

INTERNATIONAL FINANCIAL AND MONETARY LAW

SECOND EDITION

ROSA MARÍA LASTRÁ

*Professor of International Financial and Monetary Law
Centre for Commercial Law Studies
Queen Mary University of London*

OXFORD
UNIVERSITY PRESS

OXFORD

UNIVERSITY PRESS

Great Clarendon Street, Oxford, OX2 6DP,
United Kingdom

Oxford University Press is a department of the University of Oxford.
It furthers the University's objective of excellence in research, scholarship,
and education by publishing worldwide. Oxford is a registered trade mark of
Oxford University Press in the UK and in certain other countries

© Rosa M Lastra 2015

The moral rights of the author have been asserted

First Edition published in 2006
Second Edition published in 2015

Impression: 1

All rights reserved. No part of this publication may be reproduced, stored in
a retrieval system, or transmitted, in any form or by any means, without the
prior permission in writing of Oxford University Press, or as expressly permitted
by law, by licence or under terms agreed with the appropriate reprographics
rights organization. Enquiries concerning reproduction outside the scope of the
above should be sent to the Rights Department, Oxford University Press, at the
address above

You must not circulate this work in any other form
and you must impose this same condition on any acquirer

Crown copyright material is reproduced under Class Licence
Number C01P0000148 with the permission of OPSI
and the Queen's Printer for Scotland

Published in the United States of America by Oxford University Press
198 Madison Avenue, New York, NY 10016, United States of America

British Library Cataloguing in Publication Data
Data available

Library of Congress Control Number: 2014946121

ISBN: 978-0-19-967109-0

Printed and bound by
CPI Group (UK) Ltd, Croydon, CR0 4YY

Links to third party websites are provided by Oxford in good faith and
for information only. Oxford disclaims any responsibility for the materials
contained in any third party website referenced in this work.

1

MONETARY SOVEREIGNTY

A. Introduction	1.01	The functions of money	1.30
B. Definition of Sovereignty	1.06	Money and the law	1.32
Sovereignty in public international law	1.07	Monetary sovereignty under public international law	1.36
Monetary sovereignty	1.09	<i>Lex monetae</i> and legal theories of money	1.40
C. History of Sovereignty	1.11	E. The Attributes of Monetary Sovereignty	1.51
Sovereignty of the monarch	1.12	F. The Erosion of Monetary Sovereignty	1.56
Bodin	1.12	Voluntary or consensual limitations of monetary sovereignty	1.59
Machiavelli	1.13	The advent of European Monetary Union	1.59
Hobbes	1.14	International obligations: The IMF Articles of Agreement	1.64
Sovereignty of the people	1.16	Other limitations of national monetary sovereignty	1.66
Locke	1.17	G. Concluding Observations	1.76
Montesquieu	1.18		
Hamilton	1.22		
Madison	1.24		
Alexis de Tocqueville	1.26		
D. Money and Monetary Sovereignty under International Law:			
<i>Lex Monetae</i>	1.29		
The concept of money	1.27		

The use of words is to express ideas. Perspicuity, therefore, requires not only that the ideas should be distinctly formed, but that they should be expressed by words distinctly and exclusively appropriate to them. But no language is so copious as to supply words and phrases for every complex idea, or so correct as not to include many equivocally denoting different ideas. Hence it must happen that however accurately objects may be discriminated in themselves, and however accurately the discrimination may be considered, the definition of them may be rendered inaccurate by the inaccuracy of the terms in which it is delivered. And this unavoidable inaccuracy must be greater or less, according to the complexity and novelty of the objects defined.

Alexander Hamilton, *The Federalist Papers*, 1788¹

A. Introduction

The power to issue currency is a sovereign power, one of the attributes of sovereignty as classically defined. This chapter explores first the notion of sovereignty and its history, a history which is linked to the evolution of the nation State. In this respect, I provide an **1.01**

¹ See Alexander Hamilton, James Madison, and John Jay, *The Federalist Papers* (New York: Mentor, New American Library, 1961; a reprint of the original McLean Edition of 1788) 229.

analysis of the philosophical and political roots of sovereignty, with references to the work of Bodin, Machiavelli, and Hobbes, and of the evolution of this concept over the centuries, with the advent of democracy and the rule of law. While the debate in the eighteenth and nineteenth centuries focused upon the evolution of this concept with regard to the *locus* of that supreme power (ie, from the sovereignty of the king—hereditary monarch—to the sovereignty of the people), the debate in recent decades has been centred on what is referred to as the ‘erosion’ of sovereignty. The receding power of the nation State in recent years has been accompanied by a redefinition of the notion of sovereignty. Power today is no longer the exclusive domain of the nation State. Centripetal and centrifugal forces have diffused the power of the nation State, and today a variety of actors, including international organizations, multinational corporations, regions, local communities, and the civil society also exercise power.

