Law Trove

Complete International Law: Text, Cases, and Materials (2nd edn)

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18. International economic law

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Learning objectives

This chapter will help you to:

- learn about the development of international economic law (IEL);
- understand the nature of IEL;
- appreciate the role of public international law in regulating economic relations among States; and
- study the role of the General Agreement on Tariffs and Trade (GATT) and the World Trade Organization (WTO), the International Monetary Fund (IMF), and the World Bank in regulating the international economy.

(p. 665) Introduction

International economic law (IEL) is a generic term used to describe the international regulation of economic relations amongst States. IEL governs not the 'economics' of individual States as such, but the economic *relations* of States. It regulates international trade by establishing common standards and rules towards ensuring the global economic health of nations. This chapter studies IEL as a distinct topic within public international law focusing mainly on the regulatory aspects of IEL, and its characteristics. The chapter discusses the institutions for regulating world economics, such as General Agreement on Trade and Tariffs (GATT) and the World Trade Organization (WTO), the International Monetary Fund (IMF), the rules of which—together with those of GATT/WTO—form the crux of IEL.

18.1 The origins and nature of international economic law

The international regulation of economics is a fairly recent phenomenon and emerged only after the Second World War. That does not mean, however, that there was no international trading before this period. Prior to the Second World War, States interacted with one another in matters of trade and economics; they conducted international commercial transactions and devised various mechanisms for engaging with one another commercially. Monies and various other forms of legal tender moved amongst States.

However, one major feature of this period was that individual States were wholly responsible for setting standards and rules that governed their commercial interactions with one another, although such rules were often negotiated and agreed between trading partners. In other words, most commercial rules at that time were bilateral in nature. There was neither international legal regulation of how States traded, nor any international regulating mechanisms for that matter.

In 'The international monetary system: a look back over seven decades' (2010) 13 J Int'l Econ L 575, 576, Andreas Lowenfeld notes that:

> It would not be accurate to say that before 1945 there was no international monetary system. States and their enterprises traded with one another, currencies were exchanged, and states held monetary reserves in gold, in silver, and in foreign currencies. But prior to the end of the World War II no international legal regime governed the conduct of states with respect to monetary affairs.

The absolute control that States had over the regulation of their economies and trading before the Second World War was facilitated by the common understanding of world economics by the major Western States. Countries, such as the UK, USA, Germany, and France, accepted

gold as the universal commodity to which they linked their currencies. After all, crude oil, perhaps the most important natural resource today, had not yet acquired the status that it currently enjoys. Thus Western States fixed the price of gold and linked the fate of their national currencies to its well-being. The consequence of this was a stable and predictable market (p. 666) and international economy. In a world of great stability and relative economic prosperity, this economic system was highly desirable.

The Second World War devastated most Western economies and shattered their economic system. This compelled a rethinking of how to conduct global economy and trading. During the war many States—particularly Nazi Germany—pursued aggressive policies of fixing gold prices. This badly affected the stability of gold as a result of which all economies that depended on gold suffered greatly. Shortly before the war ended, other major Western States started to consider how better to regulate international trade. They primarily focused on establishing an effective international monetary system that would be shielded from the manipulations and misdeeds of individual States.

The result of several conferences and negotiations, which took place in 1944 at Bretton Woods, New Hampshire, in the USA, was the establishment of the International Monetary Fund (IMF), which was mainly concerned with regulating the international currency. It was not until 1947, two years after the creation of the United Nations, that GATT, the first international mechanism to regulate international trade, would emerge. GATT laid the foundation of IEL, which would be consolidated by the more inclusive and powerful WTO when it replaced GATT in 1995 (see later).

According to Curtis Reitz, 'Enforcement of the General Agreement on Tariffs and Trade' (1996) 17 U Penn J Int'l Econ L 555:

> An important new field of international law, known today as 'international economic law', has emerged and taken form. Although the fundamentals of international economic law have existed for at least half a century, the modern international law system stands at a critical juncture.

Generally speaking, IEL can broadly be divided into 'regulatory' and 'transactional' aspects. According to John Jackson, 'Global economics and international economic law' (1998) 1(I) J Int'l Econ L 1, 9:

> Transactional IEL refers to transactions carried out in the context of international trade or economic activities, and focuses on the way mostly private entrepreneurs or other parties carry out their activity…Regulatory IEL, however, emphasizes the role of government institutions (national, local, or international).

Both aspects of IEL are undoubtedly significant and merit considerable attention. However, as John Jackson has noted (ibid.):

> Although it can be argued that the 'international trade transactions is the most government regulated of all private economic transactions...in today's world the real challenges for understanding IEL and its impact on governments and private citizens' lives, suggests a focus on IEL as 'regulatory laws'.

Key points

- International trading existed before the Second World War, but there was no international regulation of such trading until after the war. Thus 'international economic law' properly so called only existed after the Second World War.
- The stark realization during the Second World War that entrusting individual States with the responsibility of regulating their economies was sufficient to safeguard the health of global economics and trading inspired the emergence of IEL.
- IEL can be categorized as transactional or regulatory. However, it is with the regulatory aspect of IEL that international law is mostly concerned.

(p. 667) 18.2 International economic law and public international law

IEL is widely considered today as a public international law field, but its status as such has not been as long established as that of human rights, criminal law, or even environmental law. This was because for a long time international law did not concern itself with regulating economics. However, not only is IEL now a bona fide theme of public international law; it has also been said to belong to private international law—that is, the conflict of laws—in some regards.

Thomas Cottier, 'Challenges ahead in international economic law' (2009) 12(I) J Int'l Econ L 3, observes that:

> Since the conclusion of the Uruguay Round of multilateral trade negotiation and the entry into force of the WTO Agreements in 1995, international economic law has witnessed an unprecedented emphasis on trade regulation. The field has moved centre stage in public international law...The many linkages to other fields, in particular, environmental law, human rights, culture and many others, have broadened perspectives and assisted in the process of bringing trade regulation fully into the realm of public international law.

In fact, John Jackson (1998, see section 18.1), at 8, has gone as far as to state that:

> Indeed, it is plausible to suggest that 90 per cent of international law work is in reality international economic law in some form or another.

The rationale for the ultimate engagement of public international law with IEL is to be found in the realization by States and scholars that the law—and in particular international law—has a special role to play in States' economic relations. Economists use theoretical postulations and forecasting to 'regulate' economics, but leaving international economics to be regulated solely by market forces is fraught with many dangers. Law, therefore brings to bear on economics concrete rules and regulation, which economic predictions and theories often lack.

Unlike economics, the particular strength of law derives from experience, not logic or predictions.

As the famous American judge, Oliver Wendell Holmes, once pronounced, in the first of the twelve Lowell lectures delivered on 23 November 1880 (available at http://www.infoplease.com/cig/supreme-court/oliver-wendell-holmes-1902-1932.html):

> The life of the law has not been logic; it has been experience. The felt necessities of the time, the prevalent moral and political theories, intuitions of public policy, avowed or unconscious, even the prejudices which judges share with their fellow men, have had a good deal more to do than the syllogism in determining the rules by which men should be governed. The law embodies the story of a nation's development through many centuries, and it cannot be dealt with as if it contained only the axioms and corollaries of a book of mathematics.

If we adapt this statement to the present subject matter, we can say that the regulation of international economics by international law is a *necessity* dictated today by the present realities of economic relations among States. The strength of such legal regime derives not from simple theoretical formulations or logic, but from the series of events, experiences, and activities, all of which affect the economic well-being of States and people.

