also exploring the elements of monetary sovereignty through an analysis of specific legal regimes ranging from national, regional to global multilateral legal systems.

CHAPTER 3

3. MONETARY SOVEREIGNTY: A CONCEPTUAL FRAMEWORK

3.1. INTRODUCTION

The concept of monetary sovereignty, particularly in the present age, remains highly relevant in shaping the global monetary system inspite of the changes and developments that have occurred in international economic relations. The previous chapter considered the conduct of the modern state with regards to monetary affairs. It emerged that expectations have changed significantly over the years and that new paradigms have emerged in an attempt to adequately address the emerging needs of the global monetary system.

A proper understanding of the theoretical matters regarding sovereignty helps to shed light on the factors that shape decision making in international monetary relations. The powers of the state and its interaction with other institutions through bilateral and multilateral engagements are decisive determinants of the choices made by states. Since the state is an intergral part of the multilateral system, the way it is perceived continues to be highly influential.

This chapter begins by giving a brief explanation of the reasons why states cling so tightly onto sovereignty even in the face of highly compelling changes. Secondly, it unpacks the incidences of monetary sovereignty and its practical effects, thus exploring how the particular incidences such as exchange rate determination, exchange controls and capital controls shape the contemporary monetary system. Building upon the premise that sovereignity is not a static concept to be expressed only in terms of *positive* law,[143] the third section of the chapter undertakes an exploration of its normative attributes[144] as well as their role in shaping international monetary order. The fourth and the last section looks at how role players have responded to the normative demands of the age through the pulling together of sovereignty within various international institutions.

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143 Zimmermann CD "The Concept of Monetary Sovereignty Revisited" (2013) 24 (3) *European Journal of International Law* 797–818 at 805. See also Howse R "Sovereignty Lost and Found" in Shan W, Simmons P and Singh D (eds) *Redefining Sovereignty in International Economic Law* 2008 at at 61.

144 Zimmermann CD *supra* at 805.

3.2. MONETARY POWER, FISCAL MATTERS AND THE STATE

Throughout history, states have resorted to inflationary printing of money when ever they found themselves in urgent need of cheap money.[145] Inflationary printing of money is a cheap source of cash for a state during times of war or other emergencies. The state relies on 'inflation tax'[146] because of

> " … the existence of a close interaction between the monetary regime, (that is, the behavior of the central bank / monetary authorities) and the fiscal regime (that is, the tax and spending behavior of governments) …"[147]

The connection is the reason why states are not prepared to easily relinquish their monetary sovereignty. Seigniorage tax[148] is an important means to generate revenue for the state. Cohen defines it as

> "the spending power that accrues from the state's ability to create money. Technically identified as the excess of the nominal value of a currency over its cost of production …"[149]

It can be perceived as the difference between the face value of a note or a coin and the actual cost of printing the note or minting it. Debasement, a practice whereby a cheap alloy of metal is minted into coin of less real value than the face value is sometimes adopted to raise state revenue.

Mundell[150] attributes the rise of state monopoly in monetary production to the emergence of 'overvalued moneys'. States exploit their capacity to charge seigniorage tax for fiscal purposes. They use it to generate revenue and to finance governmemental expenditure. It is, however, of critical importance to realise that some states have lately sacrificed their seigiorage rights through dollarisation, adoption of currency boards and other measures. These states have been able to restrict themselves to prudent conduct as they pursue a

[145] Britain adopted this measure during the Napoleonic Wars and World War 1 while the US Legal Tender Act led to the adoption of greenbacks during the Civil War of 1861-1865. The Eurozone crisis clearly illustrates the importance of fiscal policies in adjusting domestic economies. The lack of fiscal policy harmony among members compromised the ESCB' capacity to adjust the monetary parameters.

[146] Cohen BJ *Global Monetary Governance* 2008 at 200.

[147] Bordo M D & Jonung L "A Return to the Convertibility Principle? Monetary and Fiscal Regimes in Historical Perspective: The International Evidence" in Leijonhufvud A (ed) *Monetary Theory and Experience* 2001 at 265.

[148] Baltensperger E & Cottier T "The Role of International Law in Monetary Affairs" (2010) 13 (3) *Journal of International Economic Law* 911–937 at 914 states that, "The possibility of making profits by issuing notes was one reason why the right to issue was conferred to central governments over time."

[149] Cohen BJ *supra* at 237.

[150] Mundell R A "Money and the Sovereignty of the State" in Leijonhufvud A (ed) *Monetary Theory and Experience* 2001 at 298.

greater ideal. The greater ideal is monetary stability seen as more important than inflation financing.

The concept of monetary sovereigny still faces so much criticism from various quarters, among them the free banking school. It is argued that states should liberalise the issuing of bank notes and coins to allow private players just as there is free production of shoes in an open market.[151] One of the proponents of the liberalisation of 'monetary production', Hulsmann seriously questions the economic assumptions which support the state's monopoly of monetary production.[152] The dominant view, however, is that the state's sovereignty over monetary affairs is a long established fact which needs not be debated further.[153] The normative elements of monetary regulation, which shall be discussed in one of the succeeding sections, include maintenance of monetary stability as an important quality of the monetary system, one which private parties cannot sufficiently protect. The position of states with regards to accountability, legitimacy and assurances of monetary stability poses less risk than private players would.

The prevalence of three principal corrective devices used by states, namely exchange rate alteration, direct commercial and financial controls including quantity and exchange restrictions as well as instruments of adjustment in domestic economic policies[154] are very important to the running of national economies. The privatisation of such instruments would deprive the state of the vital tools of governance. The state's choice and use of the corrective measures is the collective concern of all others because of their impact on other states. The states' use of corrective devices is the next point of the discussion.

3.3. MULTIDIMENSIONAL MONETARY SOVEREIGNTY: A SEARCH FOR IDEALS

As already mentioned in the introduction, the concept of monetary sovereignty seemingly exhibits both positive and normative attributes. A definition of the concept serves as a convenient starting point for the discusion.

[151] Lastra RM *Legal Foundations of International Monetary Stability* 2006 at 22 footnote 69. The free banking school proposes the elimination of central banking followed by the liberalisation of money production to private players. Markets would freely choose currencies based on factors such as stability and exchange rates. Such a view throws the concept of monetary sovereignty into jeopardy.

[152] Hulsmann J G "The Ethics of Monetary Production" (2011) Available at https://www.youtube.com/watch?v=8zYg4E4zbPo (Accessed on 08 November 2014.)

[153] Shuster M R *The Public International Law of Money* 1973 at 9. See Balternsperger E & Cottier T "The Role of International Law in Monetary Affairs" (2010) 13(3) *Journal of International Economic Law* 911–937 at 914 who argue that only the state can effectively to protect the monetary rights while the principles of contract cannot.

[154] Shuster M R *supra* at 317.

A reference to the positive conceptions of monetary sovereignty suggests a catalogue or list of competencies enjoyed by states in this area of law. It tells of the rights, entitlements and powers that a state enjoys in the area of monetary regulation. It is a reference to 'the law as it is rather than the law as it ought to be.' As regards legal positivism, Johnson *et al* say:

> "Austin acknowledges that beyond the law as it is or positive law, there lies the important science of ethics and morality which is concerned with law as it ought to be and how to study legislation."[155]

This approach to law, concerning itself with the formal contours of the black letter is premised upon the assumption that the law can be verifiable just by looking at what is written in the municipal and multilateral statutes and codes. Since the law is nothing but 'the commands of the sovereign',[156] it would be easy to find out what monetary law is just by looking into state enactments or international conventions. A simple study of relevant sources of law reveals the legal position on any matter. The criticism directed against Durgard[157] sheds light on the nature of the contestations that exist with regard to legal positivism. However, these debates lie outside the scope of this work.

A normative discourse of the law on the other hand leads to an enquiry into many facets of the law among them the theories of justice that underly every decree of law.[158] The concept of 'justice' refers to "the need for justifying law and governance on the basis of principles of procedural, distributive, corrective or 'commutative justice' or principles of equity."[159] The law is perceived as a discipline that is laden with values of multiple dimensions. Since the law is meant to regulate the lives of people and not innanimate objects, it cannot be seen to be distant from the needs of those whose lives it seeks to regulate. Among numerous considerations, a balance has to be struck between diverse narratives of analysis. Reference to communitarianism, liberalism, realism among others provides yardsticks against which sovereign action can be measured.[160]

Theories of justice within normative value systems therefore set a contextual background for the conceptualisation of monetary sovereignty. Petersmann suggests that there is need to

[155] Johnson D, Pete S, Max du Plessis *Jurisprudence: A South African Perspective* 2001 at 72.
[156] The view of positivism adopted in this study is based on the thesis that the law is established by the sovereign, as commands backed by a sanction and habitually obeyed by the subjects. See Roeder C and Moellendorf D *Jurisprudence* 2004 at 71.
[157] Forsyth C and Schiller J ""The Judicial Process, Positivism and Civil Liberty II" (1981) *South Africal Law Journal* 218- 230.
[158] Garcia FJ "Glob+al Justice and the Bretton Woods" (2007) 10 (3) *Journal of International Economi Law* 461–481 at 466.
[159] Petersmann EU *International Economic Law in the 21st Century: Constitutional Pluralism and Multilevel Governance of Interdependent Public Goods* 2012 at 203.
[160] These philosophical considerations of law play decisive roles in shaping the procedural process of the law.

see the importance "of 'public reason' based on cosmopolitan freedoms and other 'priciples of justice'."[161] The plurality of approaches[162] and legal traditions create a playing field where theories of justice such as utilitarianism meet with legal positivism, thus influencing both the formulation and interpretation of the law. Continual review of the changing values and aspirations of the global society need not be altogether ignored and the the law should never stagnate in comformity with the value systems of Westphalia. Rather it must continue to inform the agenda for future legal developments.

3.4. MONETARY SOVEREIGNTY: A LEGAL POSITIVISTIC VIEW

When approached from the angle of legal positivism, a number of definitions have been proposed for the concept of 'monetary sovereignty'.[163] Mundell breaks it into constituent parts as

> "the right to determine what constitutes the unit of account – the commodity or token in which the price lists are specified, the right to determine means of payment – legal tender for the purposes of discharge of debt and the right to produce money – or else to determine the conditions under which it is to be produced by others."[164]

Lastra on the other hand perceives the concept so broadly as to encompass the "power to issue notes and coins", to regulate internal and external dimensions of money, the banking system and the determination of credit levels and rules, the management of the payment and settlement systems, the competence to make decisions regarding money supply and interest rates and determine monetary policy. It also includes the right to control the exchange rates and choice of exchange regime as well as the power to introduce and maintain exchange and capital controls.[165] In recent years banking regulation and supervision have seemed to attract greater international attention due in part, to the spill-over effects arising from systemic failure experienced in various states.

Mann states that:

[161] *Petersmann E U supra* at 6.
[162] Petersmann E U *supra* at 12.
[163] Gianviti F (2006) 4 "Current Legal Aspects of Monetary Sovereignty" in IMF, *Current Developments in Monetary and Financial Law,* 3-16 at 4**.** Treves T "Monetary Sovereignty Today" in Giovanoli M (ed) *International Monetary Law: Issues for the New Millenium* 2000 at 117.
[164] Mundell R A "Money and the Sovereignty of the State" in Leijonhufvud A (ed) *Monetary Theory and Experience* 2001 at 303.
[165] Lastra RM *supra* at 22-23.

> "[T]he municipal legislator is free to define the currency of his country, to decide whether or no it should be based on gold, to depreciate and appreciate its value, to permit or abolish gold clauses, to impose exchange control or to take other measures affecting monetary relations."[166]

Explicably, it is within state competences to act in self-interest and impose exchange restrictions, maintain restrictions on current account convertibility, capital controls and to inhibit cross-border capital flows as well as to avoid currency manipulations which may cause exchange rate instability.[167] The attributes cited above are at the core of the concept and though not cast in stone, have arguably crystalised into a conclusive outline of the concept. One of the most prevailing and long-standing assertions is that "Money is a creature of the Law."[168] The state is also responsible for determining the unit which serves as the basis of the monetary system.[169]

A point by point analysis of the key attributes is the subject of the next subsection.

3.4.1 THE STATE FUNCTION OF DETERMINING THE CURRENCY UNIT

The determination of a currency unit can be approached on the basis of a technical or a nominalist theory.[170] As Knapp[171] explains, in terms of the technical approach, the value of one unit is expressed in relation to another. The application of the comparative approach is in line with the commodity approach to money. In line with the dominance of a *fiat* standard, this approach has fallen out of step with modern practice. By juristic acts, the state creates means of payment that do not have the character of commodities or *specie*. As such, bank notes express a monetary unit which has no connection with any *specie* or weights of precious commodities as used to be the case.

While the pound used to represent a weight and the gold smith or reserve bank could, if called upon to pay a pound, simply weigh bullion and give it out in payment, things became complicated in recent years due to the emergence of inconvertible paper moneys. A British Pound Sterling cannot be perceived as a weight any more. It is a creature of a national legal tradition and obtains its name through a historical and recurrent linking with the erstwhile

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[166] Mann FA *The Legal Aspect of Money* 5th Edition 1992 at 461.
[167] Viterbo A *International Economic Law and Monetary Measures: Limitations to State Sovereignty and Dispute Settlement* 2012 at 1.
[168] Knapp GF *The State Theory of Money* 1924 at 1. Cohen BJ *Global Monetary Governance* 2008 at 38.
[169] Shuster M R *The Public International Law of Money* 1973 at 24.
[170] Knapp GF *The State Theory of Money* 1924 at 8.
[171] *Ibid.*

specie that once constituted it. It can best be characterised as “simply a name for something which cannot be precisely defined.”[172] The same can be said concerning the dollar.

The value of a bank note or coin does not differ from the inscription upon its face and by the principle of nominalism a one Dollar obligation is fully discharged by a similarly denominated note or coin. The paper has no instrinsic value in itself. A dollar is what the legislature declares it to be, nothing more nothing less. A unit may be created by a treaty or supranational institution as in the case of the Euro. It is not an expression of weight. Its definition has to be sought outside the realm of weights. Whether it is to be called a pound, dollar, mark, yen or rand is a matter that can only be determined in terms of national law.[173] The South African statutory law ilustrates the point clearly:

> “The monetary unit of the Republic shall be the rand (abbreviated as R), and the cent (abbreviated as c), which is one hundredth part of the rand.”[174]

The determination of the unit is a matter that lies exclusively in the province of the state. Another important point is the locus of the power to coin and to print notes and is next point to consider.

3.4.2 COINAGE AND PRINTING OF BANK NOTES: UNASSAILABLE ATTRIBUTES OF STATEHOOD

Coinage took place in Rome as far back as 300 BC, long before the city states of Greece[175] did it. The authority of the state in regulating coinage was acknowledged in the Hellenic city states, recognising[176] the state’s exclusive authority in this regard. Meanwhile, the US Constitution empowers the Congress;

> “To coin money, regulate the Value thereof, and of foreign Coin, and fix the Standard of Weights and Measures; To provide for the Punishment of conterfeiting the Securities and current Coin of the United States;”[177]

Coinage of money by non-sovereigns has always attracted severe penalties. The trial of Louis Secretain in the middle ages is a prime example of such trials which resulted in the

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[172] Mann F A *supra* at 49.
[173] Knapp G F *supra* at 8.
[174] Section 15 (1) of the South African Reserve Bank Act 90 of 1989. This argument is premised on the assumption that the bank is a state entity, an organ of the state whose actions are attributable to the Republic.
[175] Burnett A *Coinage in the Roman World* 1987 at 1.
[176] *Id* at 17.
[177] Article 1, Section 8 of the US Constitution highlights the powers of the Congress with regards to many aspects of governance and monetary power.

execution of the convicts.[178] Jesus, more than two thousand years ago, also seemingly acknowledged Ceaser's prerogative of money production.[179] All these submissions point towards the fact that coinage has, since antiquity, been viewed as an intergral part of sovereignty.

3.4.3 MONETARY STANDARD SETTING

The state sets a monetary standard in terms of its sovereign powers through anchoring the monetary unit to one of the select standards such as commodities. It also has the power to demonetise commodities and to change parities without being liable in international law. Faced with an unstable currency in 1933, the US Congress passed a joint resolution to abrogate gold clauses. All payments in gold were subsequently rendered unlawful and obligations covered by such clauses were to be paid in terms of the nominal value 'dollar for dollar'[180]. The resolution substantially altered the value that creditors would receive. In the case of *Norman v. Baltimore & Ohio Railroad Co.*[181] one of the several prejudiced parties questioned the constitutional validity of the resolution. The importance of the resultant US Supreme Court decision in the context of the current discussion is the extent to which it butresses the argument that determination of monetary standards is a state competence.

The adoption of 'debased' or 'token' coins by the British government at the height of the Napoleonic wars was a sovereign act for which the state would not incur liablity in terms of domestic or international law. The resumption of convertibility[182] was a purely sovereign act. The US Coinage Act of 1873 which resulted in the demonetisation of silver and ended the days of the bimetalism of gold and silver was another sovereign act which demonstrably endorsed the practice of the state priviledge to determine the monetary standard.[183]

The power of state power to set a monetary standard is therefore an established fact of law and each state determines whether its money is to be based on a commodity standard such

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[178] The account of the trial is given vividly in Mundell R A *supra* at 333 footnote 17 which quotes Nussbaum's account of the execution of Sectretain.

[179] In Matthew 22:21 a point is raised that Caeser is the legitimate authority regarding the production of money which happens to bear his potrait as its superscription.

[180] The US Congress Joint Resolution of 5 June 1933 abrogated the clauses that protected the value of obligations, declaring that "All coins and currency of the Unites States (including Federal Reserve notes … … shall be legal tender for all debts public and private, …)

[181] *Norman v. Baltimore & Ohio Railroad Co.,* 294 U.S. 240 (1935).

[182] The Peel's Act of 1819, brought Britain onto a monometallic gold standard which prevailed until the outbreak of World War I in 1914. See also Wood JH *A History of Central Banking in Great Britain and the United States* 2005 at 51. Friedman M *Money Mischief: Episodes of Monetary History* 1994 at 148-149.

[183] Friedman M & Savage LJ *Milton Friedman on Economics: Selected Papers* 2007 at 151-152.

as gold[184], silver or a fiat standard. Convertibility or non-convertibility of currency into *specie* also forms part of this competence.

3.4.4 EXCHANGE RATE DETERMINATION

The state also determines the exchange regime for its currency. When exchange rates are unilaterally determined by each state, there is room for their manipulation. One of the purposes of the IMF as spelt out in its Articles of Agreement is to "avoid manipulating exchange rates or the international monetary system …"[185] The collapse of the Bretton Woods system in 1971 restored to states the powers to determine exchange regimes. The system had operated on a fixed *par value* system but its collapse allowed for several options of exchange rate regimes for states to choose from.[186] These range from fixed exchange rate regimes, free floating exchange systems, pegged floats, floats crawling within narrow bands among others. Some currencies are either pegged to stable reserve currencies such as the US Dollar or the Pound Sterling while others are anchored to a basket of dominant international currencies. The collapse of the Bretton Woods system in 1971 restored the states' power in the area of exchange rate determination. The IMF was "stripped of its pricing and regulatory role with respect to the developed world …"[187]

The debate regarding the locus of sovereignty particularly with regards to monetary power seems to favour the view that the state still enjoys a great deal of power inspite of what appears to be a sweeping tide of globalisation. After protracted diplomatic engagements between China and the USA over the allegedly undervalued Chinese currency, a factor largely considered by the USA as generating negative effects on the US economy, the adoption of a policy of "quantitative easing"[188] by the Obama administration in 2009 was undoubtedly an invocation of the state's sovereign powers.

Even though there appears to be freedom of choice and action, the IMF keeps a keen watch over the state's conduct with regards to exchange rate regimes and implementation.[189] The

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[184] Booysen H *Principles of International Trade Law as a Monistic System* 2003 at 320.
[185] Article IV:1(iii) of the IMF
[186] Jung H "Tackling Currency Manipulation with International Law: Why and How Currency Manipulation should be Adjudicated?" (2012) 9 (2) *Manchester Journal of International Economic Law* 184-200, at 193.
[187] Howse R "Sovereignty Lost and Found" in Shan W, Simmons P and Singh D (eds) *Redefining Sovereignty in International Economic Law* 2008 at at 67.
[188] Rickards J *supra* at 134 states that "Quantitative easing in its simplest form is just printing money". Rickards describes how the increase in the money supply of the Federal reserve system generated inflation abroad and produced a cheaper dollar thereby stimulating the US export market while depressing the import market. As a result, 25 Million jobs were generated.
[189] Mussa M "IMF Survellance Over China's Exchange rate Policy (2007) *Peterson Institute of International Economics* at 1.

prevalence of an allegation of exchange manipulation is indicative of the fact that neither China nor the USA enjoys unlimited right of action with regards to her exchange rate choices.[190] Even though liberty is available to the states, discriminatory multiple exchange rate systems, currency manipulations and unorthodox market interventions are the causes for so-called 'currency wars'.[191]

3.4.5 DECLARATION OF LEGAL TENDER

The law of the state determines legal tender.[192] Numerous payment instruments may perform monetary functions without necessarily being legal tender. An example of such an instrument is foreign currency. In Zimbabwe, between the years 2002 and 2009, market players circulated the South African Rand, the Botswana Pula, the US Dollar, and the British Pound Sterling even though the currencies were not legal tender. The official adoption of the foreign currencies as legal tender[193] only legitimised what had long become market practice.[194]

The effects of the declaration of legal tender by state authorities is far reaching. Once an instrument acquires legal tender status, its presentation leads to a discharge of the debt from the monetary obligation for which it is offered. The English case of mixed moneys[195] involved a dispute regarding the Queen of England's powers to declare legal tender when she *expost facto* changed legal tender to the detriment of a certain debtor. When the debtor refused the debased tender and sued for payment in terms of the previous monetary compositions, the debtor succesfully raised a 'legal tender' plea. The case illustrates "the great importance of the institution of legal tender and the authority of the sovereign to determine legal tender."[196]

The US legal tender cases of the 19th century also clearly illustrate this point. The state enacted the Legal Tender Act in 1862, in terms of which 'greenbacks' were to be accepted as 'legal tender for all debts.' The notes carried a lower intrinsic value than coins of the same

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[190] Miranda J "Currency undervaluation as a violation of GATT Article XV(4)" in Simon J Evenett (ed) *The US-Sino Currency Dispute: New Insights from Economics, A VoxEU.org Report* 2010 115-126 analyses the legal implications of the US grievance against China over the undervalued RMB which is allegedly exerting great economic strain of the US system.
[191] The tern is attributed to the Brazillian Finance Minister Guido Mantega who in 2010 said "We are in the midst of an international currency war." Source; http://www.bbc.com/news/business-11424864 (Accessed 09 November 2014).
[192] Mann F A *supra* at 42.
[193] The matter has been discussed at paragraph 2.4 of this study.
[194] Section 41 of the Reserve Bank of Zimbabwe Chapter 22:15 deals with legal tender status of bank notes. In 2009 the state adpoted a multiple currency arrangement but RBZ bank notes and coins were not demonetised (following the adoption of the foreign currencies) until 2015.
[195] Mundell R A *supra* at 303. The case occurred in England following the Irish rebellion of 1598 and the subsequent attempts by the Queen to stretch the Royal budget through inflation financing.
[196] Mundell R A *supra* at 304.

denomination. The constitutionality of the Act was questioned in the courts in a number of cases such as the *Hepburn* v *Griswold*[197] case. It was reiterated that the power to declare legal tender is inherent in the sovereignty of the state. The constitutional validity of the printing of 'greebacks was challenged on the basis that to "coin money" is not synymous with printing it.[198] As is apparent from the preceding discussion, the cases underscored the state's power to declare the instruments that serve as legal tender.

