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Law and Reform of the International Economic System

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Law and Reform of the International Economic System

By Chios Carmody

There is likely to be continuing discussion of reform in the international economic system as Canada prepares to host two global leaders' summits in 2010. Among topics currently under consideration by G8/G20 heads of government are the adequacy of international banking supervision, risk management, debt relief, a new global reserve currency, and the structure of major international institutions (IMF, World Bank, WTO). What is the role of law in this?

There are at least three considerations that governments and policy makers will want to take into account in answering this question. The first is the landscape of international economic regulation, which is today composed of a dense network of pre-existing obligations concerning monetary affairs, international trade and development that need to be simultaneously observed. Attention will have to be paid to ensuring that policies pursued in different fields of international economic law are coherent and mutually reinforcing.

A second consideration is the nature of the "problem structure" devised to deal with an international economic issue as well as the nature of resulting "solution structure". How well a network of rights and obligations can be "fitted" on to a particular problem, and how well soft law and informal mechanisms can be enlisted for the same purpose, will go a long way to ensuring the effectiveness of any resulting legal regime.

Third, there is increasing recognition that international law works best when it is accompanied by regular reporting and verification. Simply put, international legal commitments function most successfully when the parties involved have a regular opportunity to meet and discuss their behaviour, with the possibility of sanctions in cases of non-compliance. Indeed, recent proposals for new mechanisms and regimes in international economic law have foundered on exactly this point.

Each of the above issues requires some elaboration. Nevertheless, it is important to remember that what we are focusing on here is the role of law. Many noted commentators express the view that the chief role of law is to instill predictability, or what is sometimes referred to as the protection of 'expectations'. This purpose can be identified in the IMF's stabilization facilities, in the World Bank's loan and good governance programs, and in countries' tariff concessions and service commitments under the WTO Agreement.

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² John Rawls observed, for instance, that in any free society individuals "have a claim to their better situation; their claims are *legitimate expectations* established by social institutions, and the community is obligated to meet them." John Rawls, *A Theory of Justice* 103 (1971); "The law and expectations are related by a mutual feedback mechanism. Reasonable expectations affect the state of the law, and the state of the law affects reasonable expectations." Patrick Atiyah, *The Rise and Fall of Freedom of Contract* 109 (1979).

³ See *China – Measures Affecting Imports of Automobile Parts*, WTO Doc. WT/DS339, 340, 342/R, para. 7.460 (18 July 2008), where

As we will see, however, predictability is introduced differently in different issue areas. Generally speaking, it is easier for a country to make a *negative* commitment *not* to do something than a *positive* commitment that binds it to behave in a certain way. Negotiators will find it useful to consider which of these options a projected international “obligation” will involve.

It is also helpful to understand on *whom* exactly the obligation in question will fall. Today there is acute awareness that while states remain the principal subjects of international law, other actors such as international organizations and NGOs are relevant in the legal landscape and influence compliance. The success of the 1987 Montreal Protocol to the Vienna Convention for the Protection of the Ozone Layer is a case in point. There, the global refrigeration industry was enlisted to eliminate the use of environmentally destructive chlorofluorocarbons (CFCs) as an industrial coolant. By the mid-1990s use of CFCs was phased out worldwide – several years ahead of schedule.⁴ A similar phase-out initiative has been introduced for single-hulled ships in the global oil tanker industry.⁵ In both instances, the cooperation of a few key players was of critical importance.

In any legal scheme there also needs to be a clear idea of who will possess the resultant *rights*.⁶ Obligations create rights, but who will be in a position to enforce those rights can often make a difference between the success and failure of an international regulatory regime. In recent decades there has been a proliferation of judicial and quasi-judicial mechanisms that seek to monitor and enforce compliance, that are either individual- or collectively driven, and involve steps that are either hard and/or soft.⁷ In virtually all of these schemes ‘perfect’ compliance is rarely feasible, or even desirable.⁸ The WTO’s legal system, for instance, permits legal action by any WTO member country for the breach of obligations by any other member, but the sheer range of obligations under the treaty and the varying constellation of interests mean that few obligations will be enforced to the letter. WTO members also recognize that there is a considerable penumbra of non-compliance and ‘conspiracies of silence’ on certain sensitive issues, leading to the observation that international economic cooperation under the WTO Agreement is more a process than a result.