(p. 668) The relationship of IEL with public international law can, however, be a very tricky one if not properly handled. There are notable structural differences between States' approach to commerce and international law's approach to regulation and these may often cause friction:

> The very structure of international law and particularly the normal rigidities of treaties and their formation, as well as the intricate links of treaty developments to many constitutional structures, will often create barriers to what some policy makers perceive to be the optimum solutions to problems. (John Jackson, 'International economic law in times that are interesting' (2000) 3 J' Int'l Econ L 3, 5)

It is necessary to balance the international law's regulation of IEL with the constitutional realities of States if we are to achieve the full benefits of international law regulation of economics. Since we have already dealt with the relationship between international law and municipal law in general in Chapter 9, we will not repeat this discussion here.

thinking points

- *What is the relationship between IEL and public international law?*
- *What is the distinction between the transactional aspect and regulatory aspect of IEL, and of what relevance, if any, is this difference as far as the international regulation of IEL is concerned?*
- *Why is public international law important in the regulation of IEL?*

Having dealt with some preliminary issues concerning IEL, let us now consider some specific mechanisms for regulating IEL. We focus here on GATT and the WTO, on the one hand, and the IMF and World Bank, on the other. The combination of GATT and the WTO is what is usually referred to as 'international trade law' (ITL), while the IMF/World Bank angle is known as 'international finance law' (IFL). However, since we discuss both these aspects as elements of IEL and not as trade or finance law per se, we will adopt the term 'institutional mechanisms for regulating IEL' generically for both.

18.3 Institutional mechanisms for regulating international economic law

As noted earlier, the backbone of IEL comprises the institutions established for the purpose of implementing the regime. There exist today several such mechanisms, and most regions of the world now have some kind of authorities and institutions that regulate and coordinate activities within those specific regions. Our focus here is, however, on global institutions as GATT and the WTO, which are the most important international economic regulatory bodies in existence in terms of their significance and status.

(p. 669) 18.3.1 The General Agreement on Tariffs and Trade

As Curtis Reitz (1996, see section 18.1) has noted, at 555, 'The centrepiece of international economic law system is the General Agreement on Tariffs and Trade'.

The main reason for GATT is the desire to reduce governments' ability to impose measures, which either distort or restrain international trade.

As noted by William J. Davey, 'Dispute settlement in GATT' (1987–88) 11 Fordham Int'l LJ 51, 53:

> The basic goal of GATT is to promote free international trade by establishing rules that limit national impediments to trade.

Background

In order to understand how GATT developed, one needs first to appreciate the emergence of the International Trade Organization (ITO), which was originally proposed as the mechanism

for regulating international trade. At the conferences that took place in New York, Geneva, and Havana in 1946, 1947, and 1948, respectively, it was proposed that GATT, which was drafted at those conferences, would establish the ITO as an organization to implement GATT. The Geneva Conference focused on three principal issues: the finalization of the ITO Charter; the negotiation of a multilateral agreement to reduce tariffs; and the drafting of 'general clauses' of obligations relating to tariffs.

However, the USA, which was one of the principal architects of GATT, had not intended the treaty to be implemented by an organization. Thus, for this and many other reasons, with which we need not be concerned here, the US Congress refused to pass the ITO Charter, but passed GATT provisionally by the Protocol of Provisional Application (PPA) in 1948. The fact that most of the agreements on tariffs and the 'general clauses' on obligations relating to tariffs were already well developed within the US system facilitated their incorporation into GATT and the latter's acceptance, even if provisionally, by the US Congress. Indeed GATT would remain a provisional agreement until 1995 when it was replaced by the WTO. However, as a multilateral treaty, it was a force to be reckoned with.

As John Jackson (1998, section 18.1), noted at 17:

> the GATT, which for reasons partly relating to the constitutional structure of the USA had come into 'provisional force', filled the gap left by the ITO failure, and became de facto the major trade treaty and institution for international trade relations and diplomacy.

Dispute resolution under GATT 1947

One of the most remarkable features of GATT was the development of its dispute resolution mechanism. Yet despite its featuring in GATT, dispute resolution is one of the least provided-for elements in the treaty, and those provisions that do exist are, at best, basic and ambiguous.

Article XXIII(1), which is the core of GATT dispute settlement, states that:

> If any contracting party should consider that any benefit accruing to it directly or indirectly under this Agreement is being nullified or impaired or that the attainment of any objective of the Agreement is being impeded as the result of
>
> (p. 670) **(a)** the failure of another contracting party to carry out its obligations under this Agreement, or
> **(b)** the application by another contracting party of any measure, whether or not it conflicts with the provisions of this Agreement, or
> **(c)** the existence of any other situation,
>
> the contracting party may, with a view to the satisfactory adjustment of the matter, make written representations or proposals to the other contracting party or parties which it considers to be concerned. Any contracting party thus approached shall give sympathetic consideration to the representations or proposals made to it.

Clearly, this provision does not entitle any party to GATT to bring a claim for dispute settlement merely on the ground that there has been a violation of GATT obligations; rather, an aggrieved party must show that benefits, which accrue to it under the treaty directly or indirectly, have been 'nullified' or 'impaired'—terms that the Article does not clarify.

The meaning of 'nullification' or 'impairment'

Despite the lack of clarity in Article XXIII(1), case law has shed light on what 'nullification' and 'impairment' mean in the context of GATT.

● ***Report of the Working Party on the Australian Subsidy on Ammonium Sulphate***
GATT/CP.4/39, ADOPTED 3 APRIL 1950, BISD II/188

In 1949, Chile complained that Australia's discontinuance of a policy of parallel subsidies on two competing fertilizer products, as a result of which a subsidy on imported sodium nitrate was removed, whereas domestic ammonium sulphate continued to be subsidized, had nullified or impaired the tariff concession granted by Australia to Chile on sodium nitrate in 1947.

The GATT Working Party concluded:

> that no evidence had been presented to show that the Australian Government had failed to carry out its obligations under the Agreement.

However, the Working Party agreed that the injury that the government of Chile said that it had suffered constituted a nullification or impairment of a benefit accruing to Chile directly or indirectly under GATT Article XXIII:

> if the action of the Australian Government which resulted in upsetting the competitive relationship between sodium nitrate and ammonium sulphate *could not reasonably have been anticipated* by the Chilean Government, taking into consideration all pertinent circumstances and the provisions of the General Agreement, at the time it negotiated for the duty-free binding on sodium nitrate. [Emphasis added]

Clearly, a measure that one party complains constitutes nullification or impairment must not have been reasonably foreseeable by the other party.

● ***Report of the GATT Panel on the Treatment by Germany of Imports of Sardines***

G/26, ADOPTED 31 OCTOBER 1952, BISD 1S/53

The same approach was adopted in a dispute between Germany and Norway, in which the latter had complained, in 1952, that the former imposed tariffs rates, border taxes, and (p. 671) quantitative restrictions on certain types of trade in a manner that nullified or impaired benefits derivable by Norway.

The GATT Panel concluded that:

> no sufficient evidence had been presented to show that the German Government had failed to carry out its obligations under Article I:1 and Article XIII:1.

But the Panel agreed that nullification or impairment in terms of Article XXIII would exist:

> if the action of the German Government, which resulted in upsetting the competitive relationship...could not reasonably have been anticipated by the Norwegian Government at the time it negotiated for tariff reductions...

However, a change in attitude towards the interpretation of 'nullification' and 'impairment' was signalled in 1962 in a dispute involving Uruguay.

● ***Report of the Panel on Uruguay an Recourse to Article XXIII*** L/1923, ADOPTED 16 NOVEMBER 1962, BISD 11S/95

Uruguay had complained that measures taken by some fifteen State parties to GATT, limited marketing opportunities available to them and the failure of the prices of their products to be maintained at a satisfactory level. The Panel considered whether the measures complained about nullified or impaired benefits that accrued to Uruguay under GATT. Following the well-established jurisprudence of the Panel, it held that measures that would constitute nullification or impairment must be seen to affect benefits accruing to parties.