- 1.02** The process of European integration has redefined the jurisdictional boundaries of the powers of the European States. The advent of Economic and Monetary Union (EMU) signifies a voluntary surrender of the traditional monopoly power enjoyed by the State—in the case of EMU, the participating Member States—with regard to the issue of currency. The globalization of financial markets and the powers vested upon the International Monetary Fund and other international financial institutions, as well as economic considerations such as the choice of exchange regime, have also limited and altered the traditional contours of the domain of monetary sovereignty.
- 1.03** The development of alternative currencies (local currencies such as the Bristol pound² or virtual currencies such as Bitcoin), together with the increasing use of alternative payments (initiatives in digital transactions and mobile payments such as Kenya’s M-Pesa) and alternative finance provides (such as peer-to-peer lending and crowdfunding), are some of the latest manifestations of the changing powers of the State in the monetary arena.
- 1.04** Notwithstanding these limitations, States remain the key actors in the international community. Indeed, following the global financial crisis that commenced in 2007 and reached its zenith in 2008,³ there has been a certain retrenchment to national boundaries with the de-globalization (or re-nationalization) of some financial markets and institutions.
- 1.05** Institutions are creatures of their time and history plays a fundamental part in understanding their evolution. In this chapter, I contend that there is nothing sacrosanct about the notion of monetary sovereignty that has traditionally been attributed to the nation State.

² For a study of local currencies, see Mona Naqvi and James Southgate, ‘Banknotes, Local Currencies and Central Bank Objectives’ (2013) Q4 *Bank of England Quarterly Bulletin* 317.

³ Dani Rodrik, *The Globalization Paradox. Democracy and the Future of the World Economy* (New York and London: Norton, 2011), advocates the need to strengthen the nation State to solve what he calls the ‘political trilemma of the World economy’. Rodrik argues that we cannot have ‘deep economic integration’ (he uses the terms ‘hyper-globalization’), national sovereignty (nation State) and democratic politics all at once (200–1). We can have at most two out of three. Since democracy cannot be compromised, and he rejects the ‘global governance’ option, he proposes a return to national sovereignty. I disagree though with Rodrik’s solution to the ‘trilemma’; in my opinion, we need an adequate system of global governance. The dichotomy between international markets and national laws and policies can be best tackled by the internationalization of the rules and institutions governing global markets. The answer is more international law and less national law. For a discussion on this, see Thomas Cottier, John Jackson, and Rosa Lastra (eds), *International Law in Financial Regulation and Monetary Affairs* (Oxford: Oxford University Press, 2012).

B. Definition of Sovereignty

Sovereignty has traditionally being defined as the supreme authority within a territory. The State is the political institution in which sovereignty is embodied. **1.06**

Sovereignty in public international law

Sovereignty in the sense of contemporary public international law denotes the basic international legal status of a State that is not subject, within its territorial jurisdiction, to the governmental (executive, legislative, or judicial) jurisdiction of a foreign State or to foreign law other than public international law.⁴ It forms part of the fundamental principles of general international law and it is considered to be one of the principal organizing concepts of international relations.⁵ It protects the existence and the freedom of action of States, as limited by international law, in their international relations as well as with respect to their internal affairs. In particular, it protects their freedom of self-determination over their political, constitutional, and socio-economic systems and cultural identity,⁶ their territorial integrity and exclusive jurisdiction over their territory, and their personal jurisdiction over their citizens and juridical persons established under their jurisdiction as well as over matters with trans-frontier connections which have reasonably close links with or effects upon the State's territory.⁷ **1.07**

Vaughan Lowe argues that debates about sovereignty constitute a vehicle for specific discussions over rights and duties of States.⁸ **1.08**

⁴ See Helmut Steinberger, 'Sovereignty' in *Encyclopedia of Public International Law* (Amsterdam: North Holland, 1987) vol 10, 408.

⁵ See Marc Williams, 'Rethinking Sovereignty' in Eleonore Kofman and Gillian Youngs (eds), *Globalization: Theory and Practice* (London: Pinter, 1996) 109. See also Alan James, *Sovereign Statehood* (London: Allen and Unwin, 1986) 267 and Anne-Marie Slaughter, *A New World Order* (Princeton: Princeton University Press, 2004). Dan Sarooshi, 'The Essentially Contested Nature of the Concept of Sovereignty: Implications for the Exercise by International Organizations of Delegated Powers of Government' (2004) 25 *Michigan Journal of International Law* 1107, and John Jackson, 'Sovereignty Modern: A New Approach to an Outdated Concept' (2003) 97 *American Journal of International Law* 782, provide excellent legal studies on sovereignty. Jackson (790) argues that 'most (but not all) of the time that "sovereignty" is used in current policy debates, it actually refers to questions about the allocation of power'.

⁶ See UNGA Res 2625 (XXV), Declaration of Principles of International Law Concerning Friendly Relations and Cooperation among States in Accordance with the Charter of the United Nations, 24 October 1970.

⁷ See Steinberger, above note 4, 410. Sovereignty is defined in the *Black's Law Dictionary* as 'the supreme, absolute, and uncontrollable power by which any independent state is governed; supreme political authority; the supreme will; paramount control of the constitution and frame of government and its administration; the self-sufficient source of political power, from which all specified political parties are derived; the international independence of a state, combined with the right and the power of regulating its internal affairs without foreign dictation'.