In terms of South African law, a statute defines legal tender.[199] Different jurisdictions have the power to pass laws that determine legal tender.[200] The power to enact legal tender laws clearly belongs to the state.

3.4.6 CURRENCY VALUATION AS AN ESTABLISHED STATE COMPETENCE

The state's sovereign power to fix the internal as well as the external value of its currency is a settled matter in international law.[201] Customary international law does not place liablity on a state for the fluctuation of the value of its currency triggered by *bona fide* monetary reform[202] unless the state action systematically targets individuals of a particular nationality. The test for the legitimacy of state conduct is that it must be in pursuit of monetary stability, solvency and other related economic criterion. The state can devalue currency or revalue it while carrying out sovereign duties. In the *Zuk Claim*[203] case which concerned depreciated Russian Roubles, the United States Foreign Claims Settlement Commission held that "It is universally recognized that all matters pertaining to currency are inherently within the jurisdiction of the state." A simillar line of reasoning was followed in the case of *Malan Claim*[204] regarding the depreciated Italian Lira. This power of the state can however be limited in certain circumstances to avoid unfavourable results and a state will invoke diplomatic protection of the rights of its citizens in cases of discrimination and abuse of

[197] The cases questioned the constitutional validity of the Legal Tender Legislation and among them is the *Hepburn* v *Griswold , Knox* v *Lee Juilliard vGreenman* 110 US. 421 (1884). Some of these cases involved war time obligations while others involved peacetime decisions.
[198] Article 1, Section 8 and point 5 of the Constitution of the USA which outlines the powers of the state in the exercise of monetary power.
[199] Section 17 (2) of the South African Reserve Bank Act 90 of 1989 reads; "A tender, including a tender by the Bank itself, of an undefaced and unmutilated coin which is lawfully in circulation in the Republic and of current mass, shall be a legal tender of payment of money- … and the value of each coin so tendered shall be equal to the amount specified on that coin."
[200] See Mann FA *supra* at 42-43 who gives a detailed description of the legislative enactments that were operative in the UK at the time of his writing.
[201] Shuster M R *supra* at 53.
[202] *Ibid.*
[203] *Zuk Claim* United States Foreign Claims Settlement Commission *International Law Reports* Vol. 26 (1958) II at 285.
[204] *Malan Claim* United States Foreign Claims Settlement Commission *International Law Reports* Vol. 26 *(1958)* II *at* 290-1.

rights.[205] Nationalisation, prohibition of transfer as well as compulsory expropiation of property belonging to aliens, are measures which diminish a person's rights to enjoy his property and if done without adequate compensation, are actions not justifiable within the ambit of national sovereignty.[206]

3.4.7 EXCHANGE RESTRICTIONS, CURRNCY CONVERTIBILITY AND CAPITAL RESTRICTIONS

Movements of capital in and out of an economy can cause disruptions of the monetary and financial systems and to avoid these effects, states sometimes adopt restrictions of inflows and outflows as macro-economic management services. Exchange restrictions[207] are also an important tool to redress a balance of payments problem, to stabilise exchange rates and prevent capital flight.[208]

States employ the corrective instruments in response to what Kelsey calls the

> "… six distinct fears: fear of currency appreciation that impacts on exports and the broader economy; the risks of sudden capital injections and reversals arising from so-called 'hot money' flows; dislocations that large capital inflows might cause to the financial system; the disconnect between monetary policy objectives and capital inflows; the fuelling of property and stock market bubbles; and capital flight in reaction to domestic or international crises."[209]

Owing to the importance of cross border capital movements, states do sometimes adopt policies that render their currencies either convertible or inconvertible. Convertibility refers to the freedom to exchange domestic currency for foreign currencies.[210] Transactions can be classified as being either of a current or capital nature. States are, in terms of customary international law, free to unilaterally impose restrictions on international payments without

[205] *Zuk Claim supra at* 285.

[206] *Chobady Claim* United States Foreign Claims Settlement Commission *International Law Reports* Vol. 26 (1958) II *International Law* at 293. *Murescan Claim* United States Foreign Claims Settlement Commission *International Law Reports* Vol. 26 (1958) II International Law Reports 294-5.

[207] Exchange restrictions are distinguishable from Exchange Controls. Reference to exchange controls is to a wide array of measures including the acquisition of licences for foreign currency purchases and other administrative steps which do not necessarily prevent payment for transactions.

[208] Pasini FL "Movement of Capital and Trade in Services: Distinguishing Myth from Reality Regarding the GATS and the Liberation of the Capital Account" (2012) 15 (2) *Journal of International Economic Law* 581-619. Kelsey J "The Conundrum of Shifting Orthodoxies: FTAs and Korea's Currency Controls" (2011) 14 (4) *Journal of International Economic Law* 845–868 at 847.

[209] Kelsey J *supra.* at 852

[210] Viterbo A *International Economic Law and Monetary Measures: Limitations to State Sovereignty and Dispute Settlement* 2012 at 152.

incuring any international wrong by their actions.[211] Restrictions on current payments are however problematic.

Current transactions refer to "payments due in connection with foreign trade, other current business, including services, and normal short-term banking and credit facilities …"[212] A transaction is current "if it gives rise to the immediate return of goods or services"[213] and is distinguishable from a capital one which "gives rise to a future return."[214] Multilateral legal regimes such as the IMF Article VIII (2) and the OECD Code of Liberalisation of Visible and Invisible Current Transactions have brought substantial limitations on the state's power to restrict current payments. It is unveiled in Chapter4 of this study that certain constraints operate against exchange restrictions.

Capital transactions relate to movement of capital for the purposes of investment. They are principal transactions while current payments are surbodinate to some underlying transaction[215] such as a sale of visible goods or payment for an invisible transaction such as a rendered service. Exchange controls create many problems as they can sometimes prohibit the importation or exportation of domestic bank notes.[216]

Even with all the disadvantages they may pose, capital controls are an attribute of statehood often used to counter the destabilising effects of capital movements.[217] The adoption of exchange controls by Iceland[218] in 2008 is a recent example of an attempt by a state to protect its monetary system from the possible destabilising effects of cross border capital flows. Korea did the same in 2010 in order to avoid a looming crisis.[219]

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[211] Shuster MR *supra* at 71.
[212] IMF Article XXX(*d)* Payments for current transactions means payments … not for … transfering capital, and includes … (1) all payments due in connection with foreign trade, other current business, including services, and normal short term banking and credit facilities; (2) payments due as interest on loans and as net income from other investments; (3) payments of moderate amount for amortization of loans or for depreciation of direct investments; and (4) moderate remittances for family living expenses.
[213] Shuster MR *supra* at 34.
[214] *Ibid.*
[215] Pasini FL "Movement of Capital and Trade in Services: Distinguishing Myth from Reality Regarding the GATS and the Liberation of the Capital Account" (2012) 15 (2) *Journal of International Economic Law* 581-619 at 589.
[216] Mann FA *supra* at 418.
[217] Kelsey J *supra* at 847.
[218] Viterbo A "Iceland's capital controls and the constraints imposed by the EEA agreement" (2011) *Capital Markets Law Journal* 214-237.
[219] Kelsey J *supra* 845–868.

3.4.8 THE OPERATION OF QUANTITATIVE RESRICTIONS OR DIRECT CONTROLS

Quantitative restrictions are also employed to correct a balance of payments disequilibrium just as the monetary or trade measures may be used for the same purposes. Trade measures and monetary controls play complimentary corrective functions on the economy.[220] The Tokyo Declaration of 1973 stated that:

> "The policy of liberalizing world trade cannot be carried out successfully in the absence of parallel efforts to set up a monetary system which shields the world economy from the shocks and imbalances which have previously occurred."[221]

As Seigel notes, "the objectives of the WTO and the IMF are complementary."[222] GATT Article XV is the closest attempt to bridge the gap between the two international economic institutions since the coming into effect of the second amendement of IMF Article IV in 1978.[223]

3.4.9 THE BANKING SYSTEM AND DETERMINATION OF MONEY SUPPLY AND POLICY

While the state still retains the competence to coin money and print bank notes, it remains important to realise that money supply is no longer the exclusive domain of the state. Money in the form of notes and coins constitutes a very small fraction of the total monetary supply in most national monetary economies.[224] Rickards for instance notes that while the monetary base in the form of coins and bank notes constitutes about 20% of the total federal reserve system money supply, banks are responsible for creating the 80% through issuing credit and demand deposits.[225] Private institutions such as banks create monetary aggregates such as demand deposits and credit which technically increases money supply in an economy. Expansionary or contractionary outcomes on the national money supply are effected through the banking system. Unless the state exercises control over the creation of credit and other

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[220] Shuster MR *supra* at 140 argues that "restrictive trade and payment measures are both symptoms of, and cures for the same ailment- namely, a balance of payment deficit."

[221] The 7th point of the Tokyo Declaration, 14 September 1973 issued following the GATT ministerial conference known as the Tokyo round. Available at http://www.cvce.eu/obj/the_tokyo_declaration_14_september_1973-en-641c04eb-2900-4ac3-b07d-1a0467477cdc.html (Accessed on 18 January 2015).

[222] Siegel DE "Legal Aspects of the IMF/WTO Relationship; The Fund's Articles of Agreement and the WTO Agreements" (2002) 96 *The American Journal of International Law* at 563.

[223] Thorstensen V, Ramos D & Muller C "The Missing Link Between the WTO and the IMF" (2013) 16 (2) *Journal of International Economic Law* 353–381 at 357.

[224] Zimmermann CD "The Concept of Monetary Sovereignty Revisited" (2013) 24 (3) *European Journal of International Law* 797–818 at footnote 35 notes that by February 2011, cash constituted about 8.4% of the money supply in the Eurozone. At least 90% of money supply existed in scriptural forms and was generated by non-state actors.

[225] Rickards J *supra* at 179.

instruments of payment, it cannot claim to have full control over its monetary affairs. Central banks carry out supervisory functions on behalf of the state and also provide lender of last resort services so as to safeguard financial stability which has remote but realistically harmful effects on the monetary system.[226]

Having analysed the position of the law regarding the power of the state to coin money, to determine monetary units and standards, to unilaterally alter the exchange rate, to devalue the currency, to adopt and maintain exchange controls and restrictions, it is a conceivable proposition that state monetary powers are still comprehensive and far reaching. The position well expressed by Shuster who says that:

> "… a state is uninhibited in its power to alter the exchange rate of its currency and to impose exchange controls (subject to certain largely ineffective limitations), without thereby giving rise to an international wrong, even though foreign creditors and international trade will almost invariably be affected by such measures"[227],

is still highly persuasive. Shuster[228] acknowledges the existence of limitations or constraints operating against state power albeit with modest effects. It is the constraints alluded to above which lie at the heart of the next chapter of this study.

3.5. NORMATIVE TRAITS OF MONETARY SOVEREIGNTY

Every exercise of power leans on certain normative values and the exercise of monetary sovereignty is no exception. As an instrument of governance, the law needs to be justified through reference to values.[229] The values are numerous and varied and their delimitation remains a highly contested terrain.[230] Among them however are; "democracy, equality, accountability, and legitimacy and more specific ones like economic development, the maximization of global welfare, the maintenance of financial intergrity, and the promotion of

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[226] The distinction between the monetary and financial systems is somehow blurred. Viterbo A *International Economic Law And Monetary Measures Limitations to States' Sovereignty and Dispute Settlement* 2012 at 32 notes that the monetary system refers to "stability of exchange rates as well as to the transferability and convertibility of currencies" while the financial system refers to "financial markets and institutions, … the rules and regulations that govern them." The distiction is "no longer tenable". The "two are … inextricably intertwined … elements of a unique system."
[227] Shuster MR *supra* at 46.
[228] *Ibid.*
[229] Petersmann EU *International Economic Law in the 21st Century: Constitutional Pluralism and Multilevel Governance of Interdependent Public Goods* 2012 at 161.
[230] Zimmermann CD "The Concept of Monetary Sovereignty Revisited" (2013) 24 (3) *European Journal of International Law* 797–818 at 809.

financial and monetary stability."[231] Economic theory is a value system that influences the law making process in a significant way. A look at each of these values in the context of what effect it has on the exercise of monetary sovereignty will shed light on how the concept continues to evolve in an adaptative fashion in response to the on-going developments.

In one of his recent publications, Petersmann poses at least fifteen questions under the rubric of "basic systemic questions and regulatory problems of international economic regulation in the twenty first century."[232] His second question reads as follows:

> "Does IEL need to be justified by theories of justice? Is the prevailing conception of 'public international law among sovereign states' consistent with the human rights obligations of all UN member states …"[233]

He goes on to say that anyone trying to answer any of these questions will be influenced by the normative premises upon which he stands.[234] How are human rights, democracy and cosmopolitan liberties to be reconciled with majoritarian dictatorship, utilitarianism and 'state interests' normally communicated through the dominant voice of those wielding power? If a legislative act of a state can impoverish a private individual and wipe out lifetime savings as happened to *Zuk*[235], it may be asked whether international law should not come to the rescue of the individual through a creditor friendly remedy? Such questions strike at the foundation of the principles of justice.

In light of these normative concerns, it goes without saying that the erstwhile perceptions of monetary sovereignty cannot meet the demands of the age. A positivist and formalistic outlook towards the concept disregards the values, largely viewing monetary sovereignty through the prism of a cataloged list of state competences. Such a view certainly overlooks the interdependencies that have become part and parcel of the current international economic relations.

Positive rules of monetary sovereignty have increasingly fallen victim to the re-defining changes of the new age. The predominance of values such as democracy tends to promote a more people oriented perception of sovereignty than autocratic kings of antiquity were ready to admit. Instead of forcibly obtained allegiance that granted sovereign status to the

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[231] Zimmermann *supra* at 810.
[232] Petersmann E U *International Economic Law in the 21st Century: Constitutional Pluralism and Multilevel Governance of Interdependent Public Goods* 2012 at 38.
[233] Petersmann *supra* at 38.
[234] *Id* at 41.
[235] *Zuk Claim* United States Foreign Claims Settlement Commission *International Law Reports* Vol. 26 (1958) II at 285.

autocrats and hereditary monarchs, the state institutions have been re-modelled as servants of the people. Sovereignty has become representative in nature.[236] The people form the principal body and the state acts in a representative capacity on behalf of the body. It is not the head of state who is the bearer of sovereignty but he exercises it on behalf of the electorate. The social contract theories become relevant in the analysis.

Closely aligned to democratic values is the matter regarding legitimacy. Unless those endowed with power to govern are perceived as legitimate, their acts remain subject to challenge. 'Collusion' among peridically elected politicians and rent-seeking interest groups tend to divert the national agenda but decentralisation of power into international institutions is an important safeguard for democratic ideals.[237] Emphasis on the ideals of economic development, the quest for the maximisation of global welfare, the maintenance of financial intergrity, the promotion of financial and monetary stability all point towards the need for an interpretive approach that recognises the dynamism of monetary sovereignty.

3.6. RESPONSES TO CONCEPTUAL CHALLENGES IN THE FACE OF EMERGING TRENDS

Sovereignty as a concept is not static,[238] but has been evolving in response to socio-political as well as economic changes. As a concept of power allocation,[239] it has resulted in a fundamental shift of power from the realm of the state and a re-distribution of competences to regional and global institutions. The effect has been both a dimunition of sovereignty and a consolidation of it.[240] States increasingly lean towards international institutions such as monetary unions as a way to contain the challenges of a globalised market.

The EMU is a highly intergrated monetary system which has been formed in response to the creation of an open market within the European continent. The adoption of currency boards as well as dollarisations are some of the responses to the changing demands of the age.

[236] Raustiala K "Rethinking the Sovereignty Debate in International Economic Law" (2003) 6 (4) *Journal of International Economic Law* at 861.
[237] Petersmann E U *International Economic Law in the 21st Century: Constitutional Pluralism and Multilevel Governance of Interdependent Public Goods* 2012 at 162. See also Raustiala K *Id.* at 863.
[238] Lowe V "Sovereignty and International Law" in Shan W, Simmons P and Singh D (eds) *Redefining Sovereignty in International Economic Law* 2008 at 77.
[239] Jackson JH "International Law in Times that are Interesting (2000) *Journal of International Economic Law* 3-14 at 11.
[240] Raustiala K *supra* at 875 argues that international institutions "are paradoxically sovereignty enhancing."

The recession that began in 2007 saw an increased role of the G-20.[241] The G-20 made use of the "IMF as an outsourced secretariat, research department … and policy referee …"[242] and also practically outsourced the legitimacy of the IMF in the regulation of international monetary and financial matters. Since the IMF enjoys a near universal membership, a small group such as the G-20 can speak with a legitimate voice under the cover of the IMF. States displayed a high level of co-operation during the crisis on the realisation that the crisis threatened their own stability. The clandestine bailouts[243] carried out by the federal reserve bank on Eurozone institutions was clearly a sign that acting in isolation would pose a serious threat to the interests of the USA as well. Due to the globalisation of financial and other markets, a collapse of the Euro currency would have adversely impacted the trading partners of Europeans states, of which the USA is a major one.

The emergence of international institutions has seen a burgeoning of normative aspects of sovereignty to encompass human rights, a resurgence of popular sovereignty and a strengthening of democracy. [244] States have realised that some decisions are best taken at intergovernmental level so as to protect the broader economic interests. States sometimes conveniently delegate state power which they can still regain if they decide to withdraw from the institutions concerned.[245]

3.7. CONCLUSION

This chapter has explored the conceptual framework of monetary sovereignty and has contextualised it within the shifting perceptions and the emerging patterns of transnational interaction. The powers of the state to create money through deciding the name of the unit, the power to coin money and print notes, to set monetary standards and to declare legal tender, to determine exhange rates and to impose exchange controls are established competences of the state from which derogation cannot be easily entertained.

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[241] The G-20 is an organisation of twenty economically powerful states which grew spontaneously in response to the global crisis of 2007. The group played an important role of resolving the crisis. See Rickards J *Currency Wars: The making of the Next Global Crisis* 2011 at 125

[242] *Id* at 132.

[243] The Federal reserve system provided funds for the Too-Big-To-Fail institutions both domestically and abroad at a time when the Euro was severely strained by among other things the sovereign debt crisis. See Rickards J *supra.* at 114.

[244] Howse R "Sovereignty, Lost and Found" in Shan W, Simmons P and Singh D (eds) *Redefining Sovereignty in International Economic Law* 2008 at at 62

[245] Raustaila *supra* at 846 argues that sovereignty is not lost since states are still able to withdraw from international institutions and reclaim their powers.

Having noted that most of the legal cases supporting the dominant position of the state were were decided during the era of the gold and other commodity anchors,[246] it is worthwhile to ask whether adjudication of monetary disputes based on *fiat* standards should not adopt a different approach to those previously adopted. In light of the fact that 'money is not what money used to be', it is arguable that an international jurisprudence that departs from positivist 'listings' of state competences no longer serves the interests of commerce to a sufficient degree. The acknowledgement of the inadequacies of 'unqualified state monetary power' is the reason for the necessity of puting limits to the monetary sovereignty. The next chapter therefore discusses the juridical constraints that operate against monetary sovereignty.

[246] The Serbian Loans cases were decided in 1929 while the *Zuk Claim* Cases were decided in 1956.

CHAPTER 4

4. LEGAL CONSTRAINTS ON MONETARY SOVEREIGNTY

4.1. INTRODUCTION

The previous chapters of this study dealt with the nature and the scope of monetary sovereignty within the context of a globalised economic system. The incidences of sovereignty were considered within the context of traditional and unfettered dimensions of monetary sovereignty. It emerged from the discussion that states traditionally enjoyed little or no limitations to the exercise of their sovereign powers. Lately, however, the increasing propensity towards international trade, international investment and the growth of global financial markets has resulted in dramatic encroachments into the hitherto unlimited area of state monopoly. Such monopoly has demonstrably waned, leaving the state with modest remnants of monetary power as compared to the previous times.

This chapter looks at the juridical or legal constraints that have become part and parcel of international economic relations as well as their defining effects on the contours of monetary power. While it can be argued that most of the constraining factors are of a purely economic nature such as those which emanate from market dynamics or political considerations, there are others which are strictly of a legal nature. Non-legal or *de facto* constraints are mentioned in passing while the *de jure factors* form the heart of the discussion.

The chapter is divided into four sections. The first section is an exposition of the legal basis for the imposition of constraints on the exercise of state power. The second one reviews the customary public international law basis for the constraints while the third extensively discusses the role of treaties in constraining monetary sovereignty. Major multilateral treaties such as the IMF, the GATT and GATS and other organisations such as the OECD are reviewed in the context of their far reaching effects. BIT provisions also provide insightful guidelines on some of the approaches that have been adopted to control state discretion. The fourth section explores sovereignty saving devices that help to strike a balance between the need to limit the states' power and the countries' need for fall-back corrective measures in times of economic crisis.