However, in a groundbreaking move, the Panel also considered whether measures not thought to have affected benefits could constitute nullification or impairment.

The Panel held (at [15]) that:

> In cases where there is a clear infringement of the provisions of the General

Agreement, or in other words, where measures are applied in conflict with the provisions of GATT and are not permitted under the terms of the relevant protocol under which the GATT is applied by the contracting party, the action would, *prima facie, constitute a case of nullification or impairment* and would *ipso facto require consideration of whether the circumstances are serious enough to justify the authorization of suspension of concessions or obligations*...*While it is not precluded that a prima facie case of nullification or impairment could arise even if there is no infringement of GATT provisions*, it would be in such cases *incumbent on the country invoking Article XXIII to demonstrate* the grounds and reasons of its invocation. [Emphasis added]

This was a remarkable departure from the previous decisions in many respects. First, it established the possibility of a measure constituting nullification or impairment by the simple fact of its violating the relevant GATT provisions, even if no benefits had been affected. Secondly, such a general violation could be sufficient for contracting parties to authorize the suspension of obligations. Thirdly, the onus is on the party alleging breach to prove grounds invoking Article XXIII. This line of reasoning has been followed by many subsequent decisions.

The procedure for dealing with disputes is provided for by Article XXIII(2) GATT. This Article states that: **(p. 672)**

If no satisfactory adjustment is effected between the contracting parties concerned within a reasonable time...the matter may be referred to the CONTRACTING PARTIES. The CONTRACTING PARTIES shall promptly investigate any matter so referred to them and shall make appropriate recommendations to the contracting parties which they consider to be concerned, or give a ruling on the matter, as appropriate. The CONTRACTING PARTIES may consult with contracting parties, with the Economic and Social Council of the United Nations and with any appropriate inter-governmental organization in cases where they consider such consultation necessary. If the CONTRACTING PARTIES consider that the circumstances are serious enough to justify such action, they may authorize a contracting party or parties to suspend the application to any other contracting party or parties of such concessions or other obligations under this Agreement as they determine to be appropriate in the circumstances. If the application to any contracting party of any concession or other obligation is in fact suspended, that contracting party shall then be free, not later than sixty days after such action is taken, to give written notice to the Executive Secretary to the CONTRACTING PARTIES of its intention to withdraw from this Agreement and such withdrawal shall take effect upon the sixtieth day following the day on which such notice is received by him.

This rather convoluted dispute settlement procedure generated a lot of debate. Some scholars have argued that the provision does not empower legally binding decisions to be taken against defaulting parties, while others argue against such a conclusion. Whatever may be the correct

interpretation, it is interesting to note that whereas the provision of Article XXIII(2) empowers contracting parties to authorize the suspension of concessions or obligations against other parties (which would seem to suggest that the dispute settlement system is, in fact, legally binding), such a step was rarely taken.

Key points

- It is important that a party who wishes to bring a complaint for dispute settlement must show not only that the other party has breached GATT obligations, but also that such a breach has resulted in nullifying or impairing the benefits that accrue to the complainant under GATT.
- 'Nullification or impairment' is usually determined with reference to whether the wrongdoing party could have reasonably foreseen that its actions would have such effect on the complainant.
- In *Uruguay*, the Panel contemplated and established that it was possible for nullification or impairment to result from measures that merely breach GATT obligations. In other words, the complainant does not have to prove that it has suffered loss of benefits. This was a major improvement. But such a complainant must prove the ground for invoking Article XXIII against the other party.
- The whole process under Article XXIII(2) centres on the action of the contracting parties, who could authorize the suspension of obligations in a dispute.

Development in GATT 1947 dispute settlement procedure

Over the years, many developments arose in the GATT dispute settlement process. Initially, a plenary meeting of the contracting parties took place biannually, which considered the disputes submitted. This was later replaced by an intersessional committee made up of the contracting parties, after which a working party was established to look into disputes brought under GATT. (p. 673) In 1955, a new approach was established whereby a panel of experts, established in their own right and not as representatives of their governments, began to deal with disputes.

The utility of Article XXIII GATT as a dispute settlement procedure has been criticized on many fronts. Although there are several such criticisms, the most serious was that the procedure does not establish formal procedures for handling disputes (William Davey, 1987–88, at 57, see earlier in this section).

Consequently, States and scholars began to advocate for a system that could produce judicial-type decisions despite the preference of others for a largely informal conciliatory process. This issue was to be addressed during the GATT Tokyo Round, which took place between 1973 and 1979.

The Tokyo Round culminated in the contracting parties adopting, in November 1979, an Understanding Regarding Notification, Consultation, Dispute Settlement and Surveillance (the Tokyo Understanding). Paragraph 7 of the Understanding provides that:

> The CONTRACTING PARTIES agree that the customary practice of the GATT in the field of dispute settlement, described in the Annex, should be continued in the future, with the improvements set out below. They recognize that the efficient functioning of the system depends on their will to abide by the present understanding. The CONTRACTING PARTIES *reaffirm that the customary practice* includes the procedures for the settlement of disputes between developed and less-developed countries adopted by the CONTRACTING PARTIES in 1966 and that these remain available to less-developed contracting parties wishing to use them. [Emphasis added]

What the Tokyo Understanding basically did was continue the practice of dispute settlement as had already been in existence, although it proposed some improvements. For example, it recognized the conciliation role of the Director General of GATT, even if this role was hardly ever used. The Understanding also improved upon the operation of the panels.

The Tokyo Round faced many problems. The legal status of the document was questioned, because it is neither a treaty of its own accord nor a waiver as provided for in Article XXV(5) GATT. By far the most insurmountable problem of the Tokyo Understanding was with the operation of the panels, especially with regard to the status of its reports on parties' disputes. Usually, the panels submitted their reports to the Council, which acted as a standing body of GATT. It must be pointed out that the Council was not a creation of GATT but rather emerged from practice and the contracting States. The Tokyo Understanding made it possible for the Council then to adopt the reports of the Council by consensus. Thus if one State brought a complaint against another State, the panel prepared a report on the dispute and referred this to the Council. The Council would then, by consensus, adopt the report—that is, it would accept the finding of the panel.

The problem, however, is that adoption of such reports was based on consensus. This means that the State that 'lost' in a dispute would then be able effectively to block the adoption of the panel's report, which would have made some recommendations against it. This was the greatest weakness of the Tokyo Understanding.

As observed by Davey (1987–88, see earlier in this section), at 60:

> A panel report in and of itself has no force. It must first be adopted by the Council on behalf of the contracting parties. Although the issue discussed in the report are not relitigated in the Council, the Council does not usually act absent consensus. Thus, the 'losing' party (at least an **(p. 674)** important losing party) may hold up adoption of a panel report interminably while it purports to analyze it and to explore possible negotiated solutions with the prevailing party.

The wider implication of this system, as Davey further observes (ibid.), at 87, was that:

> The failure of the Council to adopt reports in these cases…undermines the system

because it deprives the panel report of any precedential effect.

That notwithstanding, the Tokyo Understanding did recognize the responsibility that the contracting States have in taking action when it comes to panel reports. Paragraph 21 of the Understanding states that:

> Reports of panels and working parties should be given prompt consideration by the CONTRACTING PARTIES. The CONTRACTING PARTIES should take appropriate action on reports of panels and working parties within a reasonable period of time. If the case is one brought by a less-developed contracting party, such action should be taken in a specially convened meeting, if necessary. In such cases, in considering what appropriate action might be taken the CONTRACTING PARTIES shall take into account not only the trade coverage of measures complained of, but also their impact on the economy of less-developed contracting parties concerned.