⁸ See Vaughan Lowe, 'Sovereignty in International Economic Law' in Wenhua Shan, Penelope Simons and Dalvinder Singh (eds), *Redefining Sovereignty in International Economic Law* (Oxford: Hart Publishing, 2008) 84. Lowe and myself were the examiners of the PhD thesis presented by Claus Zimmermann on *A Contemporary Concept of Monetary Sovereignty*, which he successfully defended at the University of Oxford on 9 December 2011. An expanded and updated version of this thesis has been subsequently published by Oxford University Press in 2013 as a monograph bearing the same title. Zimmermann advocates that monetary sovereignty is not only a positive concept but also a normative concept expressing various sovereign values that, if properly analysed, provides regulatory guidance and acts as a legitimacy benchmark for the exercise of sovereign powers strictly speaking. He approaches monetary sovereignty as a dynamic and not as a static concept. He holds there is a common pattern in most of the existing literature to confound the erosion of formal State competencies with the erosion of sovereignty as a both positive and normative concept.

Monetary sovereignty

- 1.09** Monetary sovereignty is a particular attribute of the general sovereignty of the State under international law. Some authors argue that the concept of monetary sovereignty predates by thousands of years the concept of political sovereignty that was developed in the Renaissance, since the authority to create money had been proclaimed by the rulers or priesthood of ancient civilizations (Sumer, India, Babylon, Persia, Egypt, Rome, and others).⁹
- 1.10** However, the modern understanding of the attributes of sovereignty is rooted in the political thought that was developed in the Renaissance. The history and evolution of sovereignty is intrinsically linked to the history and evolution of the nation State. Both concepts were developed in Western Europe during the end of the fifteenth century and the sixteenth century.

C. History of Sovereignty

- 1.11** The writings of Machiavelli, Bodin, and Hobbes are of particular relevance to the understanding of the concept of sovereignty. Politics operated without this organizing principle in the Middle Ages. It is generally agreed that the development of a system of sovereign States culminated at the Peace of Westphalia in 1648.¹⁰

Sovereignty of the monarch

Bodin

- 1.12** Jean Bodin (1520–96) writings soon after the Massacre of the Huguenots on St Bartholomew's Day in 1572 developed in *Les Six Livres de la République* (1576) some of the key ideas that surround the concept of sovereignty. Bodin was concerned with internal order in a time of unrest and introduced his concept of sovereignty to bolster the power of the French king over the rebellious feudal lords and the church: 'It is clear that the principal mark of sovereign majesty . . . is the right to impose laws generally on all subjects regardless of their consent . . . If he is to govern the state well, a sovereign prince must be above the law.'¹¹

Bodin's concept of *sovereignty* (sovereignty) is often regarded as the first systematic one in modern European political philosophy and deserves a landmark status.¹²

⁹ See Robert A Mundell, 'Money and the Sovereignty of the State' in Axel Leijonhufvud (ed), *Monetary Theory and Policy Experience* (Basingstoke: Palgrave/International Economic Association, 2001) 298.

¹⁰ See Williams, above note 5, 111: 'It is difficult to date precisely when sovereignty became accepted and established. The Treaty of Westphalia (1648) is normally taken as the starting point of the European states system, i.e., a system of sovereign states owing allegiance to no superior.' However, it is worth recalling that Spain started operating as a nation State in 1492, following the union between Queen Isabella of Castile and King Ferdinand of Aragon. The latter is thought by some to have inspired the figure of the maverick Prince described in Machiavelli's acclaimed work.

¹¹ For a translation into English, see Jean Bodin, *The Six Books of the Commonwealth* (Oxford: Basil Blackwell, 1955) Book I (The Final End of the Well-Ordered Commonwealth: Concerning Sovereignty), at <http://www.constitution.org/bodin/bodin_.htm> (last visited 17 July 2014).

¹² See 'Sovereignty' in *Stanford Encyclopedia of Philosophy* (31 May 2003, rev 8 June 2010), at <<http://plato.stanford.edu/entries/sovereignty>> (last visited 17 July 2014). However, some authors argue that a contemporary of Bodin, François Grimaudet (1520–80), had already printed a book in 1560 that proclaimed the doctrine of sovereignty. See Mundell, above note 9, 302. Mundell also points out that Grimaudet in his treatise on 'The Law of Payment' stated: 'The value of money depends on the State; this is to say, in a monarchy,

Machiavelli

In the early sixteenth century, Niccolo Machiavelli (1469–1527) established some of the foundations of modern political philosophy in his work *The Prince* (1513).¹³ According to Machiavelli, princes should retain absolute control of their territories and should use any means of expediency to accomplish this end. He relied on his experience of politics and diplomacy in the city States of contemporary Italy and his sound knowledge of history to elaborate on the basic principles of statehood. His aim was to show how to build a strong principality through the use of effective statesmanship rather than the reliance on moral considerations. The thrust of his advice is that the sovereign should have supreme authority within his territory and his authority should lie beyond the reach of the rule of natural law, canon law, Gospel precepts, or any of the norms or authorities relating to the then powerful Christian tradition. The sovereign must demonstrate the readiness to perform evil as a necessary means to the ultimate end which was central to Machiavelli's writings: the strength and well-ordering of the State. He was supreme within the State's territory and responsible for the well-being of this singular, unitary body. Machiavelli did not purport to describe the nature of sovereignty and the content of the relationship between the sovereign and the people. He was primarily concerned with the preservation of that authority, providing advice as to the best model of government for the sake of the government's stability and not for the sake of the people's well-being. And he confined his attention to monarchical regimes rather than republics. Machiavelli is pragmatic rather than ideologist. Force and restraint, cruelty and kindness, must be employed in their turn when necessary to strengthen the authority of the monarch. He considers the creation of strong armies as the only necessary means of holding power and legal authority, leaving no doubt as to the importance of military power as source of sovereignty:

1.13

A Prince, therefore, should have no care or thought but for war, and for the regulations and training it requires, and should apply himself exclusively to this as his peculiar province; for war is the sole art looked for in one who rules, and is of such efficacy that it not merely maintains those who are born Princes, but often enables men to rise to that eminence from a private station; while, on the other hand, we often see that when Princes devote themselves rather to pleasure than to arms, they lose their dominions.¹⁴

Hobbes

The English philosopher Thomas Hobbes (1588–1679) further developed in *Leviathan* (1651) the notion of sovereignty, which he described as the absolute and unlimited rule or authority over the territory and the peoples in it. Though there is no direct reference to Bodin's writings in the pertinent paragraphs of *Leviathan*, there is a broad consensus among theorists that there is a sequence and a common understanding of concepts between the French and the English philosophers.¹⁵ Like Bodin (who wrote at a time of civil war in

1.14

upon the prince, and in an oligarchy, upon the State, which alone has the right to coin money or to have it coined and stamp a valuation upon it.'

¹³ Niccolo Machiavelli, *The Prince* in Charles W Eliot, *The Harvard Classics* (New York: Collier and Son, 1909–14) vol 36, Pt I, at <<http://www.bartleby.com/36/1/>> (last visited 17 July 2014).

¹⁴ Machiavelli, above note 13, ch 14, para 1.

¹⁵ See eg Joel Feinberg, 'Autonomy, Sovereignty and Privacy: Moral Ideals in the Constitutions?' (1983) 58 *Notre Dame Law Review* 445, 448; Jean Bethke Elshtain, 'Sovereign God, Sovereign State, Sovereign Self' (1991) 66 *Notre Dame Law Review* 1355, 1363; Rett R Ludwikowski, 'Supreme Law or Basic Law? The Decline of the Concept of Constitutional Supremacy' (2001) 9 *Cardozo Journal of International and Comparative Law* 253, 259; David Golove, 'The New Confederation: Treaty Delegations of Legislative, Executive and

France between Calvinist Huguenots and the Catholic monarchy) Hobbes also wrote at a time of civil war. He believed that absolute sovereignty of the State over the national territory was the only safeguard of a man's preservation: 'For where there is no Commonwealth, there is, as hath been already shown, a perpetual war of every man against his neighbour; and therefore everything is his that getteth it and keepeth it by force; which is neither propriety nor community, but uncertainty.'¹⁶

- 1.15** The life of human beings was full of dangers and human nature was weak and for that reason they agreed unconditionally to submit themselves to the absolute sovereignty of the State in exchange for guaranteed internal civil order and protection from external threats.¹⁷ Activities and events beyond national borders are not an issue unless other nations threaten to enter the sovereign territory. The Hobbesian concept of sovereignty in *Leviathan* is based upon the theoretical premise that within the sovereign boundaries a State is entitled to regulate the affairs of all individuals being subordinated thereto. Interestingly, Hobbes establishes in rather clear terms the concept of monetary sovereignty.¹⁸ Coinage and the creation of money as a means of exchange and a storage of value must belong to the sovereign. His understanding is rather modern, in the sense that he points out that the value of money is affected by the change of the laws in the country in which the money is created.

Judicial Authority' (2003) 55 *Stanford Law Review* 1697, 1705; Ronald A. Brand, 'Sovereignty: The State, The Individual and the International Legal System in the Twenty First Century' (2002) 25 *Hastings International and Comparative Law Review* 279, 282–3; Joan Fitzpatrick, 'Sovereignty, Territoriality and the Rule of Law' (2002) 25 *Hastings International and Comparative Law Review* 303, 308.

¹⁶ Thomas Hobbes, *Leviathan* (New York: Collier, 1962) 174.

¹⁷ Hobbes, above note 16, ch 17 ('Of the Causes, Generation and Definition of the Commonwealth').

¹⁸ Hobbes, above, note 16, 174–6:

By concoction, I understand the reducing of all commodities which are not presently consumed, but reserved for nourishment in time to come, to something of equal value, and withal so portable as not to hinder the motion of men from place to place; to the end a man may have in what place soever such nourishment as the place affordeth. And this is nothing else but gold, and silver, and money. For gold and silver, being, as it happens, almost in all countries of the world highly valued, is a commodious measure of the value of all things else between nations; and money, of what matter soever coined by the sovereign of a Commonwealth, is a sufficient measure of the value of all things else between the subjects of that Commonwealth. By the means of which measures all commodities, movable and immovable, are made to accompany a man to all places of his resort, within and without the place of his ordinary residence; and the same passeth from man to man within the Commonwealth, and goes round about, nourishing, as it passeth, every part thereof; in so much as this concoction is, as it were, the sanguification of the Commonwealth: for natural blood is in like manner made of the fruits of the earth; and, circulating, nourisheth by the way every member of the body of man. And because silver and gold have their value from the matter itself, they have first this privilege; that the value of them cannot be altered by the power of one nor of a few Commonwealths; as being a common measure of the commodities of all places. But base money may easily be enhanced or abased. Secondly, they have the privilege to make Commonwealths move and stretch out their arms, when need is, into foreign countries; and supply, not only private subjects that travel, but also whole armies with provision. But that coin, which is not considerable for the matter, but for the stamp of the place, being unable to endure change of air, hath its effect at home only; where also it is subject to the change of laws, and thereby to have the value diminished, to the prejudice many times of those that have it.

