

Cambridge University Press

978-1-107-06363-1 - The Rule of Law in Monetary Affairs: World Trade Forum

Edited by Thomas Cottier, Rosa M. Lastra and Christian Tietje

Excerpt

[More information](#)

1

Introduction and overview

THOMAS COTTIER, ROSA M. LASTRA,
CHRISTIAN TIETJE AND LUCÍA SATRAGNO

[T]he international community needs to make headway on the issue of reform of the international monetary system. Unilateral attempts to change or to retain the status quo will not work. We need an international monetary system which supports cross-border investment and a better allocation of capital across nations and which 'facilitates international trade' – as laid out in the aims of the International Monetary Fund. What we need is a global monetary system which inspires confidence, offers stability and monitors exchange rates more efficiently. One which provides the means through which global imbalances that may risk endangering stability can be addressed.

Pascal Lamy¹

Monetary affairs are at the heart of, and continue to play a key role in, the development of economic and social systems worldwide. The 2007–9 global financial crisis demonstrated that the malfunctioning of the monetary system impedes growth, generates recession and increases protectionism in international trade. It amounted to a failure of law and economics alike.² The profound and long-lasting effects of the financial crisis triggered changes in the regulatory thinking at all levels of governance. Hence, monetary affairs – one of the last bastions of national sovereignty – are at the centre of the debate worldwide.³ The moment has come to revisit the relationship between law and economics in the field.

¹ Former Director-General of the WTO, opening speech at the WTO Seminar on Exchange Rates and Trade, held on 27 March 2012, available at www.wto.org/english/news_e/sppl_e/sppl222_e.htm.

² T. Cottier, 'Challenges Ahead in International Economic Law', *Journal of International Economic Law*, 12:1 (2009), 3–15.

³ Rosa M. Lastra, *Legal Foundations of International Monetary Stability* (Oxford University Press, 2006), pp. 4–5; Tullio Treves, 'Monetary Sovereignty Today', in Mario Giovanoli (ed.), *International Monetary Law: Issues for the New Millennium* (Oxford University Press, 2000), pp. 111–18.

Cambridge University Press

978-1-107-06363-1 - The Rule of Law in Monetary Affairs: World Trade Forum

Edited by Thomas Cottier, Rosa M. Lastra and Christian Tietje

Excerpt

[More information](#)

2 T. COTTIER, R. LASTRA, C. TIETJE AND L. SATRAGNO

In comparison with the proliferation and reinforcement of rules in the other areas of international economic law (trade and investment), the role of law in monetary affairs has been a limited one.⁴ The focus is on constitutional issues relating to the establishment and the functioning of monetary institutions, in particular securing independence and separation of powers in monetary policy-making. While the law has been important in framing agreements between the institutions and recipient countries, it has not played a significant role in informing monetary policies. Such policies, based upon economic considerations, are usually designed and implemented by national independent central banks, operating within a given legal framework, yet equally independent from legal principles and norms apart from very broadly defined goals. This constellation raises concerns of accountability and legitimacy. Soft law standards issued by the International Monetary Fund (IMF), the Basel Committee on Banking Supervision (BCBS), and the Financial Stability Board (FSB), among others, all try to address such concerns at the global level. However, the global financial crisis highlighted the need for reflections upon the role of hard law and normative guidance.

The crisis enhanced the role of law and regulation in the financial system, improving the framework and the stability for private operators and commercial banks.⁵ Financial stability has become a prime principle informing regulation both in national and European law. It is at the heart of the developments on the global level in the creation of new soft law instruments by international standard setters.⁶ However, it would seem that relatively little attention has been paid to potential lessons to be drawn from the financial crisis and the subsequent sovereign debt crisis for the global monetary system. The focus on Europe, with the ongoing sovereign debt crisis, the advent of the banking union and the consolidation of the European Central Bank (ECB), has left global concerns related to monetary affairs – other than financial regulation – less prominent. This is certainly true from the legal

⁴ See C. Brummer, 'Why Soft Law Dominates International Finance – and Not Trade', *Journal of International Economic Law*, 13:3 (2010), 631 also in T. Cottier, J. H. Jackson and R. M. Lastra (eds.), *International Law in Financial Regulation and Monetary Affairs* (Oxford University Press, 2012), pp. 95–113.

⁵ For an extended debate and analysis on the quest for international law in financial regulation, see Cottier *et al.* (eds.), *International Law in Financial Regulation and Monetary Affairs*.

⁶ This volume will address the law and policy of the major actors in the international monetary system (the national central banks, the ECB, the IMF, the Bank for International Settlements (BIS), the G-20 and the FSB, among others).