The additional obligation that the Understanding imposes on contracting parties enhances this responsibility. Paragraph 22 provides that:

> The CONTRACTING PARTIES shall keep under surveillance any matter on which they have made recommendations or given rulings. If the CONTRACTING PARTIES' recommendations are not implemented within a reasonable period of time, the contracting party bringing the case may ask the CONTRACTING PARTIES to make suitable efforts with a view to finding an appropriate solution.

But despite GATT's progressiveness, none of the decisions that came out of the dispute settlement mechanisms were enforceable:

> Final decisions in favour of complainants are not self-enforcing in any legal system, but enforcement is a particular difficulty in GATT litigation. GATT plenary bodies lack power to enforce their rulings. Compliance or noncompliance is the choice of the nations against whom decisions have been rendered. (Curtis Reitz (1996, see section 18.1), at 570)

Over time, GATT became considerably weakened. Between 1959 and 1978, GATT's dispute settlement mechanism went mostly unused. Several of the criticisms that many States levelled against GATT were to do with its structural and procedural aspects. William Davey (1987–88, see earlier in this section), at 65, summarizes the main criticisms against GATT as being that it:

(a) was inappropriate and ill-conceived because it stressed judicial solutions to problems that were really resolvable only through negotiations;
(b) had become irrelevant because it was not used, except occasionally by the USA, and it was impractical to expand its usage;
(c) was inefficient because of long delays; and
(d) was ineffective because of its inability to ensure implementation of its decisions.

One major weakness of GATT was that it dealt only with trade in goods; it did not cover other economic transactions, which were left to alternative agreements made between States and other areas of IEL. Naturally, because GATT led to a substantial reduction in tariffs on trade—which was its main objective—greater attention became focused on non-tariff measures, which States still used to inhibit competition in trade. GATT did not provide for this and it was (p. 675) also unable to deal effectively with trade measures taken by several governments in respect of their agricultural products.

Consequently, in an attempt to address the failings or flaws of GATT, another round of multilateral trade negotiations was held. Known as the Uruguay Round, it started towards the end of 1986 and finished in 1994. As a treaty, GATT was reformed and, in addition, the WTO was established as its implementing institution.

thinking points

- *What are the most important improvements made by the Tokyo Understanding to GATT dispute settlement procedures?*
- *List the major weaknesses of GATT dispute settlement procedures.*
- *Explain what 'adoption by consensus' means in relation to the GATT dispute settlement process.*
- *Summarize the factors that weakened GATT as a whole.*

18.3.2 The World Trade Organization

Following the Uruguay Round of 1994, GATT came to be regarded as almost two distinct agreements. There is GATT 1947, the original GATT agreement, on which the discussion in the previous section focused, and there is GATT 1994, the product of the Uruguay Round, which substantially changed GATT's approach and framework to many issues. The terms 'GATT 1947' and 'GATT 1994' are commonly adopted in the literature in order to distinguish the two temporal senses in which GATT may be used.

Another major document adopted during the Uruguay Round was the 1994 Understanding on Rules and Procedures Governing the Settlement of Disputes (the Dispute Settlement Understanding, or DSU), which was adopted by an annex to the Agreement. This was to

change the way in which the dispute settlement mechanism worked and will be discussed later in this section.

Furthermore, the 1994 Round produced the WTO as an institutional mechanism for the resolution of all disputes between member States of GATT. The WTO is a major force in the development of an international economy system in general and in international trade in particular.

Donald McRae, 'The WTO in international law: tradition continued or new frontier?' (2000) 3(I) J Int'l Econ L 27, 28, describes the WTO as:

> an international organization. Unlike the GATT, which was somewhat deficient institutionally, the WTO has a range of organs and responsibilities that make it a worthy study in the field of international organizations or international institutional law. Its constitution is a treaty and the legal obligations that apply to members are treaty obligations.

The WTO is governed by a Ministerial Conference and a General Council, which comprise member States. Pursuant to Article III of the Agreement, the WTO administers the 1994 DSU, and the General Council of the WTO is to act as the Dispute Settlement Body (DSB), with its own rules of procedure and chair.

18.3.3 Major improvements under GATT 1994

GATT 1994 improved upon several aspects of GATT 1947 and responded to the many weaknesses of the latter. These specifically relate to coverage and the creation of a more formal, **(p. 676)** robust, and effective dispute settlement procedure. It will be recalled that GATT 1947 dealt only with trade in goods; GATT 1994 broadened this and incorporated trade in services, intellectual property, and some aspects of foreign investments. The implication of this is that all such non-tariff measures that States previously used to inhibit trade, because GATT 1947 did not apply to such, now came under the coverage of GATT 1994. Naturally, this was to enhance the overarching goal of GATT: the constraint of measures taken by governments to inhibit trading.

Judith Hippler Bello, 'The WTO dispute settlement understanding: less is more' (1996) 90 AJIL 416, states that:

> The Agreement Establishing the World Trade Organization (WTO Agreement) dramatically expands and improves the trade rules of the predecessor General Agreement on Tariffs and Trade (GATT), thereby facilitating trade, economic growth and jobs in the increasingly interdependent global economy. Supporters of trade liberalization generally welcome these new rules, including in particular the dramatically improved procedures for settling disputes.

Another major weakness of GATT 1947 was that decisions of its panels regarding disputes

were not self-enforcing. Much depended on the States themselves—that is, on whether they wanted to comply with such decisions—and such decisions could also be avoided where there was no consensus to adopt them. GATT 1994 provides for a system whereby the provisions of GATT can be interpreted at various levels. (We will discuss this further after considering the dispute settlement procedure brought about by GATT 1994.)

Key points

- GATT 1994 modified and strengthened GATT 1947, and established the WTO as its institutional mechanism.
- GATT 1994 made some improvements to the GATT 1947 regime, especially with regard to coverage and dispute settlement procedure. Thus non-tariff measures that previously escaped from GATT 1947 became subject to GATT 1994.

Dispute settlement procedure under GATT 1994

The dispute settlement mechanism under the WTO set out by GATT 1994 is meant to address the many shortcoming of GATT 1947. The mechanism is set out and clarified in the 1994 DSU; it provides for one unified system under both GATT and the WTO, which encompasses the new areas of services and intellectual property, as were agreed at the Uruguay Round, and establishes a new appellate procedure.

The new dispute settlement procedure does not disregard the 1947 mechanism and practice, which it evolved; in fact, the DSU incorporates it. Article III(I) of the 1994 DSU states that:

> Members affirm their adherence to the principles for the management of disputes heretofore applied under Article XXII and Article XXIII of GATT 1947, and the rules and procedures as further elaborated and modified therein.

This provision is important in two respects. First, it demonstrates clearly that GATT 1994 builds on GATT 1947 in all aspects of its functions. Thus GATT 1994 places a high premium on the customary practices of State parties under GATT 1947. Secondly, this reference to GATT 1947 provides some level of continuity to the GATT system, as well as assuring State parties that the new dispensation recognizes all of the hard work that went into the old regime.

(p. 677) For the first time, the DSU stated the *purpose* of the dispute settlement system. Article 3(2) states that:

> The dispute settlement system of the WTO is a central element in providing security and predictability to the multilateral trading system. The Members recognize that it serves to

preserve the rights and obligations of Members under the covered agreements, and to clarify the existing provisions of those agreements in accordance with customary rules of interpretation of public international law. Recommendations and rulings of the DSB cannot add to or diminish the rights and obligations provided in the covered agreements.