The conduits and ways by which it is conveyed to the public use are of two sorts: one, that conveyeth it to the public coffers; the other, that issueth the same out again for public payments. Of the first sort are collectors, receivers, and treasurers; of the second are the treasurers again, and the officers appointed for payment of several public or private ministers. And in this also the artificial man maintains his resemblance with the natural; whose veins, receiving the blood from the several parts of the body, carry it to the heart; where, being made vital, the heart by the arteries sends it out again, to enliven and enable for motion all the members of the same.

He notes that there are two methods by which money is made available for public use: the first is the transfer of money to the public coffers by way of taxation and the second is the reverse circulation of money from the government to the citizens by means of public payments. In that, the Leviathan (artificial man) ‘maintains his resemblance with the natural; whose veins, receiving the blood from the several parts of the body, carry it to the heart; where, being made vital, the heart by the arteries sends it out again, to enliven and enable for motion all the members of the same.’¹⁹

Sovereignty of the people

The advent of democracy as a political form of organizing the nation State and the theory of the division of powers signified an important evolution in the understanding of the notion of sovereignty and its roots. The various social contract theories consider that sovereignty resides originally in individuals (the will of the people), who are the principal sovereignty-holders. Rousseau’s social contract theory provides a fundamental basis for the modern understanding of the general will of the State, as representative of the will of its citizens. The individuals assemble or aggregate their individual wills into a unity: a general or collective will. The holder or bearer of such collective will (to whom individuals transfer their private will for the conduct of certain affairs) is the State, and its decisions require the agreement of the original sovereignty-holders. This is the basis of democratic legitimacy. **1.16**

Locke

John Locke (1632–1704), whose work *Two Treatises of Government* (1690) marked a clear departure from the Hobbesian notion of sovereignty, considers that sovereign authority is premised on the individual freedom of every person in the land to place the legislative power into the hands of few with the ‘great end’ of enjoying their properties in peace and safety. But the power is not absolute, defined merely by geographic sovereignty, but it is limited by the obligation of sovereign authorities to respect the rights of every citizen. This power cannot be exercised arbitrarily over the lives and fortunes of the people. **1.17**

For it being but the joint power of every member of the society given up to that person or assembly which is legislator, it can be no more than those persons had in a state of Nature before they entered into society, and gave it up to the community. For nobody can transfer to another more power than he has in himself, and nobody has an absolute arbitrary power over himself, or over any other, to destroy his own life, or take away the life or property of another. A man, as has been proved, cannot subject himself to the arbitrary power of another; and having, in the state of Nature, no arbitrary power over the life, liberty, or possession of another, but only so much as the law of Nature gave him for the preservation of himself and the rest of mankind, this is all he doth, or can give up to the commonwealth, and by it to the legislative power, so that the legislative can have no more than this.²⁰

Montesquieu

Charles de Montesquieu (1688–1755) examined extensively the notion of sovereignty, in *L’Esprit des lois* [*The Spirit of Laws*] (1748).²¹ Montesquieu considers three species of **1.18**

¹⁹ Hobbes, above note 16, 174–6.

²⁰ John Locke, *Two Treatises of Government* (New York: New American Library, 1965) Pt II (‘Of the Extent of Legislative Power’), para 135, at <<http://press-pubs.uchicago.edu/founders/documents/v1ch17s5.html>> (last visited 13 September 2014).

²¹ See Charles de Montesquieu, *The Spirit of Laws*, 2 vols (London: G. Bell & Sons, 1878 and 1909), also at <<http://www.constitution.org/cm/sol.txt>> (last visited 17 July 2014).

government: republican, monarchical, and despotic. A republican government is that in which the body, or only a part of the people, is possessed of the supreme power, sovereignty. When the body of the people is possessed of sovereignty, it is called a democracy. When the supreme power is lodged in the hands of a part of the people, it is then an aristocracy. In a democracy the people are in some respects the sovereign, and in others the subject.

- 1.19** There can be no exercise of sovereignty in a democracy unless expressed by the will of the people. The people, in whom the supreme power resides, ought to have the management of everything within their reach: that which exceeds their abilities must be conducted by their ministers. Montesquieu established the separation of the legislative, executive, and judicial functions of government in the following terms:

By virtue of the first, the prince or magistrate enacts temporary or perpetual laws, and amends or abrogates those that have been already enacted. By the second, he makes peace or war, sends or receives embassies; establishes the public security, and provides against invasions. By the third, he punishes criminals, or determines the disputes that arise between individuals. The latter we shall call the judiciary power, and the other simply the executive power of the state.²²

- 1.20** In the twenty-second book of *The Spirit of Laws*, *Of Laws in Relation to the Use of Money*, the idea of the sovereign's control over the use and regulation of money is pervasive. He immediately argues in favour of the use of money, particularly among commercial nations: 'When a nation traffics with a great variety of merchandise, money becomes necessary; because a metal easily carried from place to place saves the great expenses which people would be obliged to be at if they always proceeded by exchange.'²³

- 1.21** On the nature of money, he observes that money represents the value of all merchandise.²⁴ Metal is used as the sign of money 'because it is consumed little by use; and because, without being destroyed, it is capable of many divisions. A precious metal has been chosen as a sign, as being most portable. A metal is most proper for a common measure, because it can be easily reduced to the same standard.' And he notes the importance of governments almost naturally: 'Every state fixes upon money a particular impression, to the end that the form may correspond with the standard and the weight, and that both may be known by inspection only.'²⁵ He also provides an account of the exercise of the State prerogative over money throughout history.²⁶ He states: 'it would be an excellent law for all countries who

²² See Montesquieu, above note 21, vol I, Bk XI, 162–3.