One further consideration about the role of law is that all legal systems must pay attention

it was observed that “the main purpose and objective of the WTO Agreement and the GATT 1994 is to maintain the security and predictability of reciprocal market access arrangements manifested in tariff concessions. This, in our view, means that tariff concessions must be interpreted to benefit both the importing Member, China, and exporting Members.”

⁴ Richard E. Benedick, *Ozone Diplomacy* (1991); Karen T. Litfin, *Ozone Discourses* (1994).

⁵ R.B. Mitchell, *Intentional Oil Pollution at Sea: Environmental Policy and Treaty Compliance* (1994)

⁶ The assimilation of legal relations under the labels “rights” and “obligations” is probably guilty of generalization. Wesley Newcomb Hohfeld originally pointed out that a “right” potentially comes in at least four different forms: claim-rights, freedom-rights, power-rights and immunity-rights. Similarly, an “obligation” comes in at least four correlative forms: requirement-duties, liability-duties, constraint-duties and disability-duties. These pairings suggest that any normative arrangement can be more diverse than the plain right-obligation dyad described in this article. See Philip Allott, *Eunomia* 159-162 (1990).

⁷ A useful overview of these mechanisms is contained in the NYU Project on International Courts and Tribunals Synoptic Chart, the latest of which is available at http://www.pict-pecti.org/publications/synoptic_chart/synop_c4.pdf (accessed Jan. 12, 2010).

⁸ “Compliance is not an on-off phenomenon. For a straightforward prohibitory norm like a highway speed limit, it is in principle a simple matter to determine whether a particular driver is in compliance ... The problem for the system is not how to induce all drivers to obey the speed limit, but how to contain deviance within acceptable levels. And, so it is for international treaty obligations.” Abraham Chayes & Antonia Handler Chayes, *The New Sovereignty* 17 (1995).

to factors beyond predictability. These can be thought of ‘realities’. A body of law therefore works at reconciling the law of predictability with the flexibility required by real conditions. A certain ‘pitch’ - or balance – is struck between these two goals. The degree to which a legal system is able to achieve this balance successfully is an important factor in its viability. For example, the International Center for the Settlement of Investment Disputes (ICSID) was created as an arm of the World Bank in 1965 to resolve investment disputes between investors and host countries. In the last four decades it has resolved hundreds of such disputes. ICSID has attracted widespread adherence, in part, because arbitrators have refused to adhere to a one-size-fits-all definition of an ‘investment’.⁹ Instead, they have looked to national definitions or to definitions contained within treaties, allowing a margin of appreciation that is considered respectful of national sovereignty. ICSID’s ‘give’ in this respect has been identified as an important factor in its success.¹⁰

1. The International Economic System Today: A Dense Neighborhood

The existing landscape of international economic law is heavily built-up and, like the core of a great city, constitutes a dense network of pre-existing structures. Introducing anything new requires planning and consideration.

There are at least three ways of dealing with conflict of norms in international law. One classic method is the latter-in-time doctrine (*lex posterior*) reflected in Art. 30 of the Vienna Convention on the Law of Treaties.¹¹ The doctrine holds that the most recent international engagement on a topic governs the legal relationship between the parties. However, trying to determine whether a new international agreement is, in fact, meant to supersede existing obligations can be problematic.¹² A second method is the ‘special law’ or ‘special rule’ doctrine (*lex specialis*) reflected in Art. 5 of the Vienna Convention.¹³ This doctrine holds that a more specialized international agreement prevails over a more general one. Again, however, it can be difficult to determine if one engagement is more specialized than another.¹⁴ Often the matter is left to be decided by characterization. A third method is to provide a conflicts clause that 1. either accords a firm priority between two international engagements or 2. avoids a straightforward priority and instead seeks to coordinate application of the two sets of obligations. An example of prioritization are rules under the WTO Agreement that give precedence to certain determinations of the