4.2. LEGAL BASIS FOR CONSTRAINTS

In international law, there are primary as well as secondary rules. The primary rules are the ones that lay down "the content of obligations" and state the substantive rules to be invoked in solving a pertinent legal problem. Secondary rules on the other hand lay down "the

general conditions under international law for the State to be considered responsible for wrongful actions or omissions, and the legal consequences which flow therefrom."[247] Whereas primary rules pertinent to monetary law are specicific to the particular legal relationships and would apply narrowly within the monetary law sphere, secondary rules apply broadly as general principles applicable to international law problems in a general manner. Whether a state is liable for a breach of the international monetary law is a question than can be answered by looking at the content of the monetary law rules, which incidentally fall within the ambit of primary rules of monetary law.

It was unveiled in chapter 3 that the determination of the value of a currency, the imposition and maintenance of exchange controls among others are competences perculiarly within the province of the state. It was also revealed that there are certain exceptions and limitations that constrain monetary sovereignty. Literature on international monetary law recognises two sources of limitations on state power. The two are customary public international law as well as treaty law.[248] The remaining sections of the chapter discuss these limitations in their broader operational context beginning with customary law and then followed by treaty based exceptions.

4.3. CONTOURS OF CUSTOMARY LAW CONSTRAINTS

Customary public international law recognises several constraints that operate against monetary sovereignty. It recognises that a state has a duty not to abuse the rights of aliens through discrimination or otherwise. In the *Zuk Claim* case, the US Claims Commission acknowledged the aspect of monetary sovereignty and further said;

> "International law recognizes two exceptions to this general rule. The first exception is founded on the theory of a denial of justice. … The second may be found in a provision in a treaty or other international agreement."[249]

Denial of justice is undeniably a customary law principle which is largely applied in municipal law and its application is extended to international law on the basis that it forms part of "the general principles of law recognized by civilized nations."[250] An individual is deprived of justice when there is a deprivation of rights accompanied by denial of access to legal redress. If, for instance, a state deprives a foreign national of his rights through

[247] International Law Commission (2001) II (2) "Draft articles on Responsibility of States for Internationally Wrongful Acts with commentaries" *Yearbook of the International Law Commission* at 31.
[248] Mann F A *The Legal Aspect of Money* 1992 at 461.
[249] *Zuk Claim* United States Foreign Claims Settlement Commission *International Law Reports* Vol. 26 (1958) II at 285.
[250] Article 38 of The Statute of the International Court of Justice.

nationalisation, expropriation or other forms of deprivation, the act is not necessarily deemed a deprivation unless the aggrieved foreign national is also denied adequate compensation and access to national courts. The insistence by international jurisprudence on the need for the exhaustion of national remedies[251] shows that a finding of a denial of rights is not a matter that can be easily inferred.

When a country undertakes currency valuations, imposes and maintains exchange controls and restrictions, imposes quantitative restrictions, alters its monetary standards or abrogates gold and other value clauses, it acts within its sovereign powers and its actions need not be questioned. Mere massive devaluations of currency are not sufficient to establish state liability.[252] The measures, however, raise concern when their employment adversely affects the property interests of aliens particularly if such measures are discriminatory or in instances where the state fails to provide adequate compensation. Such failure amounts to an abuse of rights.[253] Such cases of unjustifiable taking of property belonging to aliens may result in state responsibility in international law. Owing to the negative effect that discrimination can have on the monetary interests of aliens, it is important to consider how it can be a basis of state liability.

4.3.1 DUTY OF NON-DISCRIMINATION IN TREATMENT OF ALIENS

Discrimination in international law is not wrongfull by itself. A mere finding that a state has acted in a discriminatory manner does not automatically give rise to state liability. As Shuster notes, "… the blanket proposition that a currency valuation, if it can be found to be discriminatory … will give rise to an international tort is incorrect."[254] What then is the basis of the action if discrimination is not a sufficient ground? An economic test is applied to determine when discrimination will be actionable.[255] Discrimination is not actionable as against a state if the measures are adopted for *bona fide* and necessary economic adjustment purposes. Suffice it to note, however, that discrimination based on race, religion or sex is always unjustifiable unless there are exceptional grounds to excuse it. The Nazi practice of compelling the Jewish people to leave Germany while at the same time imposing measures to prevent international transfers of money was clearly discriminatory[256] and such discrimination cannot be justified in international law.

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[251] *Certain Norwegian Loans, France v Norway, Judgment, Jurisdiction,* [1957] ICJ Rep 9, ICGJ 175 (ICJ 1957), 6th July 1957*, International Court of Justice [ICJ] Oxford Reports on International Law* paragraph 91(2).

[252] *Zuk Claim supra* at 284.

[253] Schreuer CH "Protection against Arbitrary or Discriminatory Measures" in Rogers CA Alford RP (ed) *The future of investment arbitration* 2009 183-198 at 186.

[254] Shuster MR *The Public International Law of Money* 1973 at 62.

[255] *Ibid.*

[256] Mann FA *supra* at 475.

If, however, one state, named A, enjoys a balance of trade surplus with state B and a trade deficit in relation to state C, state A may, as a corrective measure, impose exchange restrictions which discriminate against state C so as to stabilise its balance of payment account. The adoption of quantitative restrictions as a measure to reduce imports from state C has the effect of restricting monetary flows between the two states.[257] If capital controls were to be maintained as between states A and C, the effect would be a dsicrimination against residents of state C as compared to those of state B. The restriction of payments does not arbitrarily target residents of state C, but is only employed for adjustment purposes. Regulatory measures that discriminate between foreign and domestic persons whose situations are substantially simillar can and should give rise to an international tort.[258] Discriminatory conduct as between aliens of different nationalities is also compensable unless there are other circumstances such as a treaty obligation between the state accused of discrimination and the third state, in which case the Most Favoured Nation (MFN)[259] clauses become operational. In the *Tobacco Monopoly Bonds Case*, discrimination based on nationality was apparent and was the basis for the challenge. When the state of Portugal offered payment in Pound Sterling, a form of preferential payment made to British nationals, the US objected.[260]

The use of exchange restrictions may lead to an international tort if undertaken for sinister motives other than *bona fide* monetary regulation.[261] A state adopting such measures needs to carefully guard against injuring the interests of other states through any forms of untenable discrimination. International jurisprudence naturally prohibits arbitrariness[262] and abusive employment of discriminatory measures.

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[257] Tamirisa, NT. "Exchange and Capital Controls as Barriers to Trade." (1998) *IMF Working Paper Series* at 5. See de Vries MG *The International Monetary 1972-1978 Volume II: Narrative and Analysis* 1985 also at 958.

[258] Heiskanen V "The Contribution of the Iran-United States Claims Tribunal to the Development of the Doctrine of Indirect Expropriation" (2003) 5 *International Forum du droit international* at 178.

[259] Booysen H *Principles of International Trade as a Monistic System* 2003 at 225-226. The Most Favoured Nation (MFN) is "a treaty provision in terms of which one state undertakes an obligation towards another state to accord most favoured nation treatment in an agreed area. … a promise of non-discrimination against the commerce of the other contracting party."

[260] *Tobacco Monopoly Bonds in "*Papers Relating to the Foreign Relations of the United States (1926) Volume II *United States Government Printing Office Washington* at 880-881. Available http://digicoll.library.wisc.edu/cgi-bin/FRUS/FRUS-idx?type=article&did=FRUS.FRUS1926v02.i0002&id=FRUS.FRUS1926v02&isize=text&q1=italy (Accessed on 06 November 2014.)

[261] *In re Helbert Wagg & Co Ltd* England Chancery Division (1956) 2 *World Law Reports* at 183.

[262] Schreuer CH *supra* at 183.

4.3.2 ABUSE OF RIGHTS, INCURRING AN INTERNATIONAL TORT

A state abuses the rights of foreign nationals when it expropriates their property without giving them adequate compensation.[263] Compensation is adequate if it meets international standards of fair compensation which is "adequate, prompt and effective."[264] The application of the 'Minimum Standard of Treatment' (MST) is essential for the protection of the monetary rights of aliens. Various international agreements adopt it so as to guarantee investment protection against the effects of expropriation.[265] It sets "a baseline below which state conduct must not fall."[266]

The standard is "essentially similar to standards of justice and treatment accepted by civilised nations" and may even include a standard higher than the one that the state applies against its own nationals.[267] In its development, the MST was juxtaposed with the "Calvo doctrine," a doctrine which denies the granting of preferential treatment to foreigners as compared to nationals. The MST, instead, prefers an equal standard of protection for nationals and foreigners based on the sovereign equality of states and an premise that a state cannot interfer in the affairs of another. Another view is that the doctrine is a "rejection of superiority or imperial prerogatives of powerful states and their nationals."[268] Its operation in recent years has been neutralised by increased propensity towards greater levels of investment protection offered by BITs. Paradoxically, it has seen some resurgence in Latin America in recent years.[269] The interconnection between the MST and other customary law principles is aptly expressed by Francioni who says:

> "So, in its historical evolution, access to justice is inseparable from the ' minimum standard of treatment of aliens'. This is confirmed by the customary rule requiring prior exhaustion of local remedies as a precondition of diplomatic protection. This rule presupposes the international obligation of every state to ensure access to

[263] Newcombe A & Paradell L *Law and Practice of Investment Treaties: Standards of Treatment* 2009 at 377-8.

[264] Shuster MR *supra* at 59. Newcombe A & Paradell L *supra* at 18. The Hull Rule is applied in most international agreements as the basic standard of compensation in cases of expropriation. Payment must meet the "adequate, effective and prompt criterion."

[265] Kelsey J "The Conundrum of Shifting Orthodoxies: FTAs and Korea's Currency Controls" (2011) 14 (4) *Journal of International Economic Law* 845–868 at 865.

[266] Forcese C "The Capacity to Protect: Diplomatic Protection of Dual Nationals in the 'War on Terror'" (2006) 17 (2) *European Journal of International Law* 369–394 at 376.

[267] Newcombe A & Paradell L *supra* at 12.

[268] Shan W "Calvo Doctrine, State Sovereignty and the Changing Landscape of International Law" in Shan W, Simmons P and Singh D (eds) *Redefining Sovereignty in International Economic Law* 2008 at 248.

[269] Shan W *supra* at 283.

courts to aliens and to administer justice in accordance with minimum standards of fairness and due process."[270]

Francioni explains that 'access' to courts is a reference to the courts of the particular state concerned and not necessarily international tribunals. Whether the national standard of treatment offers adequate protection for aliens remains a grey area. It is certain, however, that international agreements have raised the bar, showing a preference for a minimum standard of treatment.

4.3.3 NATIONALISATION, CONFISCATION, EXPROPRIATION, COMPULSORY LIQUIDATION OF PROPETY OF ALIENS TO BE DONE WITHIN THE BOUNDS OF THE LAW

A taking over by a host state, of property belonging to aliens amounts to a compensable deprivation of property unless it can be justified on grounds of necessity.[271] Included under the rubric of takings are numerous forms such as expropriation, nationalisation or confiscation.[272] These measures have varying effects on the monetary interests of aliens. In this study, the term 'expropriation' is adopted to refer to various take-overs of the monetary assets belonging to aliens. The measures may take direct or indirect approaches. Direct expropriation occurs when the state or a third party mandated by it, compulsorily acquires property belonging to an alien. States usually confiscate private property while pursuing public purposes. Indirect expropriation, on the other hand, occurs in ways that are not overt hence such descriptions of the measures as 'creeping', 'constructive', or 'disguised'[273] expropriation.

It is unusual for states to openly expropriate property belonging to aliens. As a result, the most common forms of expropriation are indirect or disguised. Indirect expropriations, creeping nationalisation or disguised measures are difficult to prove because of their concealed nature. Whether a taking of property is compensable or not can raise questions of applicable standards of which two have attained dominance. The balancing of the two emergent standards namely, the "effects" doctrine and "police" powers doctrine[274] is set to bring about a balance between the diametrically opposing interests of the state and those of the alien investor. In terms of the "effects" doctrine, "if a governmental measure deprives the owner of control over his property or substantially affects its commercial value,

[270] Francioni F "Access to Justice, Denial of Justice and International Investment Law" (2009) 20 (3) *The European Journal of International Law* at 731.
[271] *CMS v. Argentine Republic* (ICSID Case No ARB/01/8) Annulment Proceedings (2008) at paragraph 146.
[272] Newcombe A & Paradell L *supra* at 324.
[273] *Ibid.*
[274] Heiskanen V *supra* at 177.

compensation is required ..."[275] This is the case even if the state claims to have adopted the said measure in order to carry out its police powers. The "police" powers doctrine on the other hand holds that if a regulatory measure is "taken for a legitimate public purpose and is not discriminatory, the measure … does not give rise to the right to compensation."[276]

The "sole effects doctrine" was applied by the Iran-US Claims Tribunal which held that:

> "… measures taken by a state can interfere with property rights to such an extent that these rights are rendered so useless that they must be deemed to have been expropriated, even though the state does not purport to have expropriated them and the legal title to the property formally remains with the original owner. [277]

Customary international law principles hold that expropriations must be carried out for a public purpose, must follow the due process of the law, must be non-discriminatory and accompanied by adequate compensation.[278] The principles bolster the argument that expropriatory government measures must at least be subject to some form of control.

4.3.4 EFFECTS OF CONTRACTS ON MONETARY SOVEREIGNTY

A question may be asked whether a contract concluded between a state and a private party has an effect of limiting monetary sovereignty. If a state, *ex post facto* changes its monetary law, invokes its sovereignty and invalidates the contract lawfully concluded to the detriment of the other contracting party, a question arises whether such exercise of power is legitimate. Unilaterally changing the contract runs against the principle that:

> "a state cannot invoke its sovereignty to disregard commitments freely undertaken through the exercise of the same sovereignty and cannot, through measures belonging to to its internal order, make null and void the rights of the contracting party"[279].

There is a convincing counter-proposition that sovereignty cannot be signed away in terms of a contract.[280] The state retains sovereignty even under such circumstances but can be held to account on the basis of *pacta sunt servanda.* The principles applicable in terms of the law

[275] *Ibid.*
[276] *Ibid.*
[277] *Starret Housing Corporation v. Iran* Iran-US Claims Tribunal (16) Iran-US Claims Tribunal Reports 122, 154 (19 December 1983)
[278] Newcombe A & Paradell L *supra* at 321.
[279] *Texaco Overseas Petroleum Company v. The Government of the Lybian Arab Republic* (1978) (17) *International Law Material* 1 at 24.
[280] In *Certain Norwegian Loans Case v. France v Norway,Judgment, Jurisdiction, [1957] ICJ Rep 9, ICGJ 175 (ICJ 1957), 6th July 1957, International Court of Justice [ICJ]* at paragraph 53.

of contract bind the state to the terms of the contract but its sovereignty remains untouched. However, since a foreign individual does not have international legal personality, every contract between a state and the individual is subject to the law of the contracting state.[281] The conclusion of a contract does not negate the operation of sovereignty. As an example, a contract to purchase sovereign bonds is governed by the law of the issuing state. In the *Certain Norwegian Loans* case, the governement of France argued:

> "That undertakings as to the amount of the debts contracted under the said loans by the Norwegian State with French nationals, containing express conditions as to performance, cannot be unilaterally modified by that State without negotiation with the holders."[282]

Having initially undertaken to discharge the obligation in terms of "gold value of the coupons", the Kingdom of Norway's unilateral variation of contractual terms was being seriously questioned by the French. The argument advanced by the French government is unconvincing, much as it questioned the exercise of sovereign power by the Kingdom of Norway. The Kingdom of Norway rightly argued that the matter was not an international legal dispute but was exclusively within its national jurisdiction. This alteration of terms was certainly a breach of contract and the application of *pacta sunt servanda* would have been more appropriate under the circumstances.

4.4. LEGAL CONSTRAINTS UNDER SPECIFIC LEGAL REGIMES

The impact of treaty regimes on sovereignty since the end of the Second World War, has been exceedingly great. Treaties have imposed numerous limitations on state power and have drastically constrained monetary sovereignty. A treaty by treaty analysis of provisions follows below. It is very important however to sound an alarm of caution that rules of monetary conduct emanating from treaties do not "express universally binding duties" but are only binding to the contracting parties.[283]

4.4.1 IMF ARTICLES AND THEIR CONSTRAINING EFFECT ON SOVEREIGNTY

The International Monetary Fund is by far the the most globally representative institution as regards monetary regulation. Its membership consists of 188 states which gives its regulatory role a great deal of influence. Its legal provisions seriously encroach into the

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[281] Shuster MR *supra* at 71. Booyesen H *Principles of International Law as a Monistic System* 2003 at 338.
[282] *Certain Norwegian Loans, France v Norway* [1957] ICJ Rep 9, ICGJ 175 (ICJ 1957), 6th July 1957, International Court of Justice [ICJ] *Oxford Reports on International law* at paragraph 11.
[283] Mann FA *Legal Aspect of Money* 5th Edition 1992 at 510.

sovereignty of the states. The IMF provisions which have a great bearing on sovereignty are Articles IV, VI, VII, VIII, XIV and the definitions in Article XXX(d). The scopes and applications of these provisions are discussed below. This study evaluates the validity of an argument that the operation of the Articles of Agreement of the IMF causes little curtailment to sovereignty.[284] Article IV plays a very central role in monetary relations. It is a general undertaking by the members to co-operate in bringing about "a stable system of exchange rates."[285] The current version of Article IV, which came into effect in 1978 following the second ammendment of the Articles of the Agreement, spells out the "obligations regarding exchange arrangements."[286] Unlike its predecessor, it is based on 'discretionary judgment' of the IMF instead of 'rules'.[287] The *par value* system set rigid rules which made the adjustment of the monetary system very difficult.[288] An 'undertaking to collaborate,' or an 'endeavour to direct' economic policies is certainly not a way to spell out rigidly enforceable obligations. Terms that vaguely state the obligations largely leave the "sovereignty and discretion of member states almost completely intact."[289] Consultations in terms of Article IV(1)(iii) aim to avoid the manipulation of exchange rates while the allegations of exchange rate manipulations would only flow from a violation of this Article.[290] 'Soft obligations' are placed side by side with 'forceful obligations' in what Lastra labels a "hesitant tone."[291] The former are stated in relatively apologetic words while the latter express absolute imperatives couched in uncompromising parlance.

Article IV consultations provide vital information for the IMF to formulate policy transformations and in cases of violations of members' obligations, the IMF may impose sanctions in terms of Article XXVI(2). The "elimination of exchange restrictions" is clearly an important goal of the IMF.[292] Members determine exchange arrangements in terms of Article IV(2)(b) which leaves members the discretion to apply … (iii) "other exchange arrangements of a member's choice." However, the freedom of a member to alter its exchange rate regime is subject to the requirement for a prompt notification to the fund. The Article forms the basis for surveillance over the exchange rates and when read in conjunction with Article XXVI(2), it imposes a manifest constraint on sovereignty. The application of the conditionality principle, however, does not cause a dimunition of sovereignty because it is not a mandatory

[284] Mann F A *supra* at 514.
[285] Article IV:1 of the IMF.
[286] The title of Article IV of the IMF.
[287] Lastra RM *Legal foundations of International Monetary Stability* 2006 at 400.
[288] *Ibid.*
[289] Mann FA *supra* at 513.
[290] Article IV:1 (iii) of the IMF. The IMF conducts periodic surveillance checks on members and also gives technical support to states.
[291] Lastra RM *supra* at 403.
[292] Viterbo A *International Economic Law And Monetary Measures Limitations to States' Sovereignty and Dispute Settlement* 2012 at 159.

provision. Instead, it only operates against a member that seeks to borrow from the fund.[293] Lastra defines conditionality as "the policies and procedures developed by the fund to govern the access to and use of its resources by member countries."[294]

Monetary sovereignty endures some serious curtailment from the operation of the Agreement of IMF.[295] It imposes substantial fetters on a state's policy space by stating that:

> "Subject to the provisions of Article VII, Section 3(b) and Article XIV, Section 2, no member shall, without the approval of the Fund, impose restrictions on the making of payments and transfers for current international transactions."[296]

Fund approval is a pre-requisite for the imposition of restrictions on current payments and transfers. Under certain circumstances, however, the Fund may permit the imposition of restrictions. Current transactions are payments for goods and services rendered while capital transactions are concerned with transfers for investments whether on a short or long term basis.[297] A current transaction is defined in Article XXX(d) of the agreement of the IMF as a transaction which is "not for the purpose of transfering capital." It gives a list of transactions including payments in connection with foreign trade. Examples are payments for goods or services purchased or services rendered. Inflows and outflows carried out for the purposes of investment are classified as capital transactions but the list includes transactions which economic theory sometimes classifies as capital transactions.[298] These are "payments due as interest on loans and as net income from other investments," and "payments of moderate amount for amortization of loans or for depreciation of direct investments." Proceeds from partial or full liquidation of an investment are also included in the definition. The limitation on state power to restrict such payments is clearly demarcated.

The provision encumbers sovereignty to a great extent much as the choices of the state are made to depend on the approval of an international organisation. The burden is, however, only imposed as regards current transactions for which there is a greater level of protection than there is for capital ones. The power of the state to deal with capital transactions and to even impose controls enjoys a great measure of latitude. Members of the IMF are still permitted to maintain capital controls in terms of Article VI(3) of the IMF.

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[293] Conditionality is a weak instrument to enforce compliance, lacks coercive influence over stable self-sufficient economies.
[294] Lastra RM *supra* at 412.
[295] Hagan S "Enhancing the IMF's Regulatory Authority" (2010) (13) (3) *Journal of International Economic Law* 955–968 at 957.
[296] Article VIII:2(a) of the IMF.
[297] Article XXX(d) of the IMF.
[298] Lastra RM *supra* at 394.