Cambridge University Press

978-1-107-06363-1 - The Rule of Law in Monetary Affairs: World Trade Forum

Edited by Thomas Cottier, Rosa M. Lastra and Christian Tietje

Excerpt

[More information](#)

perspective. The focus has been on governance issues, in particular quotas and decision-making, but not so much on normative principles and rules which may inform monetary policies in the coming decades, contributing to the goal of monetary stability.

This edited volume purports to contribute to filling this vacuum by discussing the potential of law and legal methodology to contribute to international monetary stability. To attain this ambitious objective, the book seeks to explore and identify the underlying principles and norms which could guide and contribute to the formulation of policies, which have almost exclusively pertained to the domain of macroeconomics, with recourse to regulatory theory to address the role of law and legal principles in allocating powers and normative guidance for governmental action affecting individuals and society at large. In doing so, it attempts to draw lessons and insights from regulatory theory.⁷ It aims to identify to what extent monetary affairs pertain to the field of international economic law and thus to what extent they may share common principles with trade and investment.⁸ Comparison and linkages with the fields of international investment law and trade regulation within the WTO, and with the prominent role which law plays in these areas,

⁷ See, generally, R. Baldwin, M. Cave and M. Lodge (eds.), *The Oxford Handbook of Regulation* (Oxford University Press, 2010). One of the editors of this volume has given a particular focus to regulation and the principle of legality in his work both constitutionally and in international law, developing a regulatory theory which may also offer guidance in the field of monetary law, T. Cottier, *Die Verfassung und das Erfordernis der gesetzlichen Grundlage*, 2nd edn (Zurich: Verlag Rüeger, 1993); T. Cottier, 'Constitutional Trade Regulation in National and International Law: Structure-Substance Pairings in the EFTA Experience', in M. Hilf and E.-U. Petersmann (eds.), *National Constitutions and International Economic Law* (The Hague: Kluwer Law International, 1993), pp. 409–42; T. Cottier, 'Towards a Five Storey House', in C. Joerges and E.-U. Petersmann (eds.), *Constitutionalism, Multilevel Governance and International Economic Law* (Oxford: Hart, 2011), pp. 495–532.

⁸ Georg Schwarzenberger, known as one of the fathers of international economic law, noted in 1948 that international economic law is a special branch of international public law which involves different subject matters with the economic element as the common denominator. Hence, he remarked that 'an admittedly extraneous criterion is made the test of whether a subject falls within this new branch of international law'. See Georg Schwarzenberger, 'The Province and Standards of International Economic Law', *International Law Quarterly* 2:3 (1948), 405–6. Later on, he pointed out that each branch of international law 'has its own legal principles and standards which distinguish it from the general principles of international law and from each other'. See Georg Schwarzenberger, 'The Frontiers of International Law', *Yearbook of World Affairs* 246:6 (1952), 249. More recently, S. Charnovitz, while trying to address the question of what international economic law is, states that 'a body of law needs to be based on unifying principles (e.g. economic logics) or motivated by underlying theory of law'. See S. Charnovitz, 'What is International Economic Law', *Journal of International Economic Law* 14:1 (2011), 6.

Cambridge University Press

978-1-107-06363-1 - The Rule of Law in Monetary Affairs: World Trade Forum

Edited by Thomas Cottier, Rosa M. Lastra and Christian Tietje

Excerpt

[More information](#)

4 T. COTTIER, R. LASTRA, C. TIETJE AND L. SATRAGNO

complement and enrich the analysis. The history of international monetary institutions, in particular the Bretton Woods system, shows a very close interaction between trade, investment and monetary affairs. When the IMF was founded, trade imbalances and the balance of payments were the main concerns, and monetary affairs were discussed closely related to trade policy issues. Monetary interests and policies were mainly shaped in line with the trade interests of a country.⁹ The institutional divide between trade, investment and monetary affairs considerably loosened the link to the real economy of goods and services, which it primarily ought to serve under stable monetary conditions. An effort thus should be made to revisit this relationship, seeking to bring about greater coherence among these different fields.

This book explores the field on the basis of the doctrine of multilevel or multilayered governance, identifying appropriate layers of vertical governance and the need for greater coherence between domestic and international spheres. Studies on specific policy issues that have direct impact on monetary affairs, such as exchange rate policy, sovereign debt, competitiveness, trade imbalances, austerity programmes and the human rights dimensions, are provided to illustrate the complexity of the issues and the role that the law can play in such realms. We are confronted with the problem that there is no consensus among economists as to what constitutes good monetary policy and what the role of central banks should be. As *The Economist* put it in September 2013:

Yet for every critic who believes that central banks have done too little, there is one who fears they have done far too much. By propping up asset prices artificially, some complain, central bankers are stoking inequality, rewarding financial firms despite their past misdeeds and sowing the seeds of the next crisis. Many, especially on the right in America, give warning that the massive increase in the money supply QE [quantitative easing] entails can lead only to a debasement of the currency and hyperinflation. Others gripe that low interest rates in the rich world have sent a flood of hot money towards emerging markets, generating financial instability.¹⁰

Competing interests and conflicts are inherent to the task of law and we are committed to exploring to what extent the law can assist in guiding monetary policies and affairs under the legal principles of both domestic

⁹ See B. Steil, *The Battle of Bretton Woods: John Maynard Keynes, Harry Dexter White and the Making of the New World Order* (Princeton University Press, 2013).