⁹ See contrasting decisions in *Fedax N.V. v. The Republic of Venezuela*, ICSID Case No. ARB/96/3, Decision on Jurisdiction, July 11, 1997 and *Salini Costruttori S.P.A. and Italstrade S.P.A. v. Kingdom of Morocco*, ICSID Case No. ARB/00/4, Decision on Jurisdiction, July 23, 2001. In *Fedax* the panel found that the parties had consented to an ‘investment’ because of the extremely broad definition of the term included within the investment treaty. While the tribunal went on to consider what an objective analysis of investment would be, it based its decision on the subjective intent of the parties. In *Salini* the tribunal took an opposing view, ruling that the investment had to be met. It proceeded to apply five indicators: duration, commitment, risk, profit and economic development of the state, before concluding that the contract was an investment. For criticism of this varying approach by YC AD see Devashish KziSlan, “A Notion of ICSID Investment,” in Todd WealEv (ed.), *Investment Treaty Arbitration and International Law* ¶1 j2008).

¹⁰ Fabio Yala, “The Notion of Investment in ICSID Case Law”, 22 *J. Intl. Arb.* 1–5 (2005).

¹¹ Art. 30(3): “When a later treaty is entered into between the parties but the earlier treaty is not terminated or suspended ... the earlier treaty applies only to the extent that its provisions are compatible with the later treaty.”

¹² International Law Commission, *Fragmentation of International Law*, A/CN.4/L.68: 53 April 2006.

¹³ *Lex specialis* is provided for in Art. 5 of the *Vienna Convention on the Law of Treaties*, 18 I.L.M. 771 (1978) and Art. 55 of the *International Law Commission’s Articles on State Responsibility*, U.N.G.A. A/RES/56/83 (12 Dec 2001).

¹⁴ International

Law Commission, *Fragmentation of International Law*, A/CN.4/L.603/51 (13 April 2001).

IMF in monetary affairs that may have an impact on trade obligations.¹⁵ An example of coordination is found in the International Treaty on Plant Genetic Resources for Food and Agriculture, the preamble of which provides that it should not be interpreted as “implying in any way that a change in the rights and obligations under other international treaties.” It then expresses the understanding that this principle “is not intended to create a hierarchy between this Treaty and other international agreements.”¹⁶

These relatively straightforward rules can give rise to issues of great complexity in practice. Nevertheless, as Benedict Kingsbury has observed, coherence remains the norm: “states have remained unitary enough on their legal policy to avoid conflicts of obligation [and] the members of international tribunals have shown a commitment to systemic coherence and to comity, and the sense of a unified legal system with a unified international political order has generally been preserved.”¹⁷ Canadian policy makers would therefore do well to think about how a new set of obligations could be inserted into the existing landscape of international economic law in a way that coheres with and reinforces pre-existing commitments.¹⁸

2. Regime Design

A second general consideration relates to the ‘design’ of a legal regime. Much attention has been paid recently to means of optimizing the structure of rules and practices that together form international regimes.

Generally speaking, the nature of the ‘problem structure’ arises from the way in which the interests in question are to be conceived. If a particular problem is thought about as disagreement over a ‘good’, then there are three forms of goods to be regulated: 1. private goods, 2. public goods, or 3. ‘privatized’ versions of public goods. Private goods are those considered to be held by countries individually, such as natural resources found within territorial boundaries. Public goods are those that belong to states as a group or to the international community as a whole (sometimes referred to as *res communis*), such as the deep seabed or the ozone layer. Privatized public goods are those which exist in their original form as belonging to states or humanity as a whole, but over which some form of privatization is permitted. The introduction of market mechanisms in international law, most evident in the Kyoto Protocol’s and Clean Development Mechanism (CDM) and Joint Implementation (JI) scheme¹⁹, is an attempt to harness the power of economic

¹⁵ GATT Art. XV:2.

¹⁶ The International Treaty on Plant Genetic Resources for Food and Agriculture was signed 10 June 2002 and entered into force for Canada 29 June 2004. A further example is provided in Art. 60 of the 2005 UNESCO Convention on Cultural Diversity which states in somewhat stronger terms that parties shall “serve their commitments under the Convention and all other treaties to which they are party in good faith and “without subordinating this Convention to any other treaty which they may conclude in the future.”