It is moreover noteworthy that exchange controls are different from restrictions.[299] Controls are less burdensome measures than restrictions. The former are governmental regulatory processes that merely inconvenience international payments and transfers through delays and other forms of nuisance. However, they do not totally prevent the payments. They may include administrative processes designed to obtain information or to ensure compliance with application procedures to obtain a foreign exchange licence. Shuster explains that controls do not prevent the payment[300] as such. The term 'exchange controls' is a much broader concept than 'exchange restriction'. It is broadly inclusive of "any governmental action, whether of a formal or informal nature, that impedes the making of current international payments and transfers".[301] The measure is a restriction if while permitting transfers and payments nevertheless "increases their cost or subjects them to an unreasonable burden or delay'.[302] Having noted these perceptions of the terms, it is significant to contextualise the terms by admitting, as Gari does that:

> "…the terms 'capital control' are not a legal term of art. The legal meaning of terms related to the concept of capital control can only be established in light of their context and the object and purpose of the agreement that contains them."[303]

A member state wishing to restrict current transactions must obtain IMF approval before doing so. But precisely under what circumstances such approval will be granted to permit a state to impose restrictions on payments under Article VIII(2)(a) is far from clear. An IMF Decision summarises the circumstances as follows;

> " … the Fund will grant approval only where it is satisfied that the measures are necessary and that their use will be temporary while the member is seeking to eliminate the need for them. … the use of exchange systems for nonbalance of payments reasons should be avoided to the greatest possible extent, …"[304]

The circumstances of the state must be such that it is absolutely necessary to temporarily impose the restrictive measures. There must be evidence that the state is seeking alternative and more sustainable ways to deal with the problem at hand. As Gold

[299] Hagan S *supra* at 957.
[300] Shuster MR *supra* at 32.
[301] UNCTAD *Transfer of Funds* UNCTAD/ITE/IIT/20 (UN New York and Geneva 2000) at 14.
[302] *Ibid.*
[303] Gari G "GATS Disciplines on Capital Transfers and Short-term Capital Inflows: Time for Change?" (2014) 17 *Journal of International Economic Law* 399–435 at 404.
[304] Decision 1034 –(6027) in Selected Decisions *and Selected Documents of the International Monetary Fund Thirty-Fourth Issue, Washington DC December 31,* 2009 Paragraph 1 at 518.

convincingly affirms, “The IMF's practice is to grant approval, when justifiable, for a limited period only because the restrictions are derogations.”[305]

There are instances where a state may choose to apply trade measures in order to deal with an exchange crisis. This becomes possible because the effects of exchange and trade measures on the balance of payment position of a state are similar.[306] Trade measures can also be applied to adjust balance of payment accounts with the same effects. Drawing a distinction between an exchange and a trade measure is, however, a daunting task.[307] An IMF determination is that, “The guiding principle in ascertaining whether a measure is a restriction on payments and transfers for current transactions under Article VIII(2), is whether it involves a direct governmental limitation on the availability or use of exchange as such.”[308] If it does not involve foreign exchange, it may be a trade restriction instead of an exchange restriction. A distinguishing feature of a trade action is that it involves the underlying transaction such as the maximum quantity of a particular class of goods that can be imported or exported by a country.

It is possible for states to circumvent the Articles of Agreement of the IMF through the use of trade measures such as quantitative restrictions and still not be in contravention of the IMF Articles of Agreement.[309] The IMF legal regime therefore works in collaboration with the GATT so as to effectively[310] fulfill its mandate. Quantitative restrictions fall under the jurisdiction of the GATT and the implications of their adoption are discussed below.

In the context of this study, Article VIII(2)(b) of the IMF receives a cursory reference as it is a private international law or conflict of laws rule[311] which shields exchange control regulations of a member from being rendered inoperative in territories of other members. For the regulations to receive protection, their maintenance must be consistent with the IMF Agreement. It reads as follows:

> “Exchange contracts which involve the currency of any member and which are contrary to the exchange control regulations of that member maintained or imposed

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[305] Gold J “Exchange Contracts and the IMF”, Exchange Control, and the IMF Articles of Agreement: Some Animadversions on *Wilson, Smithett, & Cope Ltd. v Terruzzi* (1984) 33 (4) *International and Comparative Law Quarterly* 777-810 at 779.
[306] Tamirisa NT "Exchange and Capital Controls as Barriers to Trade." (1998) *IMF Working Paper Series* at 5-6.
[307] Shuster MR *supra* at 28.
[308] IMF Decision 1034 –(6027) *supra* at 518.
[309] Seigel DE “Legal Aspects of IMF / WTO Relationship: The Fund’s Articles of Agreement and the WTO Agreements” (2002) 96 *The American Journal of International Law* at 566.
[310] Shuster MR *supra* at 112.
[311] Lastra RM *supra* at 394. Mann FA *supra* at 366.

consistently with this Agreement shall be unenforceable in the territories of any member."[312]

As far as Article VIII(2)(b) is concerned, an IMF Decision says, "By accepting the Fund Agreement, members have undertaken to make the principle mentioned above effectively part of their national law."[313] It places a negative obligation on member states to give effect in their territories to fellow members' exchange control regulations.[314] It protects the sovereign power of a state with regards to adoption of regulations while securing the power of the state to exercise discretion within its territory.

On the other hand, Article VIII(3) of the IMF greatly constrains sovereignty as it categorically prohibits the adoption of discriminatory and multiple currency practices. A multiple currency practice exists when official action causes exchange or cross rate spreads to differ by more than 2 percent between buying and selling rates for spot exchange transactions between a member's currency and currency of any other member.[315] Such a practice discriminates between transactions and distorts trade to the extent that certain transactions are placed at an exchange advantage as compared to others. The prohibition narrows the margin of manoeuvre and levels the field for all transactions.

Sovereignty has been significantly constrained by the IMF law. A determination regarding the legal obligations of a state now has to take into account the implications of the IMF law on the state concerned. The connection between the IMF and the WTO regime is another critical area of great interest and the matter is discussed in the next section.

4.4.2 RECOURSE TO THE WTO REGULATORY TOOLKIT TO NEUTRALISE UNORTHODOX USE OF TRADE MEASURES

The World Trade Organisation (WTO), consisting of a number of agreements such as the General Agreement on Tariffs and Trade (GATT) the General Agreement of Trade in Services (GATS), Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), is a highly influential monetary legal regime.

As discussed above, the IMF mostly regulates exchange measures but restricts the abuse of trade measures by states. Abuse occurs when states employ measures that affect

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[312] Article VIII:2b of the IMF.

[313] IMF Decision No. 446, June 10, 1949 in Selected Decisions *and Selected Documents of the International Monetary Fund Thirty-Fourth Issue, Washington DC December 31,* 2009 paragraph 2 at 510.

[314] Gold J *supra* at 782. Lichtenstein CC *supra* at 67.

[315] IMF Decision No. 6790-(81/43) March 20 1981, ammended by Decision 11728-(98/56).

underlying transactions as a way to adjust balance of payment positions.[316] States often devise numerous measures to disguise exchange restrictions. Import surcharges,[317] retention quotas, advance deposits, taxations on the purchases of foreign currency tend to frustrate trade liberalisation.[318] States exploit the Fund's lack of direct influence on trade measures and maintain quantitative or financial barriers in a manner that frustrates efforts to attain the goals of trade liberalisation. Tariffs, export duties, taxes on transfers, export or import quotas[319] can be employed in a way that violates states' international obligations. The role of Article XV of the GATT as a bridge between the GATT and the IMF legal regimes,[320] is relevant in ensuring that trade measures do not frustrate the goals of exchange convertibility.[321] It pre-empts a circumvention of Article VIII:2a of the IMF by stating that:

> "Contracting parties shall not, by exchange action, frustrate the intent of the provisions of this Agreement, nor, by trade action, the intent of the provisions of the Articles of Agreement of the International Monetary Fund."[322]

Article XVIII(2) of the GATT expressly permits states to "to apply quantitative restrictions for balance of payments purposes" while carrying out programes and policies of economic development.[323] In the *India-Quantitative Restrictions on Imports of Agricultural, Textile and Industrial Products*[324] case, the state of India adopted quantitative restrictions for balance of payment purposes and came under US challenge for the decision. According to the determination by the WTO panel, the restrictions were inconsistent with Articles XV(1) and XVIII(11). The consultative relationship between the IMF and the GATT operates with the effect of avoiding abuse of exchange and trade measures. The two legal regimes act in a complementary relationship to prevent evasion of obligations in either regime. Together they constrain monetary sovereignty in a substantial manner.

Yet, as compared to the IMF, the GATS system goes a step further in liberalising capital movements. The GATS aims mainly to liberalise trade in services and lays the ground rules

[316] UNCTAD *supra* at 23.
[317] GATT L / 5162, Italy- Deposit requirements for purchases of foreign currency (memo to GATT).
[318] Viterbo A *supra* at 161.
[319] Viterbo A *supra* at 161.
[320] Thorstensen V, Ramos D and Muller C "The 'Missing Link' Between the WTO and the IMF" 2013 16(2) *Journal of International Economic Law* 353–381 at 353.
[321] Seigel DE *supra* at 568.
[322] Article XV:4 of GATT 1994.
[323] *India-Quantitative Restrictions on Imports of Agricultural, Textile and Industrial Products WT/DS90/AB/R.*
[324] *Id.* at 37.

for market access that one state grants to the others.[325] Each state undertakes commitments based on a specific schedule in terms of which it spells out market access modes for the service sectors it liberalises. Depending on the mode of supply[326] chosen, the state undertakes capital account liberalisation commensurate with the mode of market access selected for the particular service. Since commitments are based on individual state negotiations,[327] the obligations of the state towards others also vary from state to state. There are basically four modes of supply to choose from, namely cross-border supply of services, consumption abroad, foreign commercial presence and lastly, movement of natural persons[328] The Articles of the GATS clearly spell out that:

> "each Member shall accord services and service suppliers of any other Member treatment no less favourable than that provided for under the terms, limitations and conditions agreed and specified in its Schedule."[329]

In terms of footnote 8 of the Articles, a state granting market access in terms of mode 1 must liberalise capital flows 'essential' for the supply of the service. With regards to mode 3, the state must liberalise all 'related' capital flows. The nature of the service as well as the chosen mode of supply therefore determine the extent of capital movement liberalisation. It is significant therefore at this point to accentuate that the GATS commitments, once undertaken, do constrain sovereignty in a substantial way.

The power to apply restrictions on international transfers is limited by Article XI(1) of the GATS which states that a "member shall not apply restrictions on international transfers and payments for current transactions relating to its specific commitments" and that a "member shall not impose restrictions on any capital transactions inconsisently with its specific commitments regarding such transactions, except under Article XII …"[330] Reference to 'schedules of specific commitments' shows the importance of negotiations and commitments[331] in demarcating the boundaries of capital account liberalisation. In the case

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[325] Articles XI and XVI of the GATS deal with transfers of payments as well as market access. Once a state commits itself to provide market access, it should also permit all transfers necessary for the enjoyment of that access.
[326] Zimmermann CD "The Promotion of Transfer-of-funds liberalization across International Economic Law." (2010) *The Society of International Economic Law Working Paper No. 2010/32* at 18-19. See also Gari G "GATS Disciplines on Capital Transfers and Short-term Capital Inflows: Time for Change?" (2014) 17 *Journal of International Economic Law* 399–435 at 412.
[327] UNCTAD *supra* at 25.
[328] Article I a-b of GATS.
[329] Article XVI of GATS.
[330] Article XI:2 of GATS.
[331] *United States -Measures Affecting the cross-border supply of Gambling and Betting Services* WT/DS285/R 10 November 2004 at 16.

of *United States-Measures Affecting the cross-border supply of Gambling and Betting Services,* the panel said:

> "Indeed, the value of specific commitments on market access and national treatment would be seriuosly impaired if Members could restrict international transfers and payment for service transactions in scheduled sectors."[332]

It is apparent, therefore, that numerous provisions within the WTO regime significantly constrain the monetary power of contracting state parties. Provisions within the GATT legal regime such as Article XV are instrumental in regulating the use of trade measures as well as in providing the essential bridge between the WTO and the IMF.[333] Articles XI, XII, and XVI of GATS, read in conjunction with Article I, help delimit the extent of capital account liberalisation for each member.

4.4.3 ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

The Organisation for Economic Co-operation and Development (OECD) is an international organisation consisting of mostly high-income countries.[334] It has two codes of liberalisation namely the Code of Liberalisation of Capital Movements (Capital Code) and the Code of Liberalisation of Current Invisible Operations (Current Code).[335] The OECD Capital Code gives an item by item list[336] of the covered transactions.

Its Article I(a) states that "Members shall progresively abolish between one another … restrictions on movements of capital to the extent necessary for effective economic co-opration." Clearly this liberalisation of capital movements is more progressive than that accorded by Article VI(3) of the IMF. The Capital Code removes obstacles impeding capital movements so as to ensure efficient co-operation.[337] Proceeds from investments or those from a full or partial liquidation of a business are liberalised in a broader way than the IMF system does. As a result, the constraint upon monetary sovereignty, particularly with regards to capital movements is relatively more drastic than that exercised by the IMF.

The OECD does not enjoy the same universality of membership as the IMF, but attains great influence by extending the benefits of its liberalisation to IMF members. Arguably,

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[332] *Id* at 233.
[333] Seigel DE *supra* at 562. Refer to Thorstensen V, Ramos D and Muller C "The 'Missing link' Between the WTO and the IMF" 2013 16 (2) *Journal of International Economic Law* 353–381 at 360.
[334] Refer to OECD website: Members and partners http://www.oecd.org/about/membersandpartners/#d.en.194378 (Accessed on 17 January 2015).
[335] UNCTAD *supra* at 18.
[336] Annexure A, OECD capital Code.
[337] Shuster MR *supra* at 255.

> "the two OECD codes on capital liberalization have also played a major role in promoting international capital movements to an extent that goes well beyond what would be required under the Fund's Articles."[338]

The Codes, however, provide very significant sovereignty saving measures through the employment of derogation clauses. In each code, Article 7 provides for derogation from obligations in the event of an economic and financial situation that justifies such a course,[339] or if the measures adopted in terms of the code lead to a serious economic and financial disturbance,[340] or to correct an unfavourable balance of payment position.[341] Other important saving provisions are Article 2b, dealing with reservations and Article 3, dealing with public order and security considerations.

4.4.4 BILATERAL INVESTMENT TREATIES

The period since the 1950s has seen a proliferation of Bilateral Investment Treaties (BITs)[342] sometimes called International Investment Agreements (IIA). They aim at the protection of foreign investments and usually have clauses which prohibit any forms of arbitrary discrimination based on subjective factors such as nationality. States pledge adequate investor compensation in the event of expropriation while also offering "guarantees on the transfer of capital and investment returns …"[343] The guarantees are based on a "broad principle of customary law and equity that a Governement which has approved the importation of capital is bound to approve its re-exportation."[344] The treaties usually define the transactions that qualify for their regulatory protection.

The treaties also provide for grievance procedures such as arbitration before a neutral tribunal[345] in the event of a dispute between the state and the foreign investor. They augment investor protection in the face of inadequate provision for funds transfer under the IMF system.[346] Although some remittances of investment related capital are done in terms of Article XXX(d) of the IMF, read in conjunction with VIII(2)(a), proceeds from a full or partial

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338 Zimmermann CD "The promotion of transfer-of-funds liberalization across International economic Law" (2010) *Second Biennial Conference of the Society of International Economic Law (SIEL)* at 1.
339 OECD Capital Code Article 7a.
340 OECD Capital Code Article 7b.
341 OECD Capital Code Article 7c.
342 Newcombe A & Paradell L *Law and Practice of Investment Treaties: Standards of Treatment* 2009 footnote 241 at 42. The first treaty was signed on 25 November 1959 between the Republic of Germany and Pakistan and provided comprehensive protection to foreign investment.
343 Newcombe A and Paradell L *supra* at 42.
344 Mann FA *supra* at 529.
345 Karl J "International Investment Arbitration: A threat to State Sovereignty?" in Shan W, Simmons P and Singh D (eds) *Redefining Sovereignty in International Economic Law* 2008 at 232.
346 Zimmermann CD *supra* at 13.

liquidation of an investment do not enjoy the same degree of protection.[347] This is hardly surprising since investment protection is not an expressely stated purpose of the IMF. BITs, therefore, have a significant impact on sovereignty because their clauses severely curtail the state's monetary power. As Mann states, they "are far less modest than the Articles of Agreement of the International Monetary Fund"[348] in constraining monetary sovereignty. Most of them impose a duty to transfer capital across jurisdictions while firmly prohibiting the use of exchange restrictions. Article VI(3) of the IMF, which permits the use of capital controls and restrictions has in the face of these provisions become "hollow"[349] and of little operative consequence.

Capital repatriation is secured through clauses that guarantee currency convertibility, spell out methods of determining the exchange rate as well as stimulate a prompt transfer of capital.[350] They spell out how payments should be made in a freely 'convertible currency,'[351] or the currency in which the investment was initially made. Some recommend payments in a freely usable currency or any other currency that parties agree to.[352] Clauses that allow for payment in the original currency of investment are clearly less restrictive to state power than the others. According to the Netherlands-United Arab Emirates treaty, "The transfers shall be made in freely convertible currency, without restriction or delay."[353] It liberalises the payment of profits, interests, dividends and current income, funds necessary for acquisition of raw materials, replacement of capital assets or to safeguard the continuity or development of investment, funds for loan repayments, royalties, fees earnings of natural persons and proceeds of sale and liquidation of investment. Its constraining effect on sovereignty is clearly more than that of the IMF Articles as it ensures a greater degree of liberalisation of capital inflows and outflows of capital.

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[347] Article XXX(d) of the IMF. Zimmernann C D *supra* at 12 notes that "free outward transfer of income derived from an international investment" is covered by the Articles of the IMF.
[348] Mann FA *supra* at 527.
[349] Zimmermann CD *supra* at 12.
[350] UK-Chile Agreement of 1997 Article 6 reads: "Each Contracting Party shall … guarantee … free transfer of their investment and returns. Transfers shall be effected without delay in the convertible currency in which capital was originally invested or in any other convertible currency agreed by the investor and the Contracting Party concerned. … at the rate of exchange applicable on the date of transfer …"
[351] Article XXX(f) of the IMF. Article 8.1 of the 2000, Mauritius-Singapore Treaty refers to freely convertible currencies. See also Article 5:1 of the Agreement on Encouragement and Reciprocal Protection of Investment between the Kingdom of the Netherlands and the United Arab Emirates, 26 November 2013.
[352] Zimmermann CD *supra* at 16.
[353] Article 5 (1) of the Agreement on Encouragement and Reciprocal Protection of Investment between the Kingdom of the Netherlands and the United Arab Emirates.

The choice of currency and the method to determine the applicable exchange rate are among the most critical concerns to an investor.[354] The UK-Chile Agreement provides that "transfers shall be made at the rate of exchange applicable on the date of transfer …"[355] Some treaties prefer the application of a "prevailing market rate."[356] The clauses are formulated in such a way as to avert the manipulation of exchange rates. Phrases such as "without delay" appear very frequently in BITs in relation to the 'time of transfer' clause. Some BITs employ terms that restrict repatratriation of proceeds before the lapsing of certain time periods such as one year. Of such terms, Gari says;

> "Unremunerated Reserve Requirement (URR) is a requirement applicable to non-residents consisting of a mandatory deposit of a percentage of their investment in a Central Bank account, not remunerated and for a minimum period of time."[357]

Without doubt, such clauses unduly restrict repatriation of capital.

In light of the above exposition, it is a conceivable deduction that BITs have advanced ahead of other regulatory regimes in curtailing monetary sovereignty. States which commit themselves to BITs clearly limit their sovereignty as far as covered investments are concerned.

Regional economic groupings or blocs also play a considerably important role with respect to international monetary regulation. One oustanding example is the European Union which performs a highly important regulatory function within the subcontinent of Europe. Regional economic groups complement the works of the multilateral systems through the creation of monetary unions and common currency areas. Monetary unions and currency areas[358] promote co-operation at regional levels even though their members still retain obedience to the global regulatory bodies.

4.5. SOVEREIGNTY SAVING PROVISIONS UNDER VARIOUS REGIMES

Even though bilateral and multilateral agreements have made gross and far reaching encroachments on national sovereignty, the state still enjoys a great measure of latitude within which to regulate its own affairs. State sovereignty has been saved by some conservative treaty provisions and other innovations. Among such provisions are transitional

[354] UNCTAD *supra* at 6.
[355] UK-Chile Agreement of 1997, Article 6.
[356] Mauritius – Singapore Treaty of 2000, Article 9 on exchange rates.
[357] Gari G *supra at* 408.
[358] The Common Monetary Area (CMA) linking Southern Africa, Lesotho and Swaziland.

arrangements,[359] reservations,[360] derogations, prudential carve-out clauses[361] as well as balance of payment derogations.[362]

In terms of Article VI(1) of the IMF, “the Fund may request a member to exercise capital controls in order to prevent”[363] any abuse of the Fund’s resources. This article particularly applies to those states that borrow or receive financial resources from the IMF. The IMF further authorises states to “exercise such controls as are necessary to regulate international capital movements,”[364] provided the controls do not “restrict payments for current transactions.”[365] In cases where a state experiences a sustained outflow of resources, restrictions may be approved.[366] Capital controls play a particularly important role in preventing volatile capital flows, seen as “the principal conduit for the transmission of global shocks.”[367] In light of the fact that the state may, on the approval of the Fund, impose exchange restrictions,[368] and also maintain limitations on foreign exchange especially as a response to a problem of currency scarcity,[369] it is a reasonable deduction that states still do enjoy a substantial measure of sovereignty.

One part of the IMF law that poses a severe challenge to the efforts to liberalise the global monetary system is Article VI(3). It permits members to “exercise such controls as are necessary to regulate international capital movements,” without unduly restricting payments for current transactions. States are thus practically free to adopt controls and restrictions on capital flows provided they do not cause any delays in transfers of funds to settle their commitments.[370] Article XIV(2), a transitional provision, permits the maintenance of exchange controls and restrictions by those states which still avail themselves to its protection. The restrictions already in operation at the date of attaining membership are maintained and gradually phased out once their necesity falls away.[371]

As Viterbo explains, the regulation of current and capital transactions by the IMF is asymmetric in nature.[372] While IMF approval is mandatory before the imposition of

[359] Article XIV:2 of the IMF.
[360] Article X of OECD Capital Code.
[361] Article 2 of the GATS Annex on Financial Services.
[362] Article XI of GATS.
[363] Article VI:1 of the IMF.
[364] Article VI:3 of the IMF.
[365] Article VI:3 of the IMF.
[366] Gari G *supra* at 419.
[367] Gari G *supra* at 420.
[368] Article VIII:2 of the IMF.
[369] Article VII:3b of the IMF.
[370] Article VI:3 of the IMF.
[371] Article XIV:2 of the IMF articles of agreement.
[372] Viterbo A *supra* at 151.

restrictions to current transactions, none is required for a restriction of capital transactions.[373] It has been argued that the IMF legal regime regulates the current account while the capital account lies outside its jurisdiction.[374] The asymmetry results from states' right to impose capital controls in terms of Article VI of the IMF.[375] The regulation of capital controls lies within the competent powers of the state. Cohen aptly highlights the fact that "there is nothing to prevent a sovereign government from limiting capital flows if it so chooses …"[376]

The revision of the IMF's Articles through the adoption of the second amendment did not extend the IMF regulatory jurisdiction over movements of capital.[377] It has been asked whether the inclusion of words "exchange of goods, services and *capital* among countries" in the preamble of the ammended Article IV of the IMF extended the organisation's jurisdiction over the capital account.[378] It is a cogent inference that the recent proposal to further ammend the articles[379] was meant to bring capital account liberalisation within the IMF jurisdiction, a sign that the IMF itself was not satisfied with the extent of its jurisdiction as regards capital controls.