Consequently, GATT 1994 maintains the panel system of GATT 1947, although with some modifications to how the panels now work. Whereas under the 1947 regime, the GATT Council established the panels, under the 1994 DSU panels are established by the DSB and the panels' main responsibility is to assist the DSB in its work. Also, unlike under GATT 1947 whereby each panel was responsible for setting up its own procedures, the 1994 DSU lays out default working procedures applicable to all panels (although a panel might decide not to use this procedure, according to Appendix 3 of the DSU). Furthermore, it was in 1994 that the qualifications to be possessed by panel members were laid down for the first time; such panellists act in their own regard, not as representatives of their governments. In fact, Article 8(9) DSU prohibits governments from influencing panellists' decisions in any way. Finally, unlike the 1947 panels, 1994 panels are not bound to apply information and arguments of disputing parties in coming to a decision. The panel is also able to receive information from outside parties and not only the States involved.

Article 13 DSU states that:

1. Each panel shall have the right to seek information and technical advice from any individual or body which it deems appropriate. However, before a panel seeks such information or advice from any individual or body within the jurisdiction of a Member it shall inform the authorities of that Member. A Member should respond promptly and fully to any request by a panel for such information as the panel considers necessary and appropriate. Confidential information which is provided shall not be revealed without formal authorization from the individual, body, or authorities of the Member providing the information.
2. Panels may seek information from any relevant source and may consult experts to obtain their opinion on certain aspects of the matter. With respect to a factual issue concerning a scientific or other technical matter raised by a party to a dispute, a panel may request an advisory report in writing from an expert review group. Rules for the establishment of such a group and its procedures are set forth in Appendix 4.

Although the DSU does not provide a list of where such extra information could be sought, this has been held to include from non-governmental organizations (NGOs).

● ***Report of the Appellate Body on United States—Import Prohibition of Certain Shrimp and Shrimp Products*** AB-1998-4, 12 OCTOBER 1998

The Appellate Body stated (at [110]) that:

> We find, and so hold, that the Panel erred in its legal interpretation that accepting non-requested information from non-governmental sources is incompatible with the provisions of the DSU. At the same time, we consider that the Panel acted within the scope of its authority under Articles 12 and 13 of the DSU in allowing any party to the dispute to attach the briefs by nongovernmental organizations, or any portion thereof, to its own submissions.

(p. 678)

Key points

- By virtue of the 1994 DSU, panels are appointed by the DSB and assist the latter in its work. This differs from the 1947 regime under which the GATT Council established the panels.
- GATT 1994 maintains the dispute settlement system under GATT 1947, although it made some major alterations—especially in relation to the qualifications of the panels, the source of information that they could consider, and the source of their rules of procedures.
- GATT 1994 did not discard the dispute settlement procedure of the old GATT, but actually incorporated it—especially in relation to the customary way in which the old regime evolved its practice.

The Appellate Body

It may be said that the appellate system is the most profound addition that GATT 1994 made to the GATT dispute settlement process. The appeal process under GATT is arguably one of the most changed areas which, despite not imposing a court structure, acts in a very similar manner.

As Curtis Reitz (1996, see section 18.1) noted, at 583:

> The single most dramatic change in the 1994 Understanding is that it establishes an Appellate Body to review panel reports...The Understanding eschews designating this body as a court, but its organization and functions have many of the essential aspects of a judicial body.

An appeal can be brought only for claims against an issue of law. Article 17(6) DSU provides

that 'An appeal shall be limited to issues of law covered in the panel report and legal interpretations developed by the panel.'

The Appellate Body has the power to 'uphold, modify or reverse the legal findings and conclusions of the panel' (Article 7(13) DSU).

One of the main improvements envisioned by the new Appellate Body's power is described by Curits Reitz (1996, see section 18.1), at 584:

> the Appellate Body should expound on the meaning of the agreements within its jurisdiction and create a corpus of decisions that will assure its jurisdiction and create a corpus of decisions that will assure consistency in GATT law and, hopefully, elevate the professional quality of the GATT dispute resolution mechanism. Growing respect for and confidence in the rulings of this professional body, even though not denominated a court, will advance international trade further into a stable regime that is governed by law and legal process.

The decision-making procedure is still that of consensus, but to prevent the GATT 1947 situation in which the 'losing' State has the ability to block a report from being adopted, a report is automatically considered adopted unless the DSB specifically chooses not to adopt it. The trade-off against consensus is the right of a losing party to appeal the decision. Where an appeal occurs, the decision is considered, not adopted. Under Article 16(4) DSU: (p. 679)

> Within 60 days after the date of circulation of a panel report to the Members, the report shall be adopted at a DSB meeting unless a party to the dispute formally notifies the DSB of its decision to appeal or the DSB decides by consensus not to adopt the report. If a party has notified its decision to appeal, the report by the panel shall not be considered for adoption by the DSB until after completion of the appeal. This adoption procedure is without prejudice to the right of Members to express their views on a panel report.

Remedies

The remedies available are also set out in the 1994 DSU, as is clarification of what the aim of the remedies ought to be. Article 3(7) DSU states that:

> Before bringing a case, a Member shall exercise its judgment as to whether action under these procedures would be fruitful. The aim of the dispute settlement mechanism is to secure a positive solution to a dispute. A solution mutually acceptable to the parties to a dispute and consistent with the covered agreements is clearly to be preferred. In the absence of a mutually agreed solution, the first objective of the dispute settlement mechanism is usually to secure the withdrawal of the measures concerned if these are

found to be inconsistent with the provisions of any of the covered agreements. The provision of compensation should be resorted to only if the immediate withdrawal of the measure is impracticable and as a temporary measure pending the withdrawal of the measure which is inconsistent with a covered agreement. The last resort which this Understanding provides to the Member invoking the dispute settlement procedures is the possibility of suspending the application of concessions or other obligations under the covered agreements on a discriminatory basis vis-à-vis the other Member, subject to authorization by the DSB of such measures.

Clearly, the scheme of remedies under DSU is three-pronged, relating to compliance, compensation, and suspension of concessions or obligations. In terms of compliance, the aim is to ensure that the wrongdoer ceases or desists from the offending measures, as provided for by Article 19(1) DSU. Due to the fact that compliance may not always be achieved, especially since it implies cessation of the offending act, compensation and suspension are provided for, although these are temporary measures to be decided upon only where compliance is not achieved within a reasonable time after the ruling (Article 22(1) DSU).

It must be pointed out that suspension is not an easy option. Once a State brings an action for suspension before the DSB, the rule of consensus relating to adoption of decisions under GATT 1947 applies, not the GATT 1994 rule. The implication of this is that a losing party could effectively block a move towards suspension, because such a party is not disqualified or otherwise prevented from taking part in the DSB's discussion of suspension. However, despite this possibility, it is often the case that political pressure exacted on the losing party prevents it from blocking a suspension; instead, a referral to arbitration is encouraged.

The most that the DSB can do in terms of enforcement is to keep appraised of the matter by considering the implementation of the recommendations or rulings that are undertaken. Article 21(6) DSU states that:

The DSB shall keep under surveillance the implementation of adopted recommendations or rulings. The issue of implementation of the recommendations or rulings may be raised at the DSB by any Member at any time following their adoption. Unless the DSB decides otherwise, the issue of implementation of the recommendations or rulings shall be placed on the agenda of the DSB meeting after six months following the date of establishment of the reasonable period of time pursuant to paragraph 3 and shall remain on the DSB's agenda until the issue is resolved. At least (p. 680) 10 days prior to each such DSB meeting, the Member concerned shall provide the DSB with a status report in writing of its progress in the implementation of the recommendations or rulings.

The decision of the DSB arbitrator is considered to be final (Article 22(7) DSU), and the arbitrator can apply both the GATT agreement and, more importantly, non-WTO laws—a system that has been criticized.