¹⁰ 'Monetary Policy after the Crash: Controlling Interest', *The Economist*, 21–27 September 2013, 62–3.

Cambridge University Press

978-1-107-06363-1 - The Rule of Law in Monetary Affairs: World Trade Forum

Edited by Thomas Cottier, Rosa M. Lastra and Christian Tietje

Excerpt

[More information](#)

and international law. We are far from finding all the pertinent answers in what amounts to an incipient field of international economic law. Yet, the first step consists in asking the appropriate questions and stimulating and informing further debate among lawyers and economists.

To achieve its objective, the book is divided according to four thematic areas, which aim to provide the reader with a comprehensive understanding of the current problems affecting the field and some of the lessons that can be learnt from other areas of law. These four thematic areas are as follows:

- (i) the legal foundations and evolution of the international monetary system;
- (ii) the specific policy issues in monetary affairs;
- (iii) the interaction between World Trade Organization (WTO) law and monetary affairs; and
- (iv) the quest for law in monetary policy.

Part I of the book gives an introductory overview of the international monetary system, its present state and likely future development, and describes the current international architecture and institutional aspects by paying special attention to the unique role of central banks. This part also focuses on the lack of global substantive principles and rules in monetary affairs and introduces the debate about what role the law can or should play in this field. Christian Tietje puts the current challenges into a historical and conceptual perspective and draws a picture of international monetary affairs in relation to the other areas of international economic law. He points out some broad structural principles that are essential for strengthening the rule of law in international monetary affairs. Mario Giovanoli describes the evolution and present situation of the international financial and monetary architecture from an institutional perspective. He states that despite the increasing relevance of the international financial standards (IFSs), a number of issues remain unresolved and open to debate, such as the implementation of the standards, the legitimacy of the standard-setting bodies (SSBs), the transparency of the standard-setting process and the lack of legal remedies. Rosa Lastra discusses the fundamental and evolving role of central banks in monetary affairs with special reference to the US Federal Reserve System and the ECB. She argues that the law must govern the relationship of the central bank upwards with the government and downwards with the banking and financial system. Jean-Victor Louis focuses on the European Economic and Monetary Union (EMU) by analysing the role of national central banks (NCBs) in times of crisis

Cambridge University Press

978-1-107-06363-1 - The Rule of Law in Monetary Affairs: World Trade Forum

Edited by Thomas Cottier, Rosa M. Lastra and Christian Tietje

Excerpt

[More information](#)

6 T. COTTIER, R. LASTRA, C. TIETJE AND L. SATRAGNO

and the difficult insertion of the euro area into the global system. He contends that these two aspects of the EMU, together with the move towards a banking and fiscal union, will enhance the global position of the euro area.

Part II of the book looks at specific policy and procedural issues in the international monetary system. Bernard Hoekman starts by analysing the spillover effects of policies that have an impact on international competitiveness from a global governance perspective. With regard to macroeconomic and monetary policies, he argues that a more open discussion and a more specific analysis of the spillover effects of such policies is needed. Claus Zimmermann explores the conflicting objectives in the setting of global benchmark interest rates both by central banks and by the private sector and their impact upon competitiveness. In this context, he reviews the recent London Interbank Offered Rate (Libor) manipulation scandal and suggests that the replacement of private benchmark rates by alternative benchmarks based on central bank key rates should be considered. Iain MacNeil assesses the extent to which credit rating agencies (CRAs), as major players in the international financial and capital markets, should be regulated and what level of reliance on ratings is more appropriate in the pursuit of financial stability. Nadia Rendak gives an overview of the functioning and current challenges of the IMF's function of surveillance. She also looks at the potential lessons that the IMF can learn from other monitoring mechanisms, such as the WTO Trade Policy Review Mechanism (TPRM) and the Organisation for Economic Co-operation and Development (OECD) surveillance tool. Annamaria Viterbo and Isabel Feichtner follow on by taking up some particular topical and controversial issues related to the effects that sovereign debt has on monetary affairs. While Viterbo discusses the impact of sovereign debt restructurings in the context of the ongoing eurozone crisis, Feichtner offers an analysis of the role that taxation plays in the reduction of sovereign debt in times of austerity.