The debate on the supposed benefits of capital account liberalisation rages on among academics. Stiglitz, among others, argues that liberalisation will not benefit national and global systems. He argues that there is no evidence that capital-market liberalisation would be good for countries on which it is imposed?"[380] Following the East-Asia financial crisis of the late 1990s and Malaysia's successful adoption of capital controls to curb capital flight, conventional thinking shifted away from outright fascination with financial liberalisation on the grounds that unlimited liberalisation may lead to systemic risk.[381] At the formation of the IMF in 1945, Keynes, a leading economic theorist of the time showed much revulsion for free capital movements, expressing concern that uncontrollably volatile cross-border surges of 'speculative capital', 'refuge capital' as well as 'hot moneys' would be disruptive to national economies.[382]

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[373] Elizalde H "The International Monetary Fund and Current Account Convertibility" in IMF, *Current Developments in Monetary and Financial Law,* Vol. 4 (2006) 17-53 at 19.
[374] Lichtenstein CC "International Jurisdiction Over International Capital Flows and the Role of the IMF: Plus Ca Change …" in Giovanoli M (ed) *International Monetary Law: Issues for the New Millenium* 2000 at 66. Article XXX(d) of IMF.
[375] Viterbo A *supra* at 161.
[376] Cohen BJ *Global Monetary Governance* 2008 at 199.
[377] Gold J *supra* at 778-9.
[378] Lichtenestein CC *supra* at 71-72.
[379] The proposal was made in 1997 though it lost momentum following the seeming weaknesses of the argument in favour of capital liberalisation.
[380] Stiglitz JE "Capital-Market Liberalisation, Globalisation, and the IMF" (2004) Vol 20 (1) *Oxford Review of Economic Policy* at 58.
[381] Cohen BJ *supra* at 177.
[382] Cohen BJ *supra* at 178. Lichtenstein CC *supra* at 62.

Attitudes, however shifted as more and more theorists began to place emphasis on 'financialisation'[383] of national economies. At the beginning the 1980s, many advocated for capital account liberalisation but the recent crises of 1997 in East-Asia and the post-2007 global contraction sounded warning sirens that liberalisation may not be an excellent idea afterall. In an article with a seemly title, Kelsey speaks of "the conundrum of shifting orthodoxies" in reference to how states have been straddling between two opposing views regarding capital account regulation.[384]

At the centre of the debate is a towering imperative to develop a multilateral legal framework dedicated to capital account regulation so as to achieve greater global instability.[385] Even though a drive emerged in 1997 towards the ammendment of the Articles of the IMF to give it direct and comprehensive jurisdiction over capital requirements, the proposal lost momentum after the East-Asia crisis.[386] The argument that capital account liberalisation could have a destabilising effect reverberated with even greater resonance.[387] More than ever before, a view crystalised that "capital controls are a legitimate part of the toolkit to manage capital inflows in certain circumstances"[388]. Yet paradoxically, the need for a coordinated regulation of capital movements is in some circles still being proposed as a response to the 2007-2010 global crisis .[389]

A prudential 'carve-out' also plays an important function of protecting national economies from the effects of systemic risk or shock. In defining prudential measures, Pasini says:

> "Prudential measures consist of regulations that aim at limiting the systemic risk on financial institutions in relation to cross-border flows. The risk is usually associated with the exposure of financial institutions to foreign currencies' fluctuations."[390]

It is apparent, therefore, that these measures regulate factors of systemic significance and are designed to curb spillover effects or the spread of shock across the national and global

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[383] Kelsey J *supra* at 846 defines financialization as "the shift in gravity from industrial production to finance as the prevailing mode of wealth creation or capital accumulation."
[384] Kelsey J *supra* at 846.
[385] Viterbo A *supra* at 196.
[386] Viterbo A *supra* at 189.
[387] Stiglitz JE *supra* at 62-63 argues that capital movements may be disruptive to a national economy.
[388] Ostry J D *et al* "Capital Inflows: The Role of Controls" *IMF Staff Position Note* February 19 2010 SPN/10/04 at 15.
[389] Camdessus M *et al* "Reform of the International Monetary System: A Cooperative Approach for the Twenty First Century February 8th 2011" *Palais-Royal Initiative* at 6 and 11. Available at http://global-currencies.org/smi/gb/telechar/news/Rapport_Camdessus-integral.pdf (Accessed on 17 January 2015).
[390] Pasini FL "Movement of Capital and Trade in Services and Trade: Distinguishing Myth from Reality Regarding the GATS and the Liberalization of the Capital Account" (2012) 15 (2) *Journal of International Economic Law* 581-619 footnote 28 at 590.

economic structures. They may operate in ways that are contrary to states' 'specific commitments' under the GATS system.[391] Prudential measures are distinguishable from capital controls[392] on the basis of how they function. In some instances, a "prudential carve-out grants a wide policy space in which to restrict capital movements in the presence of a threat to financial stability."[393] Carve-outs provide states with regulatory breathing space in light of substantial constraints imposed by international agreements. They help preserve a modicum of sovereignty[394] even though they are sometimes invoked to justify protectionism.[395]

The Balance of payment clauses, normally built into multilateral and bilateral treaties, are highly significant in preseving state sovereignty.[396] Article XI section 1 of the GATS states that:

> "[i]n the event of serious balance-of-payments and external financial difficulties or threat thereof, a Member may adopt or maintain restrictions on trade in services on which it has undertaken specific commitments, including on payments or transfers for transactions related to such commitments."[397]

The capacity of treaty provisions such as transitional arrangements, carve-out and derogation clauses in preserving sovereignty is, however, limited because they "are subject to a number of substantive and procedural conditions."[398] Inspite of the effect of the substantive and procedural conditions, the state can still invoke the provisions whenever its economic stability is being threatened.

4.6. CONCLUSIONS

The discussion in this chapter has established the basis for juridical constraints on monetary sovereignty. Two bases, namely, customary public international law principles and the treaty provisions have been identified. An exploration of customary public international was undertaken first, followed by treaty based constraints. Although customary law principles play a modest role in this area of law, they still set the minimum standards of treatment that one may expect in the absence of express treaty provisions. The constraining role of treaties on the other hand is far more substantial and clearer than that of customary rules. Since

[391] Viterbo A *supra* at 132.
[392] Pasini FL *supra* footnote 28 at 590.
[393] Pasini FL *supra* at 619.
[394] Article 2(a) of the Annex on Financial Services to the GATS.
[395] Zimmermann CD *supra* at 20.
[396] UNCTAD *supra* at 1. Gari G *supra* at 412 and 418.
[397] Article XII:1 of the GATS.
[398] Gari G *supra* at 419. Article XII:2-5 of GATS.

treaty provisions are more than mere re-statements of the customary provisions, their effect on sovereignty is more drastic than that of the former. Provisions from different treaties tend to safeguard common goals and interests. Their collective effects are complementary.

The pivotal roles played by various multilateral treaty regimes, among them the IMF, the GATT and the GATS, the OECD, as well as BITs have been highlighted. Issues such as the prohibition of exchange restrictions and exchange rate manipulations as well as the promotion of international payments and transfers across national frontiers are central to international economic law. The discussion also highlighted the ongoing debate regarding the liberalisation of capital and current payments. While the IMF regime has attained comprehensive liberalisation of current payments and transfers, its 'hands-off' approach to issues of capital transfers has resulted in an asymmetric approach to regulation, a matter that continues to engage legal scholarship and is set to do so for a long time to come.

The need to uphold a balance between the need for national economic stability, on the one hand, and the liberalisation of trade, investment and the capital account liberalisation on the other, demostrates a need for legal provisions that promote liberalisation while at the same time guarding the national economy from the adverse effects of unmonitored liberalisation. The liberal nature of most BITs and Free Trade Agreements (FTAs) has made the states more vulnerable to litigation especially with regards to the covered investments.[399] Free capital transfer provisions "offer foreign investors the possibility of suing host states before international tribunals for the breach of these provisions."[400] The absence of properly designed safeguards enhances the vulnerability of states who have to uphold commitments even when the effect of doing so would be detrimental to their economies.

The existence of sovereignty saving mechanisms is a very important factor which underscores the extent to which the onslaught against sovereignty receives some tempering, thereby keeping its effects within modest extents. The next chapter of this study is a synthesis of the main issues discussed in the other chapters. It considers how the juridical constraints on mometary sovereignty affect the states in light of concrete cases of litigation that have sprung up, taking occasion of states' restricted margin of manouvre. It explores the implications of the constraints in the context of international law's sovereigty limiting features.

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[399] Gari G *supra* at 401.
[400] *Ibid.*

CHAPTER 5

5 IMPLICATIONS OF JURIDICAL CONSTRAINTS FOR INTERNATIONAL ECONOMIC LAW

5.1 INTRODUCTION

This study has so far identified the constraints that operate against the exercise of full-fledged monetary sovereignty of states. It is the purpose of this chapter to identify the implications of these limitations in light of how they shape the legal relations and obligations. Some states have been sued for breach of treaty obligations which constrain sovereignty in a substantial manner. The legal disputes have been handled mostly by arbitral tribunals and the consequences to the respondent states have been drastic. A case by case review of some of the disputes reveals how investor-state arbitral tribunals pass verdicts whereby investor interests have prevailed over the sovereignty. This chapter, therefore, ponders the question regarding how some constraints have shaped and continue to shape the way in which role players and functionaries interact on the international economic plane as well as how the law needs to evolve so as to meet the dynamic needs of the commerce.

The legal relationships affected by the constraints are the focal point of this discussion which also attempts to illustrate how the peculiarities of each relationship determine the responses adopted in order to satisfy the demands of the particular situation.

5.2 DIVERGENT INTEREST GROUPS AND PERSPECTIVES ON SOVEREIGN RESTRICTION

The broad area of concern involves numerous interest groups, each of which is motivated differently in its consideration of issues regarding monetary sovereignty. There are interest groups that are directly affected by the way international economic law functions. These are the traders and investors, mainly saddled with concerns about securing their monetary interests and the guarantees of payment for the goods and services delivered. The state is another interest entity whose concerns border on the strategic choices its needs to make while carrying out its daily duty to legislate without fetters.[401] It also needs to make provisions for sufficient policy space while executing its mandate to govern particular territory to the

[401] Spears S A "The Quest for Policy Space in a New Generation of International Investment Agreements" (2010) (13) 4 *Journal of International Economic Law* 1037–1075 at 1071.

satisfaction of the demands of the citizenry. Another crucial interest group is the international community whose goals, among others, encompass the securing of a stable global system.[402] It is constituted by the different states and it is motivated towards protecting the benefits of international trade and investment. The growing incidence of investor-state disputes[403] certainly places onerous burdens on the host states amid calls for a revision of the investment agreement concerned.[404]

The perceived benefits of foreign direct investment in stimulating national development have led to an increase in the number of international treaties signed between states.[405] As a result, the alleged breaches of these investment treaties have been the basis for the numerous investor-state arbitral disputes.[406] While it remains an important pursuit of these agreements to protect the investors, the pursuit of this legitimate objective has resulted in inconsistent decisions and interpretations of the treaties.[407] The powers of the state to apply regulatory measures have been circumscribed to the point of constraining the power of the state to achieve its legitimate policy objectives.[408]

It is expedient therefore to craft international agreements in such a way as not to unduly burden the state through treaty provisions that overly restrict its margin of manoeuvre in the event of any need for the application of corrective strategies.[409] Instead, the needs of the international economic community would best be served by a system that is sensitive to the needs of states whose mandate is to provide services to their citizens.[410] One of the developments of the recent decades was dominance of 'neo-liberalism' and its entrenched belief in the power of markets to 'self-regulate' and 'self-correct'.[411] This emphasis, which came at the expense of national sovereignty, led to the signing of investment agreements

[402] Lastra RM *Legal Foundations of Intrenational Monetary Stability* 2006 at 36.
[403] UNCTAD "World Investment Report" 2014 at 114.
[404] Spear SA *supra* at 1040.
[405] UNCTAD *supra* at 114.
[406] The USA-Argentine BIT has been the basis for most of the claims against Argentina.
[407] Spear SA *supra* at 1040.
[408] Spear SA *supra* at 1039.
[409] Kelsey J, 'How the Trans-Pacific Partnership Agreement Could Heighten Financial Instability and Foreclose Governments' Regulatory Space', (2010) 40 *New Zealand Yearbook of International Law* at 8.
[410] Franck TM "Centrifuge and Centripede: Principles for the Centralisation and Decentralisation of Governance" in Broude T & Shay Y *The Shifting Allocation of Authority in International Law* 2008 at 22.
[411] Kelsey J *Serving Whose Interests? The Political Economy of Trade in Services Agreements* 2008 at 97. See also Spear SA *supra* at 1041 who says that in terms of neo-liberalism, the state does not need to intervene in the market. Instead market forces determine the behaviour of the market. In the event of any failures, the markets have a capacity to correct themselves.

that elevated the rights of investors above the state's duty to legislate, a development that has been appropriately termed 'regulatory chill."[412]

The influence of some large corporates is a very important factor in shaping the terms of the BITs. Enjoying the advantage of their powerful domestic backing, the large corporates and transnational corporations have the ability to lobby for the entrenchment of their interests and can influence governments during the drafting of model BITs.[413] Rent seeking interests have the capacity to influence government and affluent groups often use their influential positions to push for BIT terms that are favourable to their interests.[414] All this comes at the expense of sovereignty and manifests itself through the attenuation of the powers of the state to regulate the environment and to promote development.[415] Capital exporting countries, which happen to have a dominant position by virtue of their superior economic status, usually have the opportunity to dangle the proverbial carrot of 'investment capital' before the less developed countries.[416] Because the latter are usually desperate for investment, they, without proper calculation, sign investment agreements whose terms are adverse to their future developmental needs.

In drawing up treaties, it is important to strike a balance between the need to protect investment with the need to preserve sufficient regulatory space for the state to ably deal with emergencies and crises.[417] Capital controls and exchange rate management are essential elements of the macro-economic management tool-kit to deal with unexpected surges in capital movements as well as financial speculation.[418] One of the facts to emerge from the post-2007 global financial crisis was that massive speculation had played a critical role in its genesis and as such it becomes vital for states to put in place some measures so

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[412] Spears SA *supra* at 1040.
[413] Morgenson G "Market Watch; A Company Worth More Than Spain?" 26 December 1999. Available at http://www.nytimes.com/1999/12/26/business/market-watch-a-company-worth-more-than-spain.html (Accessed on 27 December 2014). Some big corporates such as Microsoft, Hewlett-Packard among others have higher incomes than GDPs of certain nations.
[414] Raustiala K "Rethinking the Sovereignty Debate in International Economic Law" (2003) (4) (4) *Journal of International Economic Law* at 867. See also Eichengreen B "Capital Account Liberalization: What do cross-country Studies tell us?" (2001) (15) 3 *The World Bank Economic Review* at 342.
[415] Brandauer S G *Sovereign Debt and Economic Policies in Global Markets: A Political Economy Approach* 2005 at 17.
[416] Alvarez JE & Khamsi K "The Argentine Crisis and Foreign Investors: A Glimpse into the Heart of the Investment Regime" in Karl P Sauvant (ed) *The Yearbook on International Investment Law and Policy 2008/2009* at 281-282.
[417] Ostry J D *et al* "Capital Inflows: The Role of Controls" *IMF Staff Position Note* February 19 2010 SPN/10/04 at 8.
[418] Stiglitz JE " Capital-Market Liberalization, Globalization and the IMF" (2004) (20) (1) *Oxford Review of Economic Policy* at 59.

as to curb such speculation.[419] However, if the state has undertaken restrictive international commitments, controlling such problems may be seriously frustrated.[420]

While there used to be an almost neat distinction between private and public international law,[421] the recent proliferation of investment agreements has narrowed the divide in such a way that roles and functions have come to a point of overlap.[422] There has been a significant blurring of the divide between public and the private law.[423] Investors have, in some BITs, been empowered to enforce the rights contained in the treaties through tribunals and the beneficiaries of such a development are their home countries.[424] Some BITs make use of elaborate provisions regarding arbitration as a result of which there has been a significant rise in the incidence of investment disputes handled by organisations such as the World Bank's International Centre for the Settlement of Disputes (ICSID) and the United Nations Commission on International Trade Law (UNICITRAL) among others.[425] What further complicates the issue is that, until recently, the claimant investors usually belonged to developed countries while the states being sued were mostly developing ones.[426]

Karl makes a highly remarkable observation by noting how treaties limit the sovereignty of contracting state parties"[427] to the point of restricting their powers to effectively pass monetary legislation. The observation also goes far enough to point out that states still retain a great measure of autonomy since they are "the 'masters of the treaties' they conclude."[428] They reserve the freedom to pull out of burdensome treaties if they need to.[429] That precisely implies that the power to determine how a state is affected by a treaty still lies within realm of

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[419] Cottier T "The Emerging Principle of Common Concern: A Brief Outline" in Petersmann EU(ed) *Multilevel Governance of Interdependent Public Goods Theories, Rules and Institutions for the Central Policy Challenge in the 21st Century* 2012 185-193 at 188.

[420] Kelsey J "The Conundrum of Shifting Orthodoxies: FTAs and Korea's Currency Controls" (2011) 14 (4) *Journal of International Economic Law* 845–868 at 846.

[421] Petersmann EU "JIEL Debate: Methodological Pluralism and its Criticism in International Economic Law Research" (2012) 15 (4) *Journal of International Economic Law* 921-970 at 942.

[422] Picciotto S *Regulating Global Corporate Capitalism* 2011 at 186. See also Alvarez JE & Khamsi K "The Argentine Crisis and Foreign Investors: A Glimpse into the Heart of the Investment Regime" in Sauvant KP (ed) *The Yearbook on International Investment Law and Policy 2008/2009* at 281.

[423] Piccioto S *Regulating Global Corporate Capitalism* 2011 at 20.

[424] Alvarez JE & Khamsi K "The Argentine Crisis and Foreign Investors: A Glimpse into the Heart of the Investment Regime" in Sauvant KP (ed) *The Yearbook on International Investment Law and Policy 2008/2009* at 282.

[425] The recent spate of litigation against the Republic of Argentina which recorded more than 40 arbitral disputes filed against the state are testimony of how an untimely surrender of sovereignty can prevent a state from adopting corrective monetary measures when faced with a crisis.

[426] Spears SA *supra* at 1042.

[427] Karl J "International Investment Arbitration: A threat to State Sovereignty?" in Shan W, Simmons P and Singh D (eds) *Redefining Sovereignty in International Economic Law* (2008) at 230.

[428] *Id* at 244.

[429] The fact that a state has signed a treaty does not mean that its powers are permantly restricted. It can still exercise its sovereign powers by withdrawing from a treaty regime, albeit at a cost. See Raustiala K "Rethinking the Sovereignty Debate in International Economic Law" (2003) 6 (4) *Journal of International Economic Law* at 849.

the state. Such an assertion, however, is subject to qualification when one considers the disparity in economic power among the contracting states.[430] It is indeed a persuasive conclusion since, when one considers investment treaties, it is apparent that "the investment regime is built on "horizontal disequilibria among states that are supposed to be sovereign equals."[431]

By virtue of some BIT provisions, private parties in need of arbitration have been placed on a relatively favourable pedestal, an almost equal footing with the contracting state party.[432] The possibility for arbitration has opened up doors for litigation by these private economic interest groups against states.[433] While the former scenario always placed every contract within the jurisdiction of a particular state, the prospect of arbitration before a neutral tribunal removes the veil of sovereignty that once shielded states from litigation.[434] Arbitration is surely 'denationalised' in that "national law is entirely excluded and state parties are obliged to comply with the award of the tribunal, subject only to the provisions for appeal to an Annulment Committee."[435]

5.3 BITS, FTAS AND THE RESTRICTION OF POLICY SPACE

In chapter 4, this study considered the numerous factors that constrain monetary sovereignty. Those constraints have numerous and varied implications to international economic law. The powers of the state to control the inflows and outflows of capital across its national borders, to determine the exchange rate between its currency and the currencies of other states, are the attributes of monetary sovereignty normally affected by the constraints. By signing a treaty, a state may severely restrict its legislative powers,[436] constrain its policy space and put itself in a very difficult position should there arise a need to correct its balance of payments disequilibrium. Meanwhile, exercising the state's power to

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[430] Alvarez JE & Khamsi K "The Argentine Crisis and Foreign Investors: A Glimpse into the Heart of the Investment Regime" in Karl P Sauvant (ed) *The Yearbook on International Investment Law and Policy 2008/2009* at 282.
[431] *Ibid.*
[432] Picciotto S *supra* at 184 & 189.
[433] Karl J *supra* at 226.
[434] Picciotto S *Regulating Global Corporate Capitalism* 2011 at 182.
[435] *Id* at 184.
[436] Karl J "International Investment Arbitration: A threat to State Sovereignty?" in Shan W, Simmons P and Singh D (eds) *Redefining Sovereignty in International Economic Law* 2008 at 232.

determine the exchange rate may in certain circumstances be viewed as a form of currency manipulation.[437]

The implications of the constraints may raise questions of democratic legitimacy[438] among others while locking up the state's policy space may frustrate any room for manoeuvre, giving rise to national resistance.[439] The operative bias of the constraints against the national developmental goals and in favour of large corporates[440] is an issue of critical concern particularly among the less developed countries.

As discussed in the previous chapter of this study, there are certain sovereignty saving measures that bring moderation to the adverse effects of the juridical constraints. It is, however, plausible to state that the effects of these measures tend to be mostly modest and insufficient to mitigate the results of the international law encroachments on national economies. It is arguable that the predominance of market fundamentalism,[441] expressing its sway through multilateral trade and investment agreements is excessively restrictive of national sovereignty and is a great compromise to developmental goals. The Seattle demonstrations of 1999[442] sent a clear message of scepticism towards economic globalisation and all its ramifications. As a result, the orientation of the Doha Development Agenda,[443] towards a development agenda was an acknowledgement of the limitations of

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[437] De Lima-Campos A & Gil JAG "A Case for Misaligned Currencies as Counter-vailable Subsidies" in UNCTAD XIII Pre-Conference Event Policy Dialogue: *Redefining the Role of the Government in Tomorrow's International Trade* 26 – 27 March 2012 Room XVI, Palais des Nations, Geneva at 2.