²³ See Montesquieu, above note 21, vol II, Bk 22, ch 1 ('Of Law in Relation to the Use of Money') 81.

²⁴ Montesquieu, above note 21, vol II, Bk 22, ch 1 ('Of Law in Relation to the Use of Money') 82.

²⁵ Montesquieu, above note 21, vol II, Bk 22, ch 1 ('Of Law in Relation to the Use of Money') 82.

²⁶ Legislators have sometimes had the art not only to make things in their own nature the representative of specie, but to convert them even into specie, like the current coin. Cæsar, when he was dictator, permitted debtors to give their lands in payment to their creditors, at the price they were worth before the civil war (Cæsar, *Commentarii de Bello Civili*, iii). Tiberius ordered that those who desired specie should have it from the public treasury on binding over their land to double the value (Tacitus, *Annals*, vi 17). Under Cæsar the lands were the money which paid all debts; under Tiberius ten thousand sesterces in land became as current money equal to five thousand sesterces in silver. The Magna Charta of England provides against the seizing of the lands or revenues of a debtor, when his movable or personal goods are sufficient to pay, and he is willing to give them up to his creditors; thus all the goods of an Englishman represent money. The laws of the Germans constituted money a satisfaction for the injuries that were committed, and for the sufferings due to guilt. But as there was but very little specie in the country, they again constituted this money to be paid in goods or chattels. This we find appointed in a Saxon law, with certain regulations suitable to the ease and convenience of the several ranks of people. At first the law declared the value of a sou in cattle; the sou of two tremises answered to an ox of twelve months, or to a ewe with her lamb; that of three tremises was worth

are desirous of making commerce flourish to ordain that none but real money should be current, and to prevent any methods from being taken to render it ideal.²⁷

Hamilton

The Declaration of Independence of the United States of America and the Constitution of the United States reflected a notion of sovereignty clearly anchored upon the principles of democracy (the holders of sovereign power: ‘We the People...’) and the rule of law. Alexander Hamilton wrote illuminatingly in *The Federalist Papers* about the nature of sovereign power: **1.22**

[T]here is in the nature of sovereign power an impatience of control that disposes those who are invested with the exercise of it to look with an evil eye upon all external attempts to restrain or direct its operations. From this spirit it happens that in every political association which is formed upon the principle of uniting in a common interest a number of lesser sovereignties, there will be found a kind of eccentric tendency in the subordinate or inferior orbs by the operation of which there will be a perpetual effort in each to fly off from the centre. This tendency is not difficult to be accounted for. It has its origins in the love of power. Power controlled or abridged is almost always the rival and enemy of that power by which it is controlled or abridged.²⁸

Hamilton and Madison were concerned about the balance between the powers of the States and the powers of the Union (federal government). According to Hamilton, the powers of the Union (ie, the attributes of the sovereign power vested upon the federal Union) were: ‘the common defence of the members; the preservation of the public peace, as well against internal convulsions as external attacks; the regulation of commerce with other nations and between the States; the superintendance of our intercourse, political and commercial with foreign countries’.²⁹ **1.23**

Madison

According to Madison, the powers conferred on the government of the Union were: **1.24**

1. Security against foreign danger;
2. Regulation of the intercourse with foreign nations;
3. Maintenance of harmony and proper intercourse among the States;
4. Certain miscellaneous objects of general utility;
5. Restraint of the States from certain injurious acts;
6. Provisions for giving due efficacy to all these powers. The powers falling within the first class are those of declaring war and granting letters of marque; of providing armies and fleets; of regulating and calling forth the militia; of levying and borrowing money.³⁰

He includes the issuance of money (coins and paper money) as a prerogative of the Union on the basis that, ‘[h]ad every State right to regulate the value of its coin, there might be as many different currencies as States, and thus the intercourse among them would be impeded; **1.25**

an ox of sixteen months. With these people money became cattle, goods, and merchandise, and these again became money.

See Montesquieu, above note 21, vol II, Bk 22, ch 1 (‘Of Law in Relation to the Use of Money’) 83.

²⁷ Montesquieu, above note 21, vol II, Bk 22, ch 1 (‘Of Law in Relation to the Use of Money’) 84.

²⁸ See Hamilton et al, above note 1, 111.

²⁹ Hamilton et al, above note 1, 153.