For example, Joel P. Trachtman, 'The domain of WTO dispute resolution' (1999) 40 Harv Int'l LJ 333, 337, argues that:

> One persistent problem of the WTO legal system is the recognition and application of legal rules from outside the system.

thinking points

- *Explain the jurisdiction of the Appellate Body.*
- *What is the nature of decisions given by the Appellate Body?*
- *What difficulty is present in the use of the same consensus process under GATT 1947 for decisions as to whether a matter should be referred to an arbitrator under GATT 1994?*
- *When can compensation and suspension be resorted to as remedies under the 1994 DSU, and why?*

18.3.4 Weaknesses of GATT 1994/WTO system

There are several factors that undermine the strength of the GATT 1994/WTO system. It has been said (Curtis Reitz, 1996, at 599, see section 18.1) that, as a governmental institution, the WTO:

> lacks significant strength in legislative and executive function. The Director-General and the Secretariat cannot be expected to take strong initiatives in shaping the law.

Another criticism is that the GATT 1994/WTO system is unable to develop in the way in which GATT 1947 did through the incorporation of practice, and cannot easily react to the changing nature of trade due to its more defined institutional procedures and legal rule approach.

John H. Jackson, 'Dispute settlement and the WTO: emerging problems' (1998) 1(3) J Int'l Econ L 329, 347, suggests that:

> Thus the opportunity to evolve by experiment and trial and error, plus practice over times, seems considerably more constrained under the WTO than was the case under the very loose and ambiguous language of the GATT, with its minimalist institutional language.

Furthermore, the fact that a State's right to avail itself of one of the remedies (suspension) can be curtailed by the losing party's decision not to support suspension is detrimental to the

process.

That notwithstanding, one of the most remarkable improvements that has occurred since 1994 and the reformation of the old GATT system is the increase in cases that are being brought before the DSU, by both developed and developing countries. This would imply that States are reacting favourably to the stricter structure and procedures that are imposed.

(p. 681) 18.4 International finance law

The second leg of IEL is that which deals with the regulation of international finance, which is commonly known as international finance law (IFL). This section briefly looks at the IMF and the World Bank, the major pillars of this aspect.

18.4.1 The International Monetary Fund

The IMF came out of the United Nations Monetary and Financial Conference, more commonly known as the 'Bretton Woods Conference', held in July 1944. The results were agreements requiring the setting up of GATT, the International Bank for Reconstruction and Development (IBRD), and the IMF. The IMF sought to help to develop an international monetary system.

Following the Second World War, it was felt that, for a peaceful coexistence between States, trade and other international monetary aspects should be encouraged. The Bretton Woods Conference saw the adoption of the Articles of Agreement for an International Monetary Fund (the Articles of Agreement), which were based on the collaborative draft of John Maynard Keynes and Harry Dexter White. The Keynes and White proposal also envisioned the World Bank as a sister institution.

The IMF is composed of a board of governors, which represent the finance ministers or central bank governors of the member States, as well as a board of executive directors, with the president of the World Bank and the managing director of the IMF heading up the staff.

Andreas Lowenfeld (2010, see section 18.1), at 577, explains how tradition has come to play a major role in determining the appointment of the president and managing director:

> Under a tradition not stated in the Articles of Agreement of either institution, the President of the World Bank has always been an American, and the Managing Director of the IMF has always been a European.

The purposes of the IMF

The purpose of the IMF, as described by Article I of the Articles of Agreement, is:

> **(i)** To promote international monetary cooperation through a permanent institution which provides the machinery for consultation and collaboration on international monetary problems.

(ii) To facilitate the expansion and balanced growth of international trade, and to contribute thereby to the promotion and maintenance of high levels of employment and real income and to the development of the productive resources of all members as primary objectives of economic policy.
(iii) To promote exchange stability, to maintain orderly exchange arrangements among members, and to avoid competitive exchange depreciation.
(iv) To assist in the establishment of a multilateral system of payments in respect of current transactions between members and in the elimination of foreign exchange restrictions which hamper the growth of world trade.
(v) To give confidence to members by making the general resources of the Fund temporarily available to them under adequate safeguards, thus providing them with opportunity to (p. 682) correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity.
(vi) In accordance with the above, to shorten the duration and lessen the degree of disequilibrium in the international balances of payments of members.

It will be recalled from the introduction to this chapter that the whole rationale for developing a coherent international economic and monetary system was against the backdrop of a fixed gold value in the early 1940s, which, in turn, created stability in the international market.

As Rosa Maria Lastra notes in 'The International Monetary Fund in historical perspective' (2000) 3 J Int'l Econ L 504, 513:

> The IMF's mandate was to maintain the good order of this predictable and 'stable' international monetary system, by enforcing rules about adjustment in international monetary relations and by providing temporary resources to deal with short-term balance of payments problems.

thinking points

- *Explain the mandate of the IMF.*
- *List the purposes of the IMF, and explain the link between these purposes and the historical background to the emergence of the IMF.*

The functions of the IMF

The IMF performs three essential functions: conducting surveillance; providing conditional financial support; and providing technical assistance (Lastra, 2000, at 514 *et seq*, see earlier in this section). Whereas surveillance entitles the IMF to undertake an assessment of a country's economic policies and prepare a report to advise the country accordingly, conditional financial support enables the Fund to provide loans to member States. Such loans can, however, be provided only on the basis of 'conditionality', which, according to Lastra

(ibid., 516) is:

> The set of policies and procedures developed by the Fund to govern the access to and the use of its resources by member countries…The logic behind the conditionality requirements is that a country with external payment problems is spending more than it is taking in. Unless economic reform takes place, it will continue to spend more than it takes in.

It is through 'conditionality' that the IMF is able to determine how much a member State is able to borrow from the Fund, since such borrowing is usually linked to the amount contributed by the State upon joining the IMF. Conditionality, therefore, is the adoption and implementation by a member State of adjustment policies prescribed by the IMF. In this way, 'conditionality' looks more like collateral security, which a borrower in a domestic system is required to provide as a means of demonstrating his or her ability to repay. However, conditionality does more than serve as a substitute for collateral. As Lastra notes (ibid., 517):

> IMF conditionality can signal policy credibility to the market. The existence of an IMF program encourages private investment into the country. Being in arrears to the IMF brings a country into the status of an 'economic pariah'.

Thus, when countries take loans from the IMF, they are particularly careful not to default, because this sends the wrong signal to investors and can lead to an isolation of that State from **(p. 683)** the international economic community—known as 'pariah status'. It must be pointed out that the use of conditionality has been greatly reduced over the years as a result of the emergence of new facilities and procedures.

The IMF also provides technical assistance to its member States. This is extremely important when we consider that developing and least developed countries often lack the necessary technological know-how and capacity to acquire the sophisticated and expensive facilities required in today's global financial market. The IMF is thus able to provide training in several aspects of banking and financial services to staff of its member States.

In general, the IMF was meant to allow States that were unable to meet their obligations to seek financial help, as well as to enable those States having financial difficulties to receive help in order to establish equilibrium in the international monetary system.

The IMF established a pool of funds upon which its members would be able to draw. The funds were received from the member States in accordance with a specifically designed quota which, in theory, represented their economic importance. It also soon became a fact that not all currencies were to be used for international account settlements.

Lowenfeld (2010, see section 18.1), at 578–579, notes that:

> As it turned out, only a few members' currencies were generally acceptable convertible

currencies. Typically, a member state needing resources to settle its accounts would draw US dollars from the Fund and use these to redeem its own currency…held by a creditor country.

Key points

- The IMF performs a surveillance function and provides member States with loans (subject to conditionality), as well as technical assistance.
- Conditionality enables the IMF to prescribe programmes that States that intend to draw funds from it must implement. It enables the Fund to assess the repayment capability of the borrowing States and, to that extent, it resembles collateral security in the domestic banking system.
- The IMF funds are pooled from the contributions made by member States upon joining (usually called 'quotas'), which are often determined in accordance with the economic abilities of individual States.