Part III of the book addresses and explores the relationship between specific areas of WTO law and monetary affairs. Robert Howse opens by exploring the underlying principles potentially informing monetary policy and trade, in particular the role of equity. Based on the broad precepts of this overarching principle, hardly ever referred to in this context, he offers reflections on a more coherent integration of finance, trade and sustainable development in international economic law, and the interaction of WTO law and the IMF in particular. Juan Marchetti, Michele Ruta and Robert Teh examine the relationship of trade and

Cambridge University Press

978-1-107-06363-1 - The Rule of Law in Monetary Affairs: World Trade Forum

Edited by Thomas Cottier, Rosa M. Lastra and Christian Tietje

Excerpt

[More information](#)

INTRODUCTION AND OVERVIEW

7

monetary policies from the point of view of economics, addressing trade imbalances and exchange rate misalignments. They argue that multi-lateral trade cooperation is fundamental in correcting persistent global imbalances. However, trade rules alone will not be enough and urgent solutions for the existing 'coherence gap' in global governance are needed. Gabrielle Marceau and John Maughan discuss the complex relationship between exchange rates and trade from a legal perspective. They scrutinise potential issues involving exchange rates which could be brought before the WTO dispute settlement body (DSB). Mathias Kende ends Part III by assessing the extent to which the TPRM takes into account monetary and financial policies in the revision of trade policies and shows the scope for potential refinement.

Part IV of the book deals with the quest for law in monetary affairs from a theoretical perspective while identifying the linkages and lessons from some other areas of international economic law. Thomas Cottier and Lucía Satragno discuss and analyse the potential of law and legal methodology in monetary affairs from the perspective of regulatory theory and on the basis of the doctrine of multilayered governance. They identify important lessons from other areas of law where there is close interaction between law and economics, showing the potential for identifying appropriate economic factors and considerations to be legally taken into account in monetary policy. Ernst-Ulrich Petersmann examines the international monetary system under the framework of multilevel governance and the role of human rights. He states that stronger 'multilevel regulation' of 'governance failures' and judicial protection of cosmopolitan rights is most needed under a transnational rule of law. Christine Kaufmann and Rolf Weber stress the importance of enhanced transparency in monetary affairs from a three-dimensional perspective, institutional and procedural elements, substantive foundation, and accountability. Markus Krajewski follows on by discussing the human rights dimension in monetary affairs with a focus on the austerity measures implemented in the context of the eurozone debt crisis. Human rights have an important role to play when assessing austerity policies and conditionalities of monetary policies applied to countries under duress and need. Kern Alexander links financial regulation and monetary policy. He describes the regulatory shift in international financial regulation to a macro-prudential focus. In this context, he asks whether international trade law commitments undertaken in the WTO General Agreement on Trade in Services (GATS) limit WTO members' policy autonomy to implement macro-prudential regulatory

Cambridge University Press

978-1-107-06363-1 - The Rule of Law in Monetary Affairs: World Trade Forum

Edited by Thomas Cottier, Rosa M. Lastra and Christian Tietje

Excerpt

[More information](#)

reforms. François Gianviti explores the interaction between monetary and exchange rate policies. He notes that even though such policies are under the realm of the monetary sovereignty of the states, they should be limited by the rules of the international monetary system. Finally, Federico Lupo-Pasini observes the difficulties in balancing monetary stability and investment protection from a theoretical perspective. He argues that the IMF should assume a central role in the definition of monetary and financial stability in investment agreements and in monitoring abuses.

The contributions offer interesting and relevant building blocks for use in the quest for law in monetary affairs. We conclude that the relationship between law and monetary affairs bears the potential for a greater role of law and legal principles, linking this field to other areas of international economic law. Also, we note that the law is not limited to strict rules, which are hardly suitable for monetary policy, but that legal principles and economic factors as defined by law may assist in developing an appropriate framework offering guidance to policy-makers and macroeconomics. Linkages with trade policy can be further refined and work is needed on the interaction between trade and monetary affairs fostering mutual learning and more interaction on the common issues. It is not a matter of attracting monetary affairs to the trading regime, but of empowering the IMF and central banks to deal with potential conflicts more effectively, taking recourse to law and legally defined principles and procedures to link relevant international institutions in a more coherent manner. While the suggestions proposed and answers provided differ, all contributors agree that the relationship between law and monetary affairs should be revisited and reshaped in order to promote a more stable and predictable international monetary system contributing to the financial stability goal embraced in the aftermath of the recent global financial crisis.

Cambridge University Press

978-1-107-06363-1 - The Rule of Law in Monetary Affairs: World Trade Forum

Edited by Thomas Cottier, Rosa M . Lastra and Christian Tietje

Excerpt

[More information](#)

PART I

Legal foundations and the evolution of the international monetary system

Cambridge University Press

978-1-107-06363-1 - The Rule of Law in Monetary Affairs: World Trade Forum

Edited by Thomas Cottier, Rosa M . Lastra and Christian Tietje

Excerpt

[More information](#)