³⁰ Hamilton et al, above note 1, 256.

retrospective alterations in its value might be made . . . and animosities be kindled among the States themselves.³¹

Alexis de Tocqueville

1.26 Alexis de Tocqueville³² wrote in *Democracy in America*:

In the United States, the sovereignty of the people is not an isolated doctrine, bearing no relation to the prevailing habits and ideas of the people; it may be regarded as the last link of a chain of opinions which binds the whole Anglo-American world. That Providence has given to every human being the degree of reason necessary to direct himself in the affairs that interest him exclusively is the grand maxim upon which civil and political society rests in the United States. The father of a family applies it to his children, the master to his servants, the township to its officers, the county to its townships, the state to the counties, the Union to the states; and when extended to the nation, it becomes the doctrine of the sovereignty of the people.³³

1.27 According to Tocqueville, '[t]he very essence of democratic government consists in the absolute sovereignty of the majority.' And he defined sovereignty as 'the right of making laws'.³⁴

1.28 This is the basis of modern constitutionalism: the rule of law and the sovereignty of the people, as original holders of such supreme power. The fact that power ultimately resides upon the people explains why such power can be restricted. Indeed, the attributes of sovereignty can also be curtailed if the people who hold such power so decide. The implications of European integration and other developments that have affected monetary sovereignty need to be understood in this light.

D. Money and Monetary Sovereignty under International Law: *Lex Monetæ*

The concept of money

1.29 The concept of money has different meanings in different contexts. Money in this book is primarily analysed as a creature of the law, whose existence must be understood within a legal framework.³⁵

The functions of money

1.30 The economic definition of money is typically functional, based upon the four basic functions of money: commonly accepted medium of exchange, means of payment, unit of account, and store of value. Of these functions, the defining feature of money is that of

³¹ Hamilton et al, above note 1, 282. The United States has had a common currency since 1863.

³² Alexis de Tocqueville (1805–59) came to the United States in 1831 and later wrote his two-volume study *Democracy in America*. The first volume was published in 1835 and the second one in 1940. I am quoting here from Alexis de Tocqueville, *Democracy in America* (New York: Vintage Classics, 1990).

³³ See Tocqueville, above note 32, 418.

³⁴ Tocqueville, above note 32, 254 and 123.

³⁵ For a comprehensive legal study of money (focusing on private law issues), see generally Frederick A Mann, *The Legal Aspect of Money*, 5th edn (Oxford: Clarendon Press, 1992) 461. Charles Proctor completed in 2005 an excellent revision of Mann's work, *Mann on the Legal Aspect of Money*, 6th edn (Oxford: Oxford University Press, 2005) and in 2012 the 7th edn (Oxford: Oxford University Press, 2012). I sometimes refer to the 5th edition in this chapter (Mann) and sometimes to the 6th edition (Proctor).

being a widely accepted means of exchange, which explains the dynamic character of money throughout history: from the sea salt used in Ancient Rome to pay the soldiers (hence the name salary), to a variety of commodities and precious metals over the centuries (with an intrinsic value), to the notes or paper money of today (with no intrinsic value, fiat money), as well as other forms such as electronic money. The current technological and financial innovations will undoubtedly continue to influence the evolution of the concept of money in future. The recent development of the so-called virtual currencies, a type of unregulated, digital money which is issued and controlled by its developers and used and accepted among the members of a special virtual community as a medium of exchange and unit of account, is an example of this evolution. Bitcoin (the online private crypto-currency), Second Life's virtual currency scheme, M-Pesa (the mobile payments solution pioneered in Kenya), and PayPal are amongst some of the innovations that are changing the traditional understanding of money.³⁶

In common parlance, money is often used as a general term to cover all financial assets. **1.31** For the purposes of the conduct of monetary policy, only some of those assets are included in the monetary aggregates used by the economists and the central banks to define the money supply (M1, M2, M3...). The concept of money supply is, however, different from the concept of money. Only the assets included in narrow definitions of the money supply (M1), namely currency in circulation and demand deposits, come closest to the definition of money as a means of payment.

Money and the law

The law tends to reflect a restrictive notion of money as 'currency' (physical notes and coins), **1.32** leaving aside other 'monetary assets' such as bank deposits. Since the monetary essence of currency rests upon the power of the issuer, that is, the State (fiat money), and since the State typically delegates this power to the central bank, which has the monopoly of note issue, the study of monetary law and the study of central banking law go hand in hand.

Though sometimes the notions of money and currency are used indistinctly, the concept of **1.33** money is broader than the concept of currency. The State can control the issue of currency within its territory, but the creation of money is not exclusively the monopoly of the State.

Economists tend to have a 'broader' understanding of the notion of money than lawyers do. **1.34** However, with regard to the functions of money, there is an element of increasing confluence between law and economics and that concerns the attention given in recent decades to the function of money as store of value. The value of money (in terms of purchasing power) has become a concern for lawyers, economists, and policy-makers.³⁷ The conduct

³⁶ See generally European Central Bank, 'Virtual Currency Schemes', Report (October 2012), at <<http://www.ecb.int/pub/pdf/other/virtualcurrencyschemes201210en.pdf>> (last visited 17 July 2014). In addition to virtual currencies, there are also parallel (local or regional) currencies, like the Brixton pound, the Bristol pound or the Lewes pound. See also Peter Sands, 'Banking is Heading Towards its Spotify Moment' *Financial Times* (28 June 2013).