Modality for drawing loans from the IMF

The IMF was subject to revision during the 1970s but, before this time, it was undecided, when a State had a **drawing right**, whether it was to be subject to specific conditions. Whereas the UK preferred a system whereby States had an automatic right to draw from the Fund—that is, to draw funds without preconditions—the USA took the line that any State wishing to receive funds had to satisfy conditions. It was this latter approach that was adopted.

> **drawing rights**
>
> Supplementary foreign exchange reserve assets maintained by IMF members for the purpose of meeting shortfalls in their economies.

A State had to provide evidence that it would be able to solve the problem with the funds and supply this in a letter of intent. Andreas Lowenfeld (2010, see section 18.1), at 580, describes the letter of intent:

> Although in the form a Letter of Intent is a unilateral declaration, in practice it is a document resulting from negotiation between the Fund and the applicant country. Letters of Intent are (p. 684) considered binding on the country involved, even though they have not been submitted to its parliament and even when the administration in office has changed during the period of the drawing.

These letters used to be confidential, but they are now public and even published online.

Things worked relatively well for the IMF until 1967, at which time problems arose that impacted the IMF considerably and almost destroyed it. The UK devalued its currency, sterling, which was at that time used as a reserve; this impacted its commitments to the IMF. Even though the USA said that it would continue with its financial commitments, this was only a temporary fix: the country started experiencing its own problems in 1971, which presented a major hurdle for the IMF when then US President Nixon made the decision that the USA would no longer be converting US dollars held by foreigners to gold or other reserve assets, due to the USA's depleting reserves. These issues meant that it was no longer possible for the IMF to use its fixed-rate system. All of the major currencies were floating by 1973—that is, there were no governmental interventions in the financial market and the currency value was allowed to fluctuate according to the foreign exchange market.

Following these problems, the IMF was able to preserve only its structure, but not its substance. The new Articles of Agreement no longer imposed the former par value obligation; instead, they only obliged member States to refrain from manipulating the exchange rate (Article IV).

Despite the fact that member States were no longer obliged to follow the fixed exchange rate and currencies were allowed to float on the open market, the IMF did still retain some of its surveillance powers. Article IV(3) of the Articles of Agreement states that:

> **(a)** The Fund shall oversee the international monetary system in order to ensure its effective operation, and shall oversee the compliance of each member with its obligations under Section 1 of this Article.
> **(b)** In order to fulfill its functions under (*a*) above, the Fund shall exercise firm surveillance over the exchange rate policies of members, and shall adopt specific principles for the guidance of all members with respect to those policies. Each member shall provide the Fund with the information necessary for such surveillance, and, when requested by the Fund, shall consult with it on the member's exchange rate policies. The principles adopted by the Fund shall be consistent with cooperative arrangements by which members maintain the value of their currencies in relation to the value of the currency or currencies of other members, as well as with other exchange arrangements of a member's choice consistent with the purposes of the Fund and Section 1 of this Article. These principles shall respect the domestic social and political policies of members, and in applying these principles the Fund shall pay due regard to the circumstances of members.

After the 1970s, the IMF ceased to play an influential role in the international monetary and economic system. In fact, GATT, and then the WTO, took over some of the areas that the IMF had previously governed.

As Lowenfeld (2010, see section 18.1) notes, at 585–586:

> Leadership in legislation concerning the international economy passed to the GATT and subsequently to the World Trade Organization (WTO) as new rules were being negotiated and drafted by trade ministries and not by finance ministries…De facto, the IMF became essentially a foreign aid agency.

The significance of the IMF in providing financial aid to developing countries has also continued to decrease over time, especially given the sensitivity inherent in the requirement that States wanting loans from the Fund should submit letters of intent. Also, there is now a proliferation of private loans and of loans provided by different groups of States outside the IMF framework. A prominent example is the so-called Paris Club, which now offers such facilities as debt restructuring, debt relief, and total debt cancellation.

(p. 685) Also, on 26 September 2009, a group of seven South American nations—Argentina, Bolivia, Brazil, Ecuador, Paraguay, Uruguay, and Venezuela—established the Bank of the South, with headquarters in Caracas, Venezuela. The Bank serves as an alternative to borrowing from the IMF. The founding States felt strongly that the IMF is dominated by Northern countries and claimed that this affected the IMF policies. Already, borrowing by Latin American countries from the IMF has fallen sharply, with many States such as Brazil refusing to borrow more from the Fund. The overall aim of the Bank is that all Latin American countries will become members—a move that will surely further whittle away the importance and relevance of the IMF in the long run.

thinking points

- *What approaches did the UK and USA prefer in terms of States drawing funds from the IMF, and which of these prevailed?*
- *What does 'surveillance' mean and why does the IMF carry out surveillance of its member States?*
- *Explain what is meant by a 'letter of intent'.*

18.4.2 The World Bank

The World Bank is another institution that emerged from the Bretton Woods Conference in response to the world wars. It originally comprised only the IBRD; it now includes the International Development Association (IDA).

Article I of the Articles of Agreement of the IBRD (amended in 1989) provides that the purposes of the Bank are:

> **(i)** To assist in the reconstruction and development of territories of members by facilitating the investment of capital for productive purposes, including the restoration

of economies destroyed or disrupted by war, the reconversion of productive facilities to peacetime needs and the encouragement of the development of productive facilities and resources in less developed countries.
(ii) To promote private foreign investment by means of guarantees or participations in loans and other investments made by private investors; and when private capital is not available on reasonable terms, to supplement private investment by providing, on suitable conditions, finance for productive purposes out of its own capital, funds raised by it and its other resources.
(iii) To promote the long-range balanced growth of international trade and the maintenance of equilibrium in balances of payments by encouraging international investment for the development of the productive resources of members, thereby assisting in raising productivity, the standard of living and conditions of labor in their territories.
(p. 686) **(iv)** To arrange the loans made or guaranteed by it in relation to international loans through other channels so that the more useful and urgent projects, large and small alike, will be dealt with first.
(v) To conduct its operations with due regard to the effect of international investment on business conditions in the territories of members and, in the immediate postwar years, to assist in bringing about a smooth transition from a wartime to a peacetime economy.

The World Bank discharges these responsibilities by providing low-interest loans, and interest-free credits and grants, to developing countries to address a wide range of issues and areas. Although most of its clients are invariably developing countries, the Bank's loan facilities are open to all member States; indeed, France was the first country to benefit from World Bank financial aid.

Under Article III(1) of the IBRD Articles of Agreement:

(a) The resources and the facilities of the Bank shall be used exclusively for the benefit of members with equitable consideration to projects for development and projects for reconstruction alike.
(b) For the purpose of facilitating the restoration and reconstruction of the economy of members whose metropolitan territories have suffered great devastation from enemy occupation or hostilities, the Bank, in determining the conditions and terms of loans made to such members, shall pay special regard to lightening the financial burden and expediting the completion of such restoration and reconstruction.

The IDA's purpose is set out in Article I of its Articles of Agreement:

The purposes of the Association are to promote economic development, increase

productivity and thus raise standards of living in the less-developed areas of the world included within the Association's membership, in particular by providing finance to meet their important developmental requirements on terms which are more flexible and bear less heavily on the balance of payments than those of conventional loans, thereby furthering the developmental objectives of the International Bank for Reconstruction and Development (hereinafter called 'the Bank') and supplementing its activities.

Key points

- The World Bank is a Bretton Woods institution that exists to assist member States to undertake a wide range of activities, such as reconstruction and development.
- The World Bank provides low-interest loans and interest-free credit facilities to developing countries. However, developed countries can also benefit from World Bank loan facilities.