[438] Spears S A "The Quest for Policy Space in a New Generation of International Investment Agreements" (2010) (13) 4 *Journal of International Economic Law* 1037–1075 at 1040.

[439] On 08 November 2014, protest marches took place in Auckland, Wellington and other cities of New Zealand as protesters marched against TPPA trade. The protesters argued that the proposed deal whose discussions were shrouded with great secrecy grossly threatened the sovereignty of New Zealand while overly granting protection to US monopolies. http://www.google.co.za/url?sa=t&rct=j&q=&esrc=s&source=web&cd=3&ved=0CC4QFjAC&url=http%3A%2F%2Fwww.stuff.co.nz%2Fnational%2F10720880%2FMarches-against-TPPA-trade-deal&ei=WXaZVM-bFcyuU-vKg7gL&usg=AFQjCNHNg_jwQK-YfBmDWpbxOM_MXVCEFw&bvm=bv.82001339,d.d24 (Accessed 23 December 2014).

[440] Kelsey J "Why you should join the TTPA Action on 08 November" available at http://thedailyblog.co.nz/2014/10/20/why-you-should-join-the-tppa-action-on-8-november/ (Accessed 23 December 2014).

[441] Stiglitz JE "Moving beyond Market Fundamentalism to a More Balanced Economy" (2009) (80) (3) *Annals of Public and Cooperative Economics* 345-360 at 346. Market fundamentalism was an important element of neo-liberalism and in terms of it, markets work efficiently on their own without governement intervention.

[442] In 1999, protestors staged protests in City of Seattle, in the USA, to express their displeasure on how the WTO was handling issues such as workers' rights, sustainable development, environmental and social issues among other things. They perceived that sovereignty was being sacrificed for the benefit of corporates while other objectives were left to suffer. Available at "World Trade Organization Protests in Seattle" http://www.seattle.gov/cityarchives/exhibits-and-education/digital-document-libraries/world-trade-organization-protests-in-seattle (Accessed on 17 January 2015).

[443] Spear SA *supra* at 1071 states that sustainable development has a great role to play in shaping the future of investment law so as to balance the need for investor protection with other objectives such as the protection of health, security etc.

the previous rounds' effectiveness in addressing the states' obligations towards their constituencies. It was an unequivocal declaration that the benefits of trade do not necessarily deserve greater legal protection than development.

It is apposite at this juncture to further to explore the effects of trade and investment agreements on the less developed countries in the context of economic theory. On 31 January 2011, a group of economists wrote a letter to the US Secretary of State, Hillary Rodham Clinton as well as Timothy Geithner, the US Treasury Secretary and Ambassador Ron Kirk of the Office of the United States Trade Representative.[444] They expressed their concerns on how the US trade Agreements were negatively affecting the US trading partners. The group of prominent economists, including Ricardo Hausmann, Dani Rodrik, Joseph Stiglitz, Arvind Subramanian among others, argued that the terms of the US Trade Agreements were unduly restrictive on its trading partners and "that capital management techniques should be included among the "carefully designed macro-prudential measures" …"[445] to deal with any unforeseen economic instability. They also noted that, under the "agreements, private foreign investors have the power to effectively sue governments in international tribunals over alleged violations of these provisions."[446] Such provisions strictly limit the powers of the trading partners to effectively deploy policy tools and to correct any macro-economic maladies.

As can be discerned from the arguments presented by the economists, the BITs and FTAs have the effect of severely restricting the states' policy space. Investors, most of whom are large corporates, are usually granted rights to sue the host states in order to enforce monetary provisions, notwithstanding the detrimental effects this might have on the overall welfare of the state.[447] The restriction on the use of capital controls exposes the states to volatile capital flows and strips them of the means to "stem the development of dangerous asset bubbles and currency appreciations…"[448]

[444] Reforming U.S Treaties: Recommendations from State Advisory Committee on International Economic Policy. www.ase.tufts.edu/gdae/policy_research/capctrlsletter.html (Accessed 23 December 2014.)
[445] Hausmann R "Letter to US Secretary of State Hillary R Clinton and Secretary of Treasury Timthy Geithner" (hereafter the letter to Hillary R Clinton). Available at www.ase.tufts.edu/gdae/policy_research/CapCtrlsLetter.pdf (Accessed on 07 January 2015).
[446] *Ibid*.
[447] *CMS Gas Transmission Company v Argentina* (ICSID 2005). Available at http://www.italaw.com/sites/default/files/case-documents/ita0184.pdf (Accessed on 12 January 2014). As a result of a series of economic challenges Argentina abandoned the currency peg which placed the Peso at a fixed peg with the US Dollar. The process known as '***pesification'*** had detrimental effects on foreign investors and a number of these investors brought action before international tribunals such as the ICSID.
[448] Hausmann R *supra*.

This danger for Free Trade Agreements and BITs to foreclose governments' regulatory capacity has been expressed by Kelsey who correctly observes that through these treaties, states sometimes bind themselves to "obligations that could heighten financial instability and prevent governments from taking appropriate pre-emptive or remedial action in relation to future crises."[449] What gives the risk of litigation a higher likelihood is the fact that these treaties provide room for investors to litigate directly. They do not necessarily have to rely on their states to litigate on their behalf or to protect them through invoking diplomatic protection. They can do it without state assistance.[450]

The response by the US Treasury office, represented by Timothy F. Geithner, however was a blatant attempt to downplay the adverse effects of the restrictions cited in the economists' letter. The US Treasury office argued that the risks which accompany swings and surges in capital flows "are best managed through a mix of fiscal and monetary measures, exchange rate adjustments, and carefully designed non-discriminatory prudential measures, such as bank reserve or capital requirement and limitations on exposure to exchange risks."[451] Such a response fell far short of appreciating the effects of the restrictions on the other states and instead sounded more as a partisan expression of a stereotyped political position than a communication of economic rationale.

The issues raised by the economists in their letter have been highlighted by the events in Argentina following the economic crisis that began in 1999 and spilled over into the 2000s. The story of Argentina is a distinct case study illustrating how far treaty clauses can limit state sovereignty. When the state faced a crippling economic crisis characterised by massive and violent street protests, it declared a state of emergency and "eliminated parity between the US Dollar and the Peso."[452] The adoption of the corrective monetary measures triggered a series of arbitral disputes by several foreign investors.[453]

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[449] Kelsey J "How the Trans-Pacific Partnership Agreement Could Heighten Financial Instability and Foreclose Governments' Regulatory Space" *New Zealand Yearbook of International Law* Vol 8 2010 at 6.

[450] Kelsey J "The Conundrum of Shifting Orthodoxies: FTAs and Korea's Currency Controls" (2011) 14 (4) *Journal of International Economic Law* 845–868 at 37.

[451] On 12 April 2011, Timothy F Geithner, US Secretary of Treasury wrote a letter in response to the economists' statement and defended the US position regarding the US trade agreement provisions in respect of the use of capital countries. Available at www.ase.tufts.edu/gdae/policy_research/Geithner_response_to_capital_controls_letter.pdf (Accessed on 07 January 2015).

[452] Binder C "Necessity Exceptions, the Argentine Crisis and Legitimacy concerns: Or the Benefits of a public International Law Approach to Investment Arbitration" in Treves T, Seatzu F & Trevisanut S *International Investment Law and Common Concern* 2014 at 72. The emergency powers of 2000 were heavily contested while the state attempted to base its argument on necessity.

[453] Alvarez JE & Khamsi K "The Argentine Crisis and Foreign Investors: A Glimpse into the Heart of the Investment Regime" in Sauvant KP (ed) *The Yearbook on International Investment Law and*

The crisis exerted enormous pressure on the monetary system of the country to the extent that the state was compelled to adopt emergency monetary measures to redress the situation. However, the consequences of these measures were detrimental to the interests of several foreign investors,[454] who being aggrieved by the measures, relied on BIT terms and launched claims for the recovery of financial loses allegedly suffered due to the state's action. An act that could, in terms of customary international law, be viewed as an unchallengeable 'act of state'[455] had been turned into a subject of arbitration before a tribunal. Investors opted for arbitration under the ICSID and UNICITRAL rules mostly on the basis of the *Treaty Between the United States and the Republic of Argentina Concerning the Reciprocal Encouragement and Protection of Investment of 1991,* (hereafter called the US-Argentina BIT.)[456] The series of arbitration cases showed the extent to which the contracting states' policy space had been narrowed by the BITs to which the state was a signatory.

The *CMS Gas Transmission Company v Argentina*[457] arbitral case was based on the United States -Argentina BIT of 1991 and was dealt with in terms of the ICSID arbitration rules while the *National Grid plc v. Argentina*[458] arbitral case was based on the UK-Argentina BIT[459] and was handled in terms of the UNICITRAL arbitration rules. Other notable cases include *LG&E Energy Corporation, LG&E Capital Corporation, LG&E International Inc. v The Argentine Republic* (2006-2007) also handled by the ICSID. The *AWG Group v The Argentine*

Policy 2008/2009 at 389. See also Binder C *supra* at 72. The emergency powers of 2000 were heavily contested while the state attempted to base its argument on necessity.

[454] Alvarez JE & Brink J "Revisiting the Necessity Defence: Continental Casualty v. Argentina" *Yearbook International Investment Law and Policy* 2010 and 2011 at 318 say that Argentina's capital control regime included measures such as bank freezes and prohibition on international currency transfers (*Corralito),* an end of convertibility with the US dollar, *'pesification'* of US dollar deposits, the rescheduling of term deposits, defaults on debt obligations.

[455] Bazyler MJ " Abolishing the Act of State Doctrine" (1986) (134) *University of Pennsylvania Law Review* 325-398 footnote 36 at 332. The 'act of state' doctrine means that acts done by a state in fulfillment of its sovereign duties should not be challenged by another. Bazyler re-iterates the statement made by Chief Justice Fuller in the "*Underhill Case"* when he said that "the courts of one country will not sit in judgment on the acts of the government of another done within its own territory." See also *Underhill v. Hernandez* 168 US 250 (1897) at 252.

[456] *The Treaty between the United States of America and the Argentine Republic concerning the Protection of Investment 14 November 1991* Available at http://2001-2009.state.gov/documents/organization/43475.pdf (Accessed 08 January 2015). The state of Argentina faced more than 40 cases brought before *ad hoc* tribunals convened in terms of World Bank's International Centre for Settlement of Investment Disputes (ICSID) tribunal. Alvarez JE & Khamsi K "The Argentine Crisis and Foreign Investors: A Glimpse into the Heart of the Investment Regime" in Karl P Sauvant (ed) *The Yearbook on International Investment Law and Policy 2008/2009* at 379.

[457] *CMS Gas Transmission v. Argentina* (ICSID Case No. ARB/01/8) 2005.

[458] *National Grid plc v. The Argentine Republic* (UNICITRAL Case 1:09-cv-00248-RBW,03 November 2008).

[459] Agreement Between the Government of the United Kingdom of Great Britain and Northen Ireland and the Government of the Republic of Argentina for promotion and Protection of Investments December 11, 1990. Available at https://treaties.un.org/doc/publication/unts/volume%201765/volume-1765-i-30682-english.pdf (Accessed on 18 January 2015).

Republic[460] case was handled in terms of UNICITRAL rules. Apparently, the claims against Argentina have numbered more than forty and have been, to say the least, overwhelming for the state.[461]

While defending its decision to adopt the emergency measures, the state of Argentina argued that the measures were necessary under the circumstances. It was argued on behalf of the state that the suspension of foreign currency payments, the abandonment of the currency peg of the Peso to the US Dollar and the decision to effect all payments in local currency were the only options open to the state at the time of the crisis and that the states' conduct was actuated by necessity. It was argued that the 'Emergency Law,' passed was "intended to cure, through realistic measures, the existing state of necessity."[462]

Investors challenged Argentina's actions on the basis of a breach of the Fair and Equitable Treatment (FET) standard. It was argued that the state had expropriated the properties of the foreign investors and had also discriminated against some of them.[463] While the tribunal found Argentina to have breached the FET standard and the state's conduct to have been discriminatory, the same could not be said in connection with expropriation.[464] In some instances, tribunals upheld the defence of 'necessity' as sufficient to excuse the conduct of Argentina under the circumstances.[465]

It would be appropriate in certain circumstances to assess the conduct of the state in terms of whether there could have been any least restrictive alternatives that could serve the purpose. Other considerations would include the "proportionality and the 'reasonable nexus to rational government policies'.[466]

For the cases based on the US-Argentina BIT, the basis for the defence of necessity was Article XI,[467] read in conjunction with Article 25[468] of the International Law Commission

[460] *Suez, Sociedad General de Aguas de Barcelona S.A., and Vivendi Universal S.A. and The Argentine Republic (ICSID Case No. ARB/03/19*) and *AWG Group v The Argentine Republic* (UNCTRAL). Available at http://www.italaw.com/sites/default/files/case-documents/ita0055.pdf (Accessed on 08 January 2014).

[461] Alvarez JE & Khamsi K "The Argentine Crisis and Foreign Investors: A Glimpse into the Heart of the Investment Regime" in Karl P Sauvant (ed) *The Yearbook on International Investment Law and Policy 2008 / 2009* at 379.

[462] *Continental Casualty Company v. Argentine Republic* (ICSID Case No ARB/03/9) 2008.

[463] *LG & E Energy Corporation, LG & E Capital Corporation, LG & E International Incorporated v. The Argentine Republic* (ICSID) 2007 at paragraphs 147-148.

[464] *Continental Casualty Company v. Argentine Republic supra* at paragraph 304.

[465] *Ibid.*

[466] Spears *supra* at 1048-1049.

[467] Article XI of the US-Argentina BIT reads as follows; "This Treaty shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfilment of its obligations with respect to the maintenance or restoration of international peace or security, or the Protection of its own essential security interests."

Articles of State Responsibility.[469] In most of the cases, the defence was viewed as insufficient to exclude compensation by the state for the losses suffered by the investors. In the case of the *Continental Casualty v Argentine Republic Award*[470] the tribunal upheld the defence of necessity just as the case of *CMS Gas Transmission Company v Argentine*[471] had also determined.[472] Owing to the fact that the necessity was of a temporary nature however, its existence with respect to Argentina did not exclude compensation.[473] The Annulment Committee said;

> "Article XI, if and for so long as it applied, excluded the operation of the substantive provisions of the BIT. That being so, there could be no possibility of compensation being payable during that period."[474]

The jurisprudence of the Argentine cases has revealed the limitations of the defence of necessity in cases of the BIT law and has highlighted the extent to which states should exercise caution when drawing as well as signing BITs. Remarkably, the *Sempra v. Argentina* Annulment Committee was more sympathetic to the state's argument and would have readily accepted its defence of necessity.[475] Evidently, the state of Argentina had bound itself to such proportions that its employment of corrective measures had become subject to limitations under the US-Argentine as well as the UK-Argentine BITs. In the absence of the defence of necessity, sovereignty is severely constrained and the potential detriment to governance is evidently high. Viterbo notes that:

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[468] Article 25 of International Law Commission Articles on Responsibility of States for Internationally Wrongful Acts reads as follows:
"1. Necessity may not be invoked by a State as a ground for precluding the wrongfulness of an act not in conformity with an international obligation of that State unless the act:
a) is the only means for the State to safeguard an essential interest against a grave and imminent peril; and
b) does not seriously impair an essential interest of the State or States towards which the obligation exists, or of the international community as a whole.
2. In any case, necessity may not be invoked by a State as a ground for precluding wrongfulness if:
a) the international obligation in question precludes the possibility of invoking necessity; or
b) the State has contributed to the situation of necessity."
International Law Commission "State Responsibility 2001 Available at http://legal.un.org/ilc/texts/instruments/english/commentaries/9_6_2001.pdf (Accessed on 12 January 2015).
[469] Alvarez-Jimenez A "The Great Recession and the New Frontiers of International Investment Law: The Economics of Early Warning Models and the Law of Necessity" (2014) (17) *Journal of International Economic Law* 517–550 at 531.
[470] *Continental Casualty Company v. Argentine Republic supra* at 134.
[471] *CMS Gas Transmission v. Argentine Republic* at paragraph 380.
[472] Proctor C *Mann on the Legal Aspect of Money* 7th Edition 2012 at 657.
[473] *CMS Gas Transmission Company v. Argentina Decision on Annulment* (ICSID Case No.ARB/01/8) (2007)at paragraph 163.
[474] *Id.* paragraphs 144-147.
[475] *Sempra Energy International* v. *Argentine Republic Annulment Decision* (ICSID Case No. ARB/02/16) 2007 at paragraph 222. Available at http://www.italaw.com/sites/default/files/case-documents/ita0770.pdf (Accessed on 09 January 2015).

> "A host State hit by an economic crisis may essentially rely on two lines of defence: the customary law principle of 'state of necessity' and the exercise of monetary sovereignty."[476]

The writer however laments the fact that "the Argentinian cases showed the uncertainties connected with these legal arguments."[477] It is noteworthy however, that the doctrine of necessity is an accepted theory which can be applied in respect of treaty provisions.[478]

As far as the question whether or not the investment decisions imposed 'excessive' restrictions on Argentina's regulatory authority, Binder writes as follows;

> "In the result, Argentina was left with very little room for measures to remedy its economic crisis situation. The Argentine decisions may thus also be read as 'excessive' or inappropriate restrictions of a state's regulatory authority in the face economic / financial emergencies."[479]

The above quote aptly bolsters the argument in favour of reserving more sovereign powers to the state during treaty formulation. A reading of some of the cases such as the *Sempra v. Argentina*[480] and the *Enron v. Argentina*[481] does attest to the fact that some of the decisions were overly investor oriented[482] and severely compromising of non-trade values instead of seeking a balance of the two.[483] Granted the prospect of severely restricting policy space by treaty, states may have to deeply consider the terms before concluding a treaty. One of the criticisms against the investor-state tribunals is that they "have rarely balanced host states' rights and duties to regulate in the public interest against investors' rights when interpreting

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[476] Viterbo A *International Economic Law And Monetary Measures Limitations to States' Sovereignty and Dispute Settlement* 2012 at 281.
[477] *Ibid.*
[478] Proctor C *supra* 2012 at 655.
[479] Binder C "Necessity Exceptions, the Argentine Crisis and Legitimacy Concerns: Or the Benefits of a Public Law Approach to Investment Arbitration" in Treves T, Seatzu F & Trevisanut S *International Investment Law and Common Concern* 2014 at 81.
[480] *Sempra v.Argentina supra.*
[481] *Enron v. Argentina Enron Corporation Ponderosa Assets L.P v. Argentine Republic* (ICSID Case No. ARB/01/3) 2007.
[482] Anna de Luca "Non Trade Values protection and Investment Protection in EU Investment Policy " in Treves T, Seatzu F & Trevisanut S *International Investment Law and Common Concern* 2014 137-153 at 153.
[483] Anna de Luca at 153 above. At 140, Anna De Luca indicates how the contracting state's freedom of action needs to be protected so that the state can freely regulate matters such as health, safety and the environment. It includes safeguarding of host parties regulatory space for regulation in public interest. Non-trade values are those aspects which are of concern to international law even though they are not directly connected with trade and also include the rule of law, human rights, the environment and sustainable development.

an IIA."[484] As can be discerned from the outcomes of the investor-state tribunals, and with the benefit of the hindsight, most BITs were silent on the duty of the state to regulate and this was in keeping with the prevailing neoliberal ideas at the time of their formulation.[485] Investment promotion and protection were topmost in the minds of those that crafted them.[486] Sovereignty was offered as a sacrifice, perceived as a lesser good.

5.4 RETENTION OF GREATER SOVEREIGNTY: CALLS AND CLAMOURS

Concern has been raised with regards to the patterns in arbitration decisions.[487] The scale seems to be tilted in favour of the developed countries while the less developed countries find themselves having to defend their conduct before investor-state tribunals. According to an UNCTAD Report, 164 arbitral cases were initiated in the year 2009 alone. A majority of these cases were "initiated by investors from developed countries, with developing and transition countries most often on the receiving end."[488] This is hardly surprising when one considers that the BITs which form the legal basis of the cases were concluded at the time when the rich countries dominated the international law making process. This explains why there were glaring "inconsistencies and lack of coherence between arbitral decisions."[489]

The skewed pattern of the decisions in favour of the corporates explains the connection between law making process and their ability to lobby for the protection of their interests. The influence of corporates in moulding opinions cannot be denied when one considers that some of them, particularly in the developed countries, have higher annual incomes than the GDPs of most nations.[490] By virtue of unlimited financial capacity, Transnational Corporations (TNCs) can surely articulate their interests to the point of getting them entrenched in BITs, FTAs as well as multilateral legal regimes.[491] Such corporate agendas are disguised behind the state negotiators so as to gain a semblance of legitimacy.[492] It is no

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[484] Spears *supra* at 1046.
[485] Spears *supra* at 1045.
[486] *Ibid.*
[487] Binder C *supra* at 81.
[488] UNCTAD *World Investment Report* 2010 at xxv.
[489] *Ibid.*
[490] Morgenson G "Market Watch; A Company Worth More Than Spain?" 26 December 1999. Available at http://www.nytimes.com/1999/12/26/business/market-watch-a-company-worth-more-than-spain.html (Accessed on 27 December 2014.)
[491] Kelsey J *Serving Whose Interest* 2008 at 58 opines that the GATS regime was born out of collaboration between US corporates and political interest groups motivated by a desire to create "a binding and enforceable treaty that could restore the country's economic supremacy."
[492] Bagwell K & Staiger R "National Sovereignty in the World Trading System" (2001) (22) 4 *Havard International Review* 54-59 at 54. Available at www.dartmouth.edu/~rstaiger/National.Sovereignty.WTO.pdf (Accessed on 10 January 2015). The

wonder that the Doha Round emphasised a development agenda instead of the theme of trade liberalism which had dominated the previous trade rounds.[493]

The emphasis on trade liberalism, a characteristic element of 'corporate capitalism', and of 'neoliberalism' lost appeal towards the end of the 20th Century. The ideas that shaped the 'Washington Consensus'[494] met stiff resistance as illustrated by the demonstrations of Seattle. The aftermath of the demonstrations saw the launch of the Doha Development Agenda. There was evidently a significant break with the traditions of the previous multilateral trade rounds. This fact was well captured by McGuirk who wrote that;

> "The launch of a new trade round in Doha last November was a major breakthrough following the debacle in Seattle in 1999. The new round places the needs and interests of developing countries at the heart of its work, but a successful outcome for rich and poor nations alike is by no means a foregone conclusion."[495]

Yet, the Doha Round also got into a kind of inertia at some point resulting in calls for its revitalisation through the adoption of exchange rate determination as one of the key areas on its table.[496] It is equally important to realise that the Doha Round is characterised by an absence of 'private sector' interests that had dominated the previous rounds.[497] Market access as provided through GATS commitments had tended to favour "private sector' interests but events following the 1999 WTO Ministerial Conference tilted the scale in favour of the weaker sovereigns.