³⁷ See Antonio Sainz de Vicuña, 'An Institutional Theory of Money' in Mario Giovanoli and Diego Devos (eds), *International Monetary and Financial Law: The Global Crisis* (Oxford: Oxford University Press, 2010) 517; and 'The Concept of Money in the XXIst Century', paper presented at the Committee on International Monetary Law of the International Law Association (MOCOMILA) meeting, Tokyo (1 April 2004). In this latter paper Antonio Sainz de Vicuña stated: 'A currency is trusted by society and markets, when there is an institutional framework that ensures preservation of purchasing capacity, ie price stability. Money is then defined as the dematerialized "commodity" produced and managed by central banks that serves the function of store of value.'

of a price-stability oriented monetary policy by an independent central bank (which I discuss in depth in Chapter 2) is today enshrined in a legal framework, which adds a new dimension to the role of the State in monetary affairs. In this context, the growth of money in circulation, the choice of exchange regime, and other economic and financial issues which have a bearing on the 'value of money' are also relevant for lawyers.

- 1.35** Public international law, as I explain below, focuses on the issue and regulation of money by the State. Private law, on the other hand, focuses on the notion of payment and the function of money as a means of payment,³⁸ and on the protection of the private rights of contracting parties and the discharge of monetary obligations.³⁹ If the notion of money is unsettled, so is the notion of payment. Payment has been defined as an act, such as the transfer of money, which discharges the debt.⁴⁰ Goode defines payment (settlement) as any act accepted in performance of a monetary obligation.⁴¹ The private law of monetary obligations exceeds, however, the scope of my study.⁴²

Monetary sovereignty under public international law

- 1.36** The state sovereignty over the State's currency, that is, the power to issue and regulate money, is traditionally recognized by public international law.⁴³ In 1929, the Permanent Court of International Justice stated that 'it is indeed a generally accepted principle that a state is entitled to regulate its own currency.'⁴⁴
- 1.37** This judgment is cited as authority of the State's sovereignty over its currency.⁴⁵ Treves,⁴⁶ however, argues that the interpretation of the notion of sovereignty has changed since 1929, and that the Court's statement 'can only be accepted as a figure of speech' and not as a 'right' of States.

[S]tate 'sovereignty' belongs to the area of fact and not to the area of law. Sovereignty as the stable and undisturbed exercise of power within a given territory is seen as a factual situation from whose existence international law draws consequences which are the rights and obligations of states, in particular the state's right not to suffer interference from other states in the exercise of the power and the obligation of other states not to interfere with the exercise of the power of the sovereign state.⁴⁷

³⁸ Without a means of payment and a unit of account, our system of trade and commerce would have to revert to barter (or counter-trade).

³⁹ See Proctor, 6th edn, above note 35, Pts II and III, for a lucid analysis of these issues.

⁴⁰ See Proctor, 6th edn, above note 35, 160 n 2.

⁴¹ See Roy Goode, *Commercial Law*, 2nd edn (London: Penguin Books, 1995) 501.

⁴² See Proctor, 6th edn, above note 35, Pts II and III.

⁴³ See Mann, 5th edn, above note 35, 461. See also Proctor, 6th edn, above note 35, 500.

⁴⁴ *Case Concerning the Payment in Gold of Brazilian Federal Loans Contracted in France (France v Brazil)*, Judgment, 12 July 1929, PCIJ Ser A No 21, 44–5, at <http://www.worldcourts.com/pcij/eng/decisions/1929.07.12_payment2.htm/> (last visited 17 July 2014) and *Case Concerning the Payment of Various Serbian Loans Issued in France (France v The Kingdom of the Serbs, Croats and Slovenes)*, Judgment, 12 July 1929, PCIJ Ser A No 21, 122, at <http://www.worldcourts.com/pcij/eng/decisions/1929.07.12_payment1.htm/> (last visited 17 July 2014).

⁴⁵ See Mann, 5th edn, above note 35, 461 and Proctor, 6th edn, above note 35, 500. See also Geneviève Burdeau, 'L'exercice des compétences monétaires par les États' (1988) 212 *Recueil des Cours* 211, 236; Dominique Carreau, *Souveraineté et Coopération Monétaire Internationale* (Paris: Cujas, 1970) 52–4; and Milan Robert Shuster, *The Public International Law of Money* (Oxford: Clarendon Press, 1973) 9.

⁴⁶ See Tullio Treves, 'Monetary Sovereignty Today' in Mario Giovanoli (ed), *International Monetary Law: Issues for the New Millennium* (Oxford: Oxford University Press, 2000) 111–18.

⁴⁷ Treves, above note 46, 112.

Burdeau accepts the Court's submission with no further comment,⁴⁸ and the same applies for Mann.⁴⁹ Mann contends that every country has exclusive authority to replace its currency with a new currency and to fix the conversion of the old currency in relation to the new one.⁵⁰ **1.38**

Monetary sovereignty has a territorial dimension. The law of the currency is always confined to a territory. It can only be enforced in that territory.⁵¹ This territoriality does not preclude a voluntary surrender of sovereignty. But it implies that 'limitations to sovereignty cannot be presumed'.⁵² **1.39**

Lex monetae and legal theories of money

The 'State theory of money' holds that it is the jurisdiction of issue of a currency which determines what is to be considered money and what nominal value it has ('only those chattels are money to which such character has been attributed by law'). Money is only what is recognized as such by the laws of a State. **1.40**

The best known proponent of the theory of *lex monetae* (literally, law of the currency) is Mann, who developed it—as Proctor points out—in the light of the universal acceptance of the principle of 'nominalism', which establishes that the parties contract by reference to a currency, irrespective