¹⁷ Benedict Kingsbury, “The International Legal Order in Crisis,” *Oxford Handbook of Legal Studies* 271 at 281 (2003).

¹⁸ It could be, for instance, that coordinating mechanisms might be used to clarify the relative priority of obligations. One source of support for the view that international law is to be interpreted systematically comes from Art. 7(3)(c) of the *Vienna Convention on the Law of Treaty*, which provides that “There shall be taken into account, together with the context, (c) any relevant rules of international law applicable in the relations between the parties.” See Campbell McLachlan, “The Principle of Systemic Integration and Article 31(3)(c) of the Vienna Convention”, 54 *Y. L.J.* 279 (April 2005).

¹⁹ Under the Kyoto Protocol, Annex I countries have committed themselves to national and joint reduction targets. The GDM allows the creation of new projects by developing countries in non-Annex I countries, while Joint Implementation projects are to be diverted from existing projects earned within other Annex I countries.

forces to meet international goals.

In designing a ‘solution structure’, consideration then needs to be given to the range of interests that may be involved in exploiting the ‘good’ in question. One example from domestic experience involves Canada’s West Coast fishing industry. Total allowable catch quotas set by the federal government for the region during the 1980s led to widespread dumping of unwanted fish, misrepresentation of catches, and the closure of the groundfishery in 1995. The remedy for this initial failure involved re-opening the fishery in 1997 but divided the coastal area into more than 50 sectors, assigning transferable quotas, and requiring that all ships have neutral observers on board to record catches.²⁰

The design of solution structures in international law in future may draw on the work of Elinor Ostrom, 2009 Nobel Laureate in Economics, who has highlighted how communities in different parts of the world have evolved ways of managing public property, or ‘common pool resources’.²¹ Ostrom’s work challenges conventional wisdom that common property is poorly managed and should be either regulated by central authorities or privatized. Based on numerous studies of user-managed fish stocks, pastures, woods, lakes, and groundwater basins, she concludes that the outcomes are, more often than not, better than predicted by standard theories. Resource users frequently develop sophisticated mechanisms for decision-making and rule enforcement to handle conflicts of interest.

An international level, the analogous task in relation to international economic law will involve the assignment of rights and obligations in a way that is sensitive to both actual and ideal notions of the ‘good’ involved. For instance, international attempts to discipline the risk-taking activities of major financial institutions have not borne fruit so far because of continuing disagreement over the appropriate point of regulation and limited appreciation of international financial well-being as a single ‘good’.²² The central problem is one of polycentric governance. Ostrom is clear that a broad diagnostic framework is necessary and identifies a number of variables that are associated with self-organization.²³ At the same time, she is clear that there are many efforts currently underway to decentralize the management of public goods and that one-size-fits-all solutions rarely succeed.

²⁰ See C.W. Clark, *The Worldwide Crisis in Fisheries* (2006). Since 1997 the Governments of Canada and B.C. have assigned groundfish trawl quota to individual licence holders. To ensure that British Columbia's coastal communities continued to benefit from the West Coast groundfish trawl industry a B.C. Groundfish Development Authority (GDA) was created. The GDA now administers a system designed to ensure fair crew treatment, aid in regional development, promote the attainment of stable market and employment conditions, and encourage sustainable fishing practices. Under the scheme 10 per cent of individual vessel quotas are set aside by the Minister of Fisheries to be allocated back to licence holders to reflect the interests of the communities and the labour force. An additional 10 per cent is added to the licence holders' allocation at the start of each fishing season. On the advice of the GDA, a portion or all of this quota can be withdrawn from the licence should the licence holder be found to be treating crew members in an unfair manner. However, a report by Ecotrust Canada disputes the view that individually transferrable quotas are a panacea for the BC and global fishing industry, noting that their implementation in the BC groundfishery has led to absentee ownership and quota leasing, the development of a false sense of security to fishers, the facilitation of privatization and a growth in the capitalization of fisheries. See “A Cautionary Tale of ITQ Fisheries”, available at www.ecotrust.ca/fisheries/cautionarytale (accessed Jan. 11, 2009).