Even if that is the case, it is regrettable that international investment has not received as much attention as ideally should be the case following the adoption of the so-called Singapore Issues at WTO Ministerial conference[498] in 1996. The Singapore issues were

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Seattle demonstrations of 1999 were a reaction to the cumulative dominance of corporate interests which were seem as detrimental to developmental needs of the people.

[493] Fergusson I F "World Trade Organization Negotiations: The Doha Development Agenda" (2011) *Congressional Research Service* at 2. The Uruguay Round of Multilateral Trade negotiantions was a tariff round culminated in the formation of the WTO and its annexes namely the GATT, GATS, and the TRIPS. It is noteworthy though that GATT began in 1947 and the 1994 Agreement was a confirmation of GATT 1947. Other Trade Rounds were the Kennedy Round, the Tokyo Round and the latest being the Doha Round.

[494] Williamson J "The Washington Consensus as Policy Prescription for Development" (2004) *Institute for International Economics* at 1-2

[495] Anne McGuirk "The Doha Development Agenda" http://www.imf.org/external/pubs/ft/fandd/2002/09/mcguirk.htm (Accessed 24 December 2014)

[496] Mattoo A & Subramanian A "Currency Undervaluation and Sovereign Wealth Funds: A New Role for the World Trade Organization" (2008) *World Bank Policy Research Working Paper, no. WPS 4668*. at 22.

[497] *Id* at 20.

[498] Fergusson IF *supra* at 20. The conference was held in Singapore, hence the name 'Singapore Issues'.

adopted as part of the Doha round in 2001 but their discussion came to a halt at the Ministerial Conference of Cancún, in 2003[499] following a deadlock over them.[500] Efforts to bring investment issues to the forefront of multilateral discussions came to a limbo following the collapse of the Cancún conference.

5.5 CURRENCY MANIPULATIONS, DOLLARISATION AND THEIR IMPLICATIONS TO INTERNATIONAL ECONOMIC LAW

The power of a state to determine its exchange arrangement is an integral aspect of statehood.[501] In terms of Article IV of the IMF,

> "Each member shall notify the Fund … of the exchange arrangements it intends to apply in fulfilment of its obligations … and shall notify the Fund promptly of any changes in its exchange arrangements."[502]

This precisely leaves every state with the freedom to decide its own exchange arrangements. A complaint against a state's exercise of this right is, at face value, an untenable affront to the principle of sovereignty. Yet the subject of 'currency manipulation' has in recent years been a topical matter particularly in connection with a monetary dispute involving the USA and China.[503] The matter has drawn the attention of international jurists in recent years,[504] generating a huge academic conversation on the legitimacy of China's currency peg of the Yuan[505] to the US Dollar.

Beginning from 1997, China maintained a currency peg at a rate of RMB 8.28: US1.00.[506] The initial purpose of the peg[507] was to stabilise the financial system at a time when the East-Asian Countries were experiencing an economic crisis. Countries such as Malaysia experienced capital flight and to curb the challenges, they introduced numerous monetary

[499] This was a conference convened to map a way forward on matters of investment, government procurement, trade facilitation and competition policy. Refer to Fergusson I *supra* at 3.
[500] Fergusson IF *supra* at 20.
[501] Chapter 3, paragraph 3.4.4. of this study.
[502] Article IV (2)a of the IMF.
[503] Proctor C *Mann on the Legal aspect of Money* 7th Edition 2012 at 605.
[504] De Lima-Campo A & Gil JAG "A Case for Misaligned Currencies as Countervailable subsidies" in UNCTAD XIII Pre-Conference Event Policy Dialogue: *Redefining the Role of the Government in Tomorrow's International Trade* 26 – 27 March 2012 Room XVI, Palais des Nations, Geneva.
[505] Staiger RW & Sykes AO 'Currency Manipulation and World Trade" (2010) (9) (4) *World Trade Review* at 583-627. See also Proctor C *supra* at 604-6010. Ahn D "Is the Chinese exchange-rate regime "WTO-legal"?" in Evenett Simon J (ed) *The US-Sino Currency Dispute: New Insights from Economics, A VoxEU.org Report* 2010 at 139-145.
[506] Proctor C *supra* at 605.
[507] Proctor C *supra* at 596 defines a monetary peg as fixing the value of one currency in terms of another currency.

measures.[508] China also adopted the peg as one of the monetary measures to contain the crisis. As the years progressed, however, US industrialists began to complain that the 'undervalue' status of the Yuan was acting as an export subsidy granting an unfair advantage to Chinese exports while serving as an import tax[509] on imports into China.[510] At the height of the East Asia crisis, China's economy remained steadfastly stable due to the peg that insulated the currency from volatile fluctuations.[511]

While the pegging of the Yuan against the US dollar may at face value appear to be adverse to US interests, it is nevertheless a legitimate exercise of sovereignty permitted in law. This fact is particularly well noted by Ahn who states that "Pegging an exchange rate to other key currency is not *per se* illegal nor irrational."[512] A question arises therefore in terms of where to draw the line between a legitimate exercise of monetary sovereignty and a violation of a state's obligations in terms of bilateral as well as multilateral legal regimes.

Yet, even in spite of its clear benefits to the Republic of China, the use of the peg remains highly contested in international law.[513] Remarkably, while all eyes have focused on the Republic of China which has been cited as a prime epitome of currency manipulation, it is not the only state to engage in it.[514] Many other states do intervene in the currency market to stabilise their economies.[515] In spite of there being a credible argument to justify the use of a currency peg,[516] it would appear that China's conduct has gone far enough to cross the line of reasonable exercise of sovereignty.[517]

The search for a suitable way to deal with state interventions in the currency markets is still on. Suggestions point towards customary international law as well as treaty law. However,

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[508] Pasini FL. "Movement of Capital and Trade in Services: Distinguishing Myth from Reality Regarding the GATS and the Liberalization of the Capital Account." (2012) 15 (2) *Journal of International Economic Law* 581-619 at 592.
[509] Subramanian A "New PPP-based estimates of renminbi undervaluation and policy implications" in in Evenett S J (ed) *The US-Sino Currency Dispute: New Insights from Economics, A VoxEU.org Report* 2010 at 75.
[510] Proctor C *supra* at 601.
[511] Cohen BJ *Monetary Governance* 2008 at 174.
[512] Ahn D *supra* at 139.
[513] Bergsten CF & Gagnon JE "Currency Manipulation, the US Economy, and the Global Economic Order" (2012) *Peterson Institute of International Economics Number PB 12-25* at 10.
[514] Lima-Campos A & Gil JAG "A Case for Misaligned Currencies as Countervailable subsidies" in UNCTAD XIII Pre-Conference Event Policy Dialogue: Redefining the Role of the Government in Tomorrow's International Trade 26 – 27 March 2012 Room XVI, *Palais des Nations, Geneva* at 5.
[515] Bergsten CF & Gagnon JE "Currency Manipulation, the US Economy, and the Global Economic Order" (2012) (Number PB 12-25) *Peterson Institute of International Economics* at 1-2. See also Kawa L "The Top 20 Currency manipulators" 11 November 2012 http://www.businessinsider.com/the-top-20-currency-manipulators-in-the-world-2012-11?op=1 (Accessed 02 January 2014).
[516] Proctor C *Mann on the Legal Aspect of Money* 7th Edition 2012 at 606.
[517] *Id* at 607, prefers the second set of the argument which holds that continued use of the peg is no longer necessary since the circumstances warranting its initial introduction have disappeared.

as Proctor asserts, customary international law does not offer grounds upon which a currency peg arrangement can be impugned.[518] In spite of that fact, a fixed peg, although perfectly consistent with the China's obligations in terms of Article IV(2), could be viewed as a violation of the Article XV(4) of the GATT.[519] If it could be proved to be both an export subsidy and an import charge, then it could be subject to a challenge in terms of the WTO Agreement on Subsidies and Countervailing Measures (ASCM).[520] Providing the proof is one of those colossal burdens upon the one who alleges that the peg is assailable in terms of the WTO law. The precise criteria to determine a currency manipulation is not straight forward. It is however, reasonable to argue that protracted periods of undervalued status may be challenged on the basis of the ASCM. Arguably, short-term undervaluations are not likely to adversely affect other states as much as long-term undervaluations would.[521]

The WTO is, however, not adequately equipped to handle the manipulations, thereby making it difficult to apply the ASCM to deal with the problem.[522] Article XV of the GATT does not refer expressly to currency manipulations but vaguely refers to "exchange action" and "trade action".[523] To stretch its application to cover currency manipulations would be to out-rightly shoehorn the argument. Proctor remarks convincingly that "it therefore seems unlikely that China's currency peg infringes the WTO Agreement on Subsidies and Countervailing Measures."[524]

Competitive devaluations are not new to international law.[525] But why have grievances regarding currency manipulations just taken centre stage in recent years and not before? To hazard an answer, one needs to take cognisance of the fact that at the formulation of GATT rules in the immediate aftermath of the Second World War, the *par value* system still held

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[518] *Id* at *596.*
[519] *Id* at 600-601. Ahn D "Is the Chinese exchange-rate regime "WTO-legal"?" in Evenett S J (ed) *The US-Sino Currency Dispute: New Insights from Economics, A VoxEU.org Report* 2010 at 140.X
[520] Magnus J & Brightbill TC "China's currency regime is legitimately challengeable as a subsidy under ASCM rules" in Evenett S J (ed) *The US-Sino Currency Dispute: New Insights from Economics, A VoxEU.org Report* 2010 at 149. Article 10 of the Agreement on Subsidies and Countervailing Measures (ASCM), read in conjunction with Article VI (3) of the GATT state that, "the term "countervailing duty" shall be understood to mean a special duty levied for the purpose of offsetting any bounty or subsidy bestowed, directly, or indirectly, upon the manufacture, production or export of any merchandise."
[521] De Lima-Campos A & Gil JAG *supra* at 3.
[522] Mattoo A & Subramanian A "Currency Undervaluation and Sovereign Wealth Funds: A New Role for the World Trade Organization" (2008) *World Bank Policy Research Working Paper, no. WPS 4668.* at 10.
[523] *Ibid.*
[524] Proctor C *supra* at 603.
[525] Cohen BJ *Global Monetary Governance* 2008 at 61. See also Auboin M "Fulfilling the Marrakesh Mandate on Coherence: Ten Years of Cooperation between the WTO, IMF and World Bank" (2007) (3) *WTO Discussion Papers* at 4. Lastra RM "The International Monetary Fund in Historical Perspective" (2000) *Journal of International Economic Law* 507-523 at 510.

sway and the prospects of manipulation were not a threat to economic relations.[526] Considering that the WTO system was not designed to regulate and pass verdicts on matters of the exchange rate, it is inconceivable how its dispute mechanisms can be of any help with regards to currency manipulations.[527] Some of the matters being brought before the WTO were initially meant to be handled by the IMF. Admittedly however, a look at the complimentary roles of the two institutions reveals that their jurisdictional boundaries are not cast in stone.[528]

While its prospects of success may seem remote and fanciful, the application of the ASCM measures is still open to the WTO members. In the absence of proper mechanisms to redress the challenge, states would resort to retaliatory[529] measures which would only serve to hurt rather than enhance the economic interaction among the nations. In cases where countervailing measures are applied, the cost of maintaining an undervalued currency is "the right that other WTO Members have to impose countervailing duties to their exports."[530] Punitive retaliations would be the closest remedy available to the agrieved states.

Another matter of great significance in international monetary law is the concept of 'dollarisation.' While a state is free to adopt the currency of another and to use it as its own, a process known as 'dollarisation', it is noteworthy that the state issuing the currency is not completely without a voice regarding the matter.[531] The European System of Central Banks (ESCB)[532] requires a state that expresses an interest to adopt the Euro as its currency to first obtain the consent of the ESCB[533] and must meet certain minimum conditions so as not to jeopardise the functioning of the currency system. This requirement seems reasonable since the use of one state's currency by another definitely has monetary policy implications on the economy of the issuing state. Problems of fiscal indiscipline in the state that adopts another's currency will no doubt affect the issuing state in an adverse way. Although its currency has been adopted by a number of states[534] in a process of dollarisation, the USA

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[526] Waibel M "Retaliating against exchange-rate manipulation under WTO rules" in Evenett S J (ed) *The US-Sino Currency Dispute: New Insights from Economics, A VoxEU.org Report* 2010 at 133.
[527] Ahn D *supra* at 139.
[528] In terms of the IMF-WTO relationship as spelt out by Article XV of the GATT, exchange action and trade action are both to be impugned in so far as they frustrate the ideals of free trade.
[529] Waibel M *supra* at 133-147.
[530] De Lima-Campos A & Gil JAG *supra* at 4.
[531] Proctor C *supra* at 603.
[532] Zimmermann CD "The Concept of Monetary Sovereignty Revisited" (2013) (24) 3 *The European Journal of International Law Vol. 24 no. 3* at 815. Although the European Monetary Union is not so much a 'state' as it is a supranational institution, it is a *sui generis* entity in which state banks are closely intergrated that their identinties are altogether merged.
[533] Proctor C *supra* at 603.
[534] Ecuador, El Savador, Panama, Zimbabwe are some of the states that dollarised in terms of the US Dollar. See Cohen BJ "U.S. Policy on Dollarisation: A Political Analysis" Available at http://www.polsci.ucsb.edu/faculty/cohen/recent/dollarization.html (Accessed on 10 January 2015).

takes a less stringent approach in that it does not directly monitor the states that use its currency.[535] The fact that a state that dollarizes can freely swing to and fro between the monetary systems, freely re-instituting its currency at will,[536] props the argument that dollarization needs to be subject to some degree of regulation particularly by the state issuing the xeno-currency. This is necessary so as to strike a balance between the needs of the issuing state and the needs of the state that adopts the currency of another.

5.6 CONCLUSION

A review of the issues discussed in this chapter raises serious questions about the legitimacy of the constraints on sovereignty. The fact that a state's power to employ corrective measures can be a subject of legal challenges before tribunals even when the state is faced with imminent collapse and a crippling economic situation places the state in an unenviable position. A salient policy question regards how a state's commitment to a stable monetary system based either on exchange controls or fixed exchange rate arrangements can be reconciled to the duty to exercise its monetary powers without hurting other states. The contestations regarding Chinese monetary policy[537] highlight the extent to which national boundaries will no longer provide an effective veil of protection for national policies.

Without doubt, the foregoing discussion reveals that the policy options available to states have been strictly circumscribed through the signing of multilateral and bilateral treaties. The state can no longer "eat its cake and still have it." States will have to exercise a great deal of caution not to violate the promises and obligations they have pledged to other international law subjects.[538] Indeed, monetary sovereignty is subject to numerous constraints and the implications of these constraints are significant both for the creditor and debtor states.

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[535] Proctor C *supra* at 603.

[536] After almost seven years of a "dollarised' monetary system, Zimbabwe seems to have started re-issuing its own currency in the form of "bond coins' amid assertions by its citizens that the state is reviving its currency by hidden means. Coins of denominations 1c, 5c, 10c , 25c, valued at *par* with US cents, went into circulation on 18 December 2014. Business Reporter "RBZ to unveil 'special' coins'. Available at www.herald.co.zw/rbz-to-unveil-special-coins/ (Accessed on 17 January 2015). See also Times Live "Zimbabweans suspicious of new 'bond coins'" available at www.timeslive.co.za/africa/2014/12/22/zimbabweans-suspicious-of-new-bond-coins (Accessed on 17 January 2015).

[537] Evenett Simon J (ed). *The US-Sino Currency Dispute: New Insights from Economics* 2010.

[538] Commitments in terms of the IMF, GATS, GATT, regional agreements as well as BITs play a significant role in limiting the powers of the state.

CHAPTER 6

6 SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

6.1 INTRODUCTION

Having considered the scope of monetary sovereignty, the challenges associated with its application as well as the implications of its limitations to international economic law, it is appropriate at this point to make a summary of the main observations made by the study as well to make recommendations regarding how to handle the divergent interests of the various international legal persons. The legal rights and obligations of states, investors and traders sometimes clash openly in as far as monetary sovereignty is concerned.[539] Each of the interest groups has some vested interests the protection of which lies at the heart of international monetary law. As the last chapter of the study, it is appropriate that the chapter wraps up the discussion by presenting recommendations.

6.2 SUMMARY OF ISSUES AND FINDINGS

The first five chapters dealt with the theoretical issues regarding monetary sovereignty. Firstly, the study identified the problems regarding the regulation of monetary matters in international law. It observed that the ubiquitous nature of cross-border commercial activities has made the need for coordinated monetary regulation an ever present challenge. National economies have become so closely integrated that inter-state co-operation has become an inescapable necessity. Among some of the most salient concerns is the manipulation of municipal monetary systems[540] by state functionaries in order to gain advantage over other states.

Owing to the fact that it is the duty of the state to ensure economic stability, the second chapter considered the role of the state in the conduct of monetary law. The subject of cross-border capital movements in response to the emerging global financial markets remains highly significant. The study revealed the changing role of the state within the international law framework and how it now plays an intermediary[541] role between the needs of its

[539] Refer to the various arbitral disputes discussed in chapter 4 & 5 above.
[540] Thorstensen V, Ramos D & Muller C (2013) 16 (2) "The Missing Link Between the WTO and the IMF" *Journal of International Economic Law* 353–381 at 380.
[541] Kaul I "The Rise of the Intermediary State" in Kaul I and Conceição P *"The New Public Finance: Responding to Global Challenges"* 2006 at 73.

citizenry and the needs of the international community. The emergent paradigms of international monetary regulation[542] were also highlighted in the context of how multiple functional centres interact in a manner that is so distinct and different from the erstwhile patterns in terms of which functional areas were neatly demarcated. The participation of "international organizations, multinational corporations, regions, local communities and the civil society"[543] in the exercise of monetary regulation has resulted in a diffusion of sovereignty much because of the centripetal and centrifugal forces acting against it.[544]

The third chapter focused on the scope and incidences of monetary sovereignty in the context of the need to deploy appropriate corrective measures while the state carries out macro-economic regulatory functions. It was highlighted that states periodically invoke sovereignty in order to correct disorders affecting national economies.[545] The numerous attributes of sovereignty were highlighted with much elaboration, delineating the scope of the operation of the state where traditional notions are still in operation. An acknowledgement of the dynamic nature of international law however highlights the extent to which states currently remain with residual sovereignty.[546] A proper understanding of the normative[547] and positive attributes of sovereignty is useful to the extent that it contextualizes the power of the state at an appropriate locus within the time spectrum. While the normative attributes illuminate what sovereignty should mean both in conceptualisation and application, its positive attributes encapsulate what actual rights, duties and rules to look for when applying the concept of sovereignty to a particular legal problem.[548]

Proctor aptly captures the positive attributes of monetary sovereignty when he writes that:

> "The municipal legislator is free to define the currency of his country, to decide whether or not it should be pegged to another currency, to determine the means by which monetary and exchange rate policies are to be defined and implemented, to devalue or revalue the currency, to allow or prohibit the use of foreign currencies within its borders, to impose exchange controls, or to take other measures affecting monetary relations."[549]

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[542] Refer to paragraph 2.7 of this study.
[543] Lastra RM *Legal Foundations of International Monetary Stability* 2006 at 26-27.
[544] *Id* at 26.
[545] Shuster M R *The Public International Law of Money* 1973 at 317.
[546] In the case of *Pringle v The Government of Ireland* (2012) 10 JIC 1901 at 20, 'residual sovereignty' is perceived in relation to powers as "those which have not in the meantime been limited by virtue in particular of what is now Title V of the TEU and the Union's external action powers."
[547] Zimmermann CD "The Concept of Monetary Sovereignty Revisited" (2013) 24 (3) *European Journal of International Law* 797–818 at 805.
[548] *Ibid.*
[549] Proctor C *Mann on the Legal Aspect of Money* 7th Edition 2012 at 526-527.

In the absence of any constraining factors, the positive attributes of sovereignty give the concept such a wide scope that state powers as against external entities would be almost totalitarian. For this reason, the juridical constraints operating against unlimited sovereignty were the focus of the fourth chapter.

The chapter identified the constraints within the framework of an inter-play between national and international interests. One of the conspicuous observations is that monetary sovereignty still occupies an important part of international economic relations.[550] The reality of its severe curtailment through the application of customary law principles as well as treaty provisions is however strongly admitted.[551] The operative effect of treaties is particularly outstanding so much as the different treaty regimes spell out some boundaries of state power previously unknown in terms of customary international law. The constraint on the power of the state to impose current payments restrictions is a novelty that was introduced by treaty provisions.[552]

States have seriously curtailed their monetary sovereignty through participation in multilateral institutions such as the IMF and the WTO. Their powers have also been significantly narrowed in this regard by the conclusion of BITs and other International Investment Agreements (IIA). The effects of the IMF provisions such as Article VIII (2), dealing with international current transactions and Article VI dealing with capital transactions are to say the least exacting. While the latter leaves the states with great latitude in dealing with capital transactions, the controversy as regards transfer of capital remains topical.[553]

Meanwhile, the GATT regime does not directly limit the rights of states to maintain capital controls. Instead, the use of controls is subject to the IMF regime as well as commitments negotiated in terms of the GATS Agreement.[554] There is an important provision within the GATT Agreement which provides a vital bridge between the IMF and the WTO legal regimes.[555] Article XV (4) provides a neat tie between the two systems by stating that;

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[550] Zimmermann CD *supra* at 814.
[551] *Zuk Claim* United States Foreign Claims Settlement Commission *International Law Reports* Vol. 26 (1958) II at 285.
[552] Article VIII(2)a of the IMF Articles of Agreement.
[553] Cohen BJ *Global Monetary Governance* 2008 at 174-185. Stiglitz JE "Capital-Market Liberalisation, Globalisation, and the IMF" (2004) Vol 20 (1) *Oxford Review of Economic Policy* at 58.
[554] Article XI of GATS, particularly footnote 8.
[555] Siegel DE "Legal Aspects of the IMF/WTO Relationship; The Fund's Articles of Agreement and the WTO Agreements" (2002) 96 *The American Journal of International Law* at 563.