18.5 The World Bank's Inspection Panel

Established in 1993 by the World's Bank Board of Executive Directors, and commencing operations on 1 August 1994, the Inspection Panel is an independent body responsible for dealing with complaints over the World Bank's funded projects. As a major developmental bank, (p. 687) the World Bank funds numerous projects across the world. Some of these projects often generate tension between the beneficiaries of the projects, usually governments, and their citizens. Sources of discord have been known to include proposals to cultivate forests, which locals claimed served traditional purposes for them, or to build resources that are perceived to threaten the ecosystem or the people's traditional way of life. While the Bank itself does not have direct responsibility for such issues, the fact that it is providing funding for the project makes it a key player.

Where there are complaints that World Bank-funded projects will adversely affect people's lives, it is important to have independent mechanisms to deal with such complaints. This is the rationale behind the Inspection Panel.

18.5.1 Composition

The Inspection Panel consists of three members appointed by the Board of Executive Directors for a five-year, non-renewable term. Selection is based on the competence and ability of each Member 'to deal thoroughly and fairly with the complaints brought to them, their integrity and independence from Bank Management, and their exposure to developmental issues and living conditions in developing countries'. (See http://ewebapps.worldbank.org/apps/ip/Pages/AboutUs.aspx). The Panel also has a Secretariat, which supports its work, and is additionally serviced by experts and consultants which it hires from time to time.

18.5.2 Function

The Panel's main function is to serve as a watchdog to the World Bank to ensure that it complies with its operational policies and procedures. These include such issues as:

- adverse effects on people and livelihoods as a consequence of displacement and resettlement related to infrastructure projects, such as dams, roads, pipelines, mines, and landfills;
- risks to people and the environment related to dam safety, use of pesticides, and other indirect effects of investments;
- risks to indigenous peoples, their culture, traditions, lands tenure, and development rights;
- adverse effects on physical cultural heritage, including sacred places;
- adverse effects on natural habitats, including protected areas, such as wetlands, forests, and water bodies.

(See http://ewebapps.worldbank.org/apps/ip/Pages/AboutUs.aspx).

The Panel is therefore an accountability mechanism although, as will be seen in the evaluation of its process later, whether it lives up to this important billing is debatable.

thinking points

- *Explain the rationale for establishing the World Bank Inspection Panel.*
- *What are the criteria for selecting the members of the Panel, and what other criteria can you suggest?*

(p. 688) **18.5.3 The Inspection Panel's review process**

The Panel review process starts with it receiving a request for inspection from one or more persons called requesters. A request for inspection is an invitation, sent to the Panel by a member(s) of the community who fears that what the World Bank-funded project is doing will destroy or is destroying their means of livelihood or environment. Such complaints, if they are found to be true, are directly opposed to the values of the World Bank's policies and procedure which is to safeguard social welfare and the environment.

Upon receiving a request, the Panel registers the request, which kicks in the eligibility phase. This phase is to determine whether the request for inspection is or is not suitable to be admitted. The World Bank's management then has twenty-one days, from the date of registration of the request, within which it must provide the Panel with evidence that it complied or intended to comply with the Bank's relevant policies and procedures. The Panel also has twenty-one business days after receiving the response from the Bank's management, to determine the eligibility of the request.

A successful determination of eligibility of request is followed by the Panel reviewing the management's response after which the Panel may undertake a visit to the concerned project,

following which it may then make recommendations to investigate the request. Up to this point, the Panel functions completely independently of the Bank's management, as it should as an oversight body. However, the picture changes once the Panel makes recommendations to investigate the request. A recommendation to investigate requires the approval of the Bank's Board of Executive Directors, and it is only after this is given that the Panel can progress to the second stage of its work, the investigation phase, in which it assesses the merits of the request. The task of the Panel in this phase includes visiting the place complained about, meeting with the local people, both those who originated the request and others whose views may be instrumental and useful to the Panel's investigation. The duration of the investigation depends on the nature of the issue at hand.

At the end of this phase, the Panel produces a report which it then submits to the Bank's management. The management will also prepare its recommendations, based on the report, which will then be considered along with the Panel report, by the Board of Executive Directors. The Board may or may not approve the recommendations.

From this, it seems overgenerous to describe the Inspection Panel as an 'independent body'. The Panel was set up to assess whether or not the Bank is following its own policies and procedures. Yet whether or not the Panel can investigate a complaint depends on the approval of the Bank management which may decide to withhold its approval. Furthermore, the final report of the Panel is submitted to the management which will consider it and write its own recommendations to be forwarded with the Panel's report to the Board. The Board's approval is given or withheld not to the Panel's report, but to the management's recommendations which do not have to agree with the Panel's report. If anything, this process is far from being independent.

thinking points

- *Describe the review process of the Inspection Panel and explain what benefits it confers for the World Bank.*
- *How far can one claim that the Inspection Panel is independent of the World Bank?*

(p. 689) Conclusion

IEL is undoubtedly a vital tool in ensuring the health of nations. The current financial crisis shows clearly why it is extremely important to put in place a strong regime of international economic regulation. However, in pursuing such an endeavour, there are various challenges to be expected, all of which will affect the future of IEL.

There are institutional-specific problems. The long-term sustainability of the funds available to such institutions as the IMF has been questioned. Also, there is an increasing perception, especially in the developing world, that rich and powerful countries are not always transparent, even in the way in which they engage with each other. For example, most WTO negotiations have been marred by bitter division between developed and

developing worlds on a number of issues such as subsidies and so on.

In addition, States are often reluctant to cede authority over their economies to international institutions. Former British Prime Minister Margaret Thatcher once said 'No one is going to tell me how to run economic policy', while an official of the US Treasury responded 'We wouldn't want to have the IMF order us around' (both restated in Lowenfeld, 2010, at 584, see section 18.1). Yet, while the preservation of sovereignty is important, it must be noted that it is only by not allowing sovereignty to stand in the way of strong international economic regulation that States can actually be guaranteed peace and prosperity. Otherwise, States risk monumental economic meltdown, such as that which has now led many States, including Portugal, Greece, and Ireland, to seek huge financial bailouts from international institutions. Such action, in itself, cannot bode well for sovereignty.

Questions

Self test questions

1 What is 'international economic law'?
2 Explain what is meant by the 'Bretton Woods institutions'.
3 What is the relationship between international economic law and public international law?
4 Explain 'conditionality' in the context of the IMF.
5 What do 'nullification' and 'impairment' mean in the context of GATT?
6 Why was the Bank of the South established?
7 What is the IBRD?
8 Explain what is meant by 'surveillance'.

Discussion questions

1 Explain the functions of the IMF.
2 What are the major weaknesses of the GATT/WTO system?
(p. 690) **3** To what extent does the dispute settlement system under GATT 1947 differ from that under GATT 1994?
4 Explain why public international law was slow to regulate international economics.
5 Which types of State can access the World Bank loan facilities?

Assessment question

'There is no real difference between the dispute settlement procedure under GATT 1947 and that under GATT 1994. In the final analysis, both deal with disputes in the same way, and use the same media and institutions. It is an exaggeration, and nothing more, to think that one is better than the other.'

Discuss.

Key cases

- *Report of the Working Party on the Australian Subsidy on Ammonium Sulphate* GATT/CP.4/39, adopted 3 April 1950, BISD II/188
- *Report of the Panel on Uruguay Recourse to Article XXIII* L/1923, adopted 16 November 1962, BISD 11S/95
- *Report of the GATT Panel on the Treatment by Germany of Imports of Sardines* G/26, adopted 31 October 1952, BISD 1S/53

Further reading

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