²¹ Elinor Ostrom, *Governing the Commons* (1990).

²² Noel Sacasa, “Preventing Future Crises” 45:4 *Finance & Development* 11-14 (2008).

²³ See Elinor Ostrom, “A General Framework for Analyzing Sustainability of Social-Ecological Systems” 325 *Science* 419, 420 (2009).

3. Reporting and Verification

For several decades the design of international regimes has been accompanied by a realization that reporting and verification of international engagements is critical to their success. The features of many modern treaty regimes, such as transparency, dispute settlement and capacity building, matter little if they are not accompanied by what has been referred to as “an iterative process of discourse among the parties, the treaty organization, and the wider public.”²⁴

Opportunities for meaningful communication between the parties matter immensely. With communication comes the formation of a ‘we’, a collective ethos as well as agreement over the boundaries of the collective good involved. The ‘we’ then being well-defined, countries are more likely to follow rules, to be cooperative and, occasionally, to sanction one another in order to help the collective continue. The most extreme sanction is obviously expulsion. At the same time, in the realm of international economic affairs formal punishment rarely pays off. In most cases it will be largely symbolic. The example of ineffective sanctions for failure to meet the Euro’s strict convergence criteria is a case in point.²⁵

A related observation is that policy making in the field of international economic law has to be accompanied by an authentic spirit of commitment. This is especially true in the case of the Eurozone (but policy making cannot be regarded as an opportunity for window-dressing) (there must be a genuine investment by governments in solutions to global financial problems). Here is where the promise and peril of the growing enthusiasm for ‘metrification’ becomes apparent.

²⁴ Abraham Chayes & Antonia Handler Chayes, *The New Sovereignty* 25 (1995).

²⁵ As part of the 1997 Stability and Growth Pact leading to the creation of a European Economic and Monetary Union in 1999, EU member states agreed to two convergence criteria leading to the creation of a common currency: an annual budget of no higher than 3 percent GDP and national debt lower than 60 percent GDP. Several countries that are part of the Union later breached these criteria. Punitive proceedings were begun against Portugal and Greece in 2002 and 2005, respectively, but fines were never applied. Subsequently, France and Germany also ran excessive deficits, but no action was taken against them.

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4. Somå C-ncluDiñw Thoughts

In the early 1990s there(wAw a ‘boomlet’ of akaDamic interest in implemejtqvioj,0aompliance and effectiveness studies related to international law.²⁷ The result has been a subsisting interest in ‘regime design’, even if the new international institutions created in the aftermath of the Cold War have not always fulfilled their aims.

In thinking about the role of law, however, it is important to remember that perfect compliance is rarely feasible and that shortcomings are often an opportunity to pinpoint weaknesses and engage in fine-tuning. Awareness of the existing landscape of international economic regulation, a clear idea of both the ‘problem-’ and ‘solution-structures’ that are possible, and a regular framework of communication, are all essential in the success of any regime of international economic law. Canadian and foreign policy makers would do well to recall these points going forward in 2010.

²⁶ The Millenium Development Goals are a series of 8 goals established at the U.N. Millenium Summit in 2000 designed to radically improve life conditions for the world’s least fortunate citizens by 2015. Early research completed by the UN Development Program has shown that progress towards attaining success by the 2015 deadline is not promising. See Centre of Concern, “Where Are We Now” in *More than a Numbers Game?* 14-21 (2005). Also Amir Attaran, “An Immeasurable Crisis? A Criticism of the Millennium Development Goals and Why They Cannot Be Measured” (2005) 2(10) *Policy Forum* 955-9.

²⁷ See for instance Thomas Franck, *The Power of Legitimacy Among Nations* (1990); Abraham Chayes & Antonia Handler Chayes, *The New Sovereignty* (1995). At the same time, a number of conferences on international law examined the subject of its effectiveness. See for instance American Society of International Law, *Proceedings of the American Society of International Law: Implementation, Compliance and Effectiveness* (1997).