> "Contracting parties shall not, by exchange action, frustrate the intent of the provisions of this Agreement, nor, by trade action, the intent of the provisions of the Articles of Agreement of the International Monetary Fund."[556]

The complimentary functions of the two systems are vividly expressed in the legal text in a way that reveals how the different institutions of international law function in such a way as to attain the same goals.[557] The WTO system also limits sovereignty through the application of schedules of commitments in terms of Article XI of the GATS. Since the schedules are drawn through the negotiations voluntarily undertaken by each individual state, the constraints are not externally imposed by the WTO on the member. Each contracting party to the GATS agreement voluntarily assumes them. The liberalisation of the monetary transfers and payments regarding trade in goods and services has been achieved through these multilateral regimes. Due to the ever increasing significance of foreign direct investment[558] as well as short term investments, it has progressively become difficult to discuss the limitations of sovereignty without reference to investment law.

The protection of investment is subject to BITs and IIAs and though the liberalisation provisions apply as between the state parties concerned, their effects tend to be drastic. The IMF system, unlike BITs and IIAs, is indeed modest in its constraints on monetary sovereignty.[559]

While the argument in favour of capital account liberalisation used to be stronger than the argument against it, there has been a significant shift with regards to the burden of proof, from the anti-liberalisation to the pro-liberalisation camp.[560] The anti-liberalisation camp has revealed the vast differences that exist between the natures of current and capital transactions.[561] The East-Asia crisis of 1997-1998, the crisis in Argentina at the beginning of this millennium as well the global crisis that began at 2007[562] are some of the events that have clearly highlighted the need for the deployment of capital controls in stabilising the

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[556] Article XV (4) of the GATT.
[557] Thorstensen V, Ramos D and Muller C *supra* at 355.
[558] Spears SA *supra* at 1027. See also UNCTAD *World Investment Report* 2014 at 114 according to which the total number of agreements went to up to 3 236 by the end of 2013.
[559] Proctor C *Mann on the Legal Aspect Money* 7th Edition 2012 at 618 shows that the terms of BITs are more restrictive of national sovereignty than the IMF does. See also Mann FA *Mann on Money* 5th Edition 1992 at 527.
[560] Ostry J D *et al* "Capital Inflows: The Role of Controls" *IMF Staff Position Note* February 19 2010 SPN/10/04 at 5. Refer also to Hagan S "Enhancing the IMF's Regulatory Authority" (2010) (13(3) *Journal of International Economic Law* 955–968 at 966.
[561] Lichtenstein CC "International Jurisdiction Over International Capital Flows and the Role of the IMF: Plus Ca Change …" in Giovanoli M (ed) *International Monetary Law: Issues for the New Millenium* 2000 at 78.
[562] Gari G "GATS Disciplines on Capital Transfers and Short-term Capital Inflows: Time for Change?" (2014) 17 *Journal of International Economic Law* 399–435 at 400.

monetary system. They also illustrate the ongoing relevance of capital controls as a significant corrective measure. Moreover, the prevailing debate[563] among economic theorists regarding the benefits of capital account liberalisation render it too risky to call for unrestricted liberalisation of capital flows.

As such, the legal position with regards to current account liberalisation is clear while the same is not true for the capital account. It is that asymmetry[564] which creates uncertainty and for which a speedy resolution is requisite. One writer sums it up by saying;

> "For all of these reasons, the asymmetry in the IMF mandate over current and capital account issues should be overcome. This entails broadening the IMF competences on capital movements: the Fund should play a more active role not only overseeing capital flows through its bilateral and multilateral surveillance, but also establishing a multilateral code of good conduct on capital account liberalization."[565]

The fifth chapter gave an exposition of the implications of the juridical constraints to international economic law. It saw an application of the theoretical issues covered in the first four chapters to certain concrete situations so as to give an exposition of how restrictive treaty provisions apply in real dispute scenarios.

This highlights the practical consequences of the constraints on sovereignty as well as the problems that emerge as a result of the legal developments. The BITs and multilateral regimes have caused a significantly notable impact in terms of limiting the policy space for the states.[566] One of the effects is to limit the ability of the states to adjust their economies in the face of rigid terms imposed in terms of the legal regimes.[567] Some BITs' provisions have opened up floodgates of litigation against states through elaborate arbitration procedures.[568] Even though such procedures do not eliminate sovereignty, they do restrict it in a substantial way so as not to defeat legitimate claims by investors. To the extent that the priviledge of the state to raise a defence of sovereignty before a tribunal[569] is limited, its powers will not be used to frustrate legitimate contractual claims.

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[563] Cohen BJ *Global Monetary Governance* 2008 at 178.
[564] Viterbo A *International Economic Law And Monetary Measures: Limitations to States' Sovereignty and Dispute Settlement* 2012 at 151.
[565] *Id* at 196.
[566] Karl J *supra* at 232.
[567] Kelsey J *supra* at 846.
[568] US-Argerntina BIT 1991.
[569] Picciotto S *Regulating Global Corporate Capitalism* 2011 at 184.

6.3 SUMMARY OF CONCLUSIONS

The concept of monetary sovereignty still occupies a very important place in international law[570] as states play an important function in monetary regulation. However, in their pursuit of national objectives they can no longer act in isolation.[571] Their survival has become so entwined with that of others such that co-operation has become the mainstay of the exercise of power.[572] As a result there has been a strengthening of international institutions geared towards the regulation of inter-state economic activities.[573] However, the proliferation of arbitral prceedings in recent years has also altered the way states perceive their international law obligations. Some states have begun to revise[574] or withdraw from IIAs and yet still others adopt clauses that limit the jurisdiction of the ICSID.[575] Withdrawal and revision are two sides of the same coin, designed to achieve the same objectives. The idea is to enable the states to negotiate treaties for more favourable terms so as to allow them enough leeway to carry out their regulatory functions without fear of being hauled before arbitral tribunals.[576]

The contours of monetary sovereignty have somehow shifted. Its attributes apply differently and even their level of curtailment is not the same. While state power remains unchallenged in respect of such aspects as the power to determine the name of the monetary unit, the monetary standard, the adoption of the currency of another state in a process of dollarisation, the power of the state is more restricted in respect of other attributes.[577] As this study has revealed, the Republic of China's right to peg its currency against the US Dollar has been a subject of great debate and scrutiny[578] in spite of it being a clear exercise of monetary sovereignty. The subject of current account convertibility is regulated in terms of Article VIII(2)a of the IMF which clearly states that a member state requires the approval of the IMF before it can impose restrictions on current transactions. Meanwhile the regulation of capital movements is not as strictly harmonized as that of the current transactions. The

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[570] Zimmermann CD "The Concept of Monetary Sovereignty Revisited" (2013) 24 *Journal of International Economic Law* 797–818 at 818.
[571] Petersmann EU "Multilevel Governance Problems of the World Trading System beyond the WTO Conference at Bali 2013 (2014) (17) *Journal of International Economic Law* 233–270 at 267-268.
[572] *Ibid.*
[573] Institutions such as the IMF are constantly reviewing themselves and considering whether to make any adjustments to their regulatory functions. Continous research and policy papers are a sign of constant self evaluation. See Ostry J D *et al* "Capital Inflows: The Role of Controls" *IMF Staff Position Note* February 19 2010 SPN/10/04.
[574] Spears SA *supra at 1051* refers to a revision of the US-Canada BIT.
[575] UNCTAD *World Investment Report* 2010 at 85.
[576] UNCTAD *ibid.* Spears SA *supra* at 1043. Spears observes that renegotiating the terms has, among others, the objective of limiting the jurisdiction of tribunals such as the ICSID.
[577] See for instance the debate on exchange rate manipulation in the foregoing discussion.
[578] Evenett SJ (ed) *The US-Sino Currency Dispute: New Insights from Economics, A VoxEU.org Report* 2010.

regulatory asymmetry[579] between current and capital accounts creates uncertainties for economic actors. Currency manipulations are a kind of a thorn in the flesh for international monetary law. Neither the IMF nor the WTO system are sufficiently designed to single handledly deal with currency manipulation disputes.

The distinction between private and public international law is somehow getting blurred as more and more private parties are taking to arbitration tribunals[580] without having to rely on their home countries[581] to pursue the cases on their behalf. Arbitration tribunals are being convened in terms of UNICITRAL rules, ICSID rules or the Arbitration Institute of the Stockholm Chamber of Commerce rules. With some of the investment treaties[582] being heavily oriented towards a greater protection of investors at the expense of citizens, it has become increasingly important for states to carefully weigh the benefits of the treaties against the cost to national sovereignty.[583]

In summary, the study identified problems such as the inordinate protection of investments which in some cases leads to a harassment of states by the investors taking advantage of investor friendly bilateral and free trade agreements. The problem is further compounded by a lack of an general international investment agreement to harmonise the terms and conditions for the acceptance of direct foreign investment.[584] Problems such as the 'catastrophic collapse'[585] of currencies also do occur from time to time with devastating effects. There is also an issue of currency manipulations by some states while asymmetric regulatory regimes for current and capital transactions pose a serious challenge to the liberalisation of the economic space. It is in light of these observations that the next segment makes recommendations for dealing with the problems identified.

[579] Viterbo A *International Economic Law and Monetary Measures: Limitations to State Sovereignty and Dispute Settlement* 2012 at 196.
[580] Karl J "International Investment Arbitration: A threat to State Sovereignty?" in Shan W, Simmons P and Singh D (eds) *Redefining Sovereignty in International Economic Law* 2008 at 232.
[581] Until the recent turn to international arbitration, diplomatic intervention was the means that foreign investors had for the protection of their rights. The application of the *'Calvo doctrine'* also meant that investors did not necessarily enjoy greater protection than nationals.
[582] The US-Argentina BIT of 1991 was largely invoked by investors in numerous arbitral cases against Argentina following the 2000-2001 crisis.
[583] Spears SA *supra* at 1042.
[584] The initiative to form a multilateral investment agreement went into a disarray in 1998 following the resistance against the OECD initiated discussions.
[585] Proctor C *supra* at 638-639.

6.4 RECOMMENDATIONS

Capital importing states, which have been harassed by massive investment claims[586] such as Argentina, should consider re-negotiating the investment agreements so to avoid continued exposure to risk of litigation by foreign investors at the expense of the protection of the state. To the extent that states end up with restricted policy space due to restrictive agreements, it is imperative to revise the treaties so as to moderate those terms that are unfriendly to the pursuit of essential state duties.[587] A level playing field is requisite in international monetary law so that the interests of less developed states are protected from domination by large corporate interests expressing themselves through the powerful political voices of the developed capital exporting countries. The revision of treaties can lead to an adoption of techniques ranging from exception clauses,[588] interpretative clauses,[589] as well as preambular language[590] that incorporates other treaty objectives besides the protection and promotion of investments.[591] Revising the terms of the treaties will strike a balance between the interests of foreign investors and the regulatory duties of the sovereign states.

Considering the decline in the popularity of the 'Calvo doctrine'[592], the mention of which is in itself superflous, it nevertheless remains appropriate to state that it was an effective device to guarantee the rights of the foreign traders without necessarily restricting the sovereignty of the host states. The arguments made against its application have, however, been so strong as to lead to its total rejection in the crafting of international agreements.[593] The US-Argentine BIT clearly excluded the 'Calvo doctrine' and that was a major milestone for

[586] Argentina is one such state which has been hauled before arbitration tribunals for investment claims. The US model BIT seems too harsh on their capital importing partners. Initiatives to block the signing of the Trans-Pacific Partnership Agreement are based on a realisation that the treaties that are designed to favour capital exporting countries are burdensome to their capital importing partners. See also Kelsey J "Why you should join the TTPA Action on 08 November" available at http://thedailyblog.co.nz/2014/10/20/why-you-should-join-the-tppa-action-on-8-november/ (Accessed 23 December 2014).

[587] UNCTAD *World Investment Report* 2010 at 85.

[588] Spears SA supra at 1059 shows that the purpose of an exception clause is to "exempt a contracting party from the obligations of the treaty in situations in which compliance would be incompatible with key policy objectives explicitly identified in the agreement."

[589] Spears SA *supra* at 1044 defines intepretative clauses as "statements that refine the principal investment disciplines to ensure that they are not interpreted so expansively as to prohibit host states from pursuing legitimate non-investment policy objectives."

[590] Preambles state the values and the objectives of the treaty. Recent treaties have adopted preambular language that espouses the ideas of the 'chastened liberalism' rather than the core ideas of the 'neo-liberal' dispensation of the 1980s and 1990s which tended to clip the proverbial 'wings' of the sovereigns. See Spears SA *supra* at 1058.

[591] Spears SA *supra* at 1075.

[592] In terms of the 'Calvo Doctrine', the rights of investors are governed by the laws of the host state and the foreign investors should not expect more favourable treatment than that afforded the locals. Refer to Picciotto S *Regulating Global Corporate Capitalism* 2011 at 158.

[593] For a detailed discussion of the 'Calvo Doctrine' is refer to 4.3.2 above.

international investment law.[594] Its exclusion therefore marked a departure from an established norm associated with Latin America.

It is imperative therefore for states to exercise more caution when signing BITs and other FTAs by avoiding treaty clauses that might bind them to the point of frustrating their power to adopt corrective measures in time of crippling economic crisis.[595] Treaty clauses which restrict the ability of the states to adjust their economic situations through the use of capital controls, alteration of parity between currencies, the imposition of restrictions on current payments among others are restrictive of the exercise of sovereignty. In recent years, there has been a growing tendency to include other objectives besides the protection of investments. Sustainable development has come up as one of those objectives being protected by the treaties.[596]

An imminent need for a favourable multilateral investment treaty was noted in the late 1990s but the collapse of the OECD sponsored Multilateral Agreement on Investments (MAI) in 1998[597] dealt a heavy blow to the initiative of creating an institution with global jurisdiction on matters of foreign direct investment. Yet, in light of the discrepancies among countries as regards the applicable investment treatment standards, it may be necessary to revisit the idea of such an organisation with the idea of bringing about uniformity[598] while at the same time ensuring greater latitude of policy space for the sovereigns concerned.

Since it is possible for the currency of a state to collapse with 'catastrophic' effects, and there being no international law duty for the debtor state to revalorise its money, contracting parties need to adopt value maintenance clauses while negotiating treaties.[599] A state that fails to negotiate for such clauses practically assumes the risks associated with the catastrophic depreciation of the currency of the other contracting party.[600] It is arguably logical that cases of catastrophic devaluations, in cases where states are debtors, should be

[594] Arnold Kantor "Letter of submittal to the President of the United States: The Treaty between the United States of America and the Argentine Republic concerning the Protection of Investment 14 November 1991. Available at http://2001-2009.state.gov/documents/organization/43475.pdf (Accessed 11 January 2015). The doctrine had originated in Argentina and its rejection in that state marked a fundamental departure that concomitantly spelt its demise.
[595] Spears SA *supra* at 1066.
[596] UNCTAD *World Investment Report* 2014 at 116.
[597] Neumayer E "Multilteral Agreement on Investment: Lessons for the WTO from the failed OECD-negotiations" (1999) (46) 6 *Wirtschaftspolitische Blätter* at 1. Available at http://www.lse.ac.uk/geographyAndEnvironment/whosWho/profiles/neumayer/pdf/Article%20in%20WiPo.pdf (Accessed on 17 January 2015).
[598] *Ibid.* Following the collapse of the negotiations for a Multilateral Agreement on Investment, and in light of the serious encroachment of BITs into the monetary sovereignty of states, it seems plausible to set minimum standards for model BITs.
[599] Proctor C *supra* at 639.
[600] *Ibid.*

distinguished from those where they are not. More accountability must be demanded in cases where the state is a debtor, and more so where bad faith[601] can be inferred.

With regards to exchange rate and currency manipulations, in light of the attendant weaknesses of the IMF and the GATT in dealing with the challenges, it seems a plausible alternative to strengthen the collaborative functions between the two global institutions.[602] While the idea of creating another institution altogether may seem reasonable, it is the sustained proposition of this study that a proliferation of institutions is not necessarily to be desired. Rather, an amendment to Article XV(4) of the GATT so as to equip it with more competencies in unambiguous terms will enable the organisation to effectively deal with the currency manipulations.[603] It is equally important to remember, however, that the amendments need to take cognisance of the role of the IMF so as to avoid a takeover of the IMF jurisdiction by the WTO.

The tribunals that have been instrumental in carrying out arbitral functions have been subject to a great deal of denunciation.[604] They are mostly *ad hoc* in nature.[605] Initially, they were meant to serve private interests and their adequacy in dealing with issues that touch upon the sovereign prerogatives of nations is itself a highly controversial matter. There is great merit in the argument that:

> "Vesting investor-state tribunals with the power to consider states' non-investment policy objectives and to balance them against states' investment policy objectives will place great responsibility on arbitrators to refine the substantive standards in IIAs and to pass judgment on host-states' public policy measures."[606]

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[601] Proctor C *supra* at 639 indicates that it is not in all cases of depreciation that bad faith is an element.

[602] Siegel DE "Legal Aspects of the IMF/WTO Relationship: The Fund's Articles of Agreement and the WTO Agreements" (2002) 96 *The American Journal of International Law* at 567-568.

[603] Mattoo A & Subramanian A "Currency Undervaluation and Sovereign Wealth Funds: A New Role for the World Trade Organization" (2008) *World Bank Policy Research Working Paper, no. WPS 4668* at 10 say that Article XV(4) "is too vague an obligation to provide a basis for effective regulation.

[604] Spears SA *supra* at 1065-1066. See Alvarez JE & Khamsi K "The Argentine Crisis and Foreign Investors: A Glimpse into the Heart of the Investment Regime" in Karl P Sauvant (ed) *The Yearbook on International Investment Law and Policy 2008/2009* at 383-384.

[605] Picciotto S *Regulating Global Corporate Capitalism* 2011 at 190 says that: "This is at the root of its problematic features: ad hoc arbitrators chosen by the parties; secrecy of proceedings; divergences of interpretation between different tribunals; and above all lawyers who tout for business both to represent clients and for appointment as arbitrators, creating blatant conflicts of interest."

[606] Spears SA *supra* at 1072.

In the absence of an appellate body, the arbitral system leaves a lot to be desired. It is to be admitted though that institutions such as the Annulment Committee[607] of the ICSID do play a balancing role as far as procedural matters are concerned. It is appropriate at this point to sound a reminder that the procedural matters regarding the arbitral institutions are outside the scope of this study and as such it suffices to mention that the system has had a great impact on the way monetary obligations are viewed within the BIT system.

It is important for the quasi-judicial institutions interpreting the monetary and other international treaty provisions to take deference towards the sovereign duty to regulate.[608] It is of critical importance to apply judicial deference so as to reconcile the demands of investors with the expectations of national law.[609] It is equally important to balance the principle of 'deference'[610] with the doctrine of 'effectiveness' which protects the objectives of a treaty from being defeated due to an unfriendly interpretations.[611] The application of deference is necessitated by the need to balance the competing interests as Petersmann argues:

> "The legitimate diversity and competing conceptions of 'principles of justice' justify judicial deference via-a`-vis diverse conceptions of human rights, economic cosmopolitan rights, corresponding 'duties to protect' and 'corporate responsibilities' as relevant context for interpreting IEL."[612]

Having observed the need for balancing the interests of investors with the regulatory duties of the state, an element which has been missing in most arbitral cases, it is imperative for tribunals to show a greater level of deference towards state interests. As far as deference is concerned, Henckels says:

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[607] An ICSID annulment Committee is an *ad hoc* committee convened in terms of Article 53 of the ICSID convention. Though it is not an appellate body for tribunal decisions, it may overturn a tribunal decision if certain grounds exist upon which a nullification of the result seems justified.

[608] Spears SA *supra* at 1048. Petersmann EU "JIEL Debate: Methodological Pluralism and its Criticism in International Economic Law Research" (2012) 15 (4) *Journal of International Economic Law* 921-970 at 839. In applying the judicial 'deference principle' in arbitration requires the tribunal would to adopt an interpretation that is favourable towards the sovereign duty to regulate and provide for the needs of the citizens. Lennard M "Navigating by the Stars: Interpreting WTO Agreements" (2002) (5) 1 *Journal of International Economic Law* at 62.

[609] Petersmann EU "Judging Judges: From Principal-Agent 'Theory' to 'Constitutional Justice in Multilevel 'Judicial Governance' of Economic Cooperation Among Citizens" (2008) (11) 4 *Journal of International Economic Law* 827–884 at 842.

[610] Lennard M *supra* at 88. See also Larouer CJ "In the Name of Sovereignty? The Battle over *In Dubio Mitius* Inside and Outside the Courts" (2009) *Cornell Law Library* at 1&6. In terms of the '*in dubio mitius'* principle, if a term is ambiguous, a less onerous meaning is to be prefered so as not to overly burden the party assuming the obligation.

[611] Lennard M *supra* at 88.

[612] Petersmann EU "JIEL Debate: Methodological Pluralism and its Criticism in International Economic Law Research" (2012) 15 (4) *Journal of International Economic Law* 921-970 at 921.

> "Investment tribunals should be more deferential in performing proportionality analysis, mindful of host state authorities' greater democratic legitimacy and proximity to host state communities, and tribunals' comparatively weak institutional capacity."[613]

Deference, as an adjudicative tool complements other usefull devices such as the exception clauses, interpretive clauses as well as linguistic devices being used in the recently developed model treaties.[614] The revision of the treaties, leading to an adoption of clauses that magnify other objectives besides the promotion and protection of investments certainly goes a long way in rehabilitating monetary sovereignty particularly in cases where BIT terms have caused so much erosion.

In light of the issues raised in the foregoing discussion, a combination of tools and devices would be helpful in mitigating the effects of the juridical constraints on monetary sovereignty. A harmonisation of the global institutions and an adjustment of some of the previously popular approaches are necessary steps required to address the needs of states while at the same time protecting the monetary interests of the traders and investors.

[613] Henckels C "Indirect Expropriations and the Right to Regulate: Revising Proportionality Analysis and the Standard of Review in Investor-State Arbitration " (2012) (15) 1 *Journal of International Economic Law* 223–255 at 223.
[614] Spears SA *supra* at 1060-1062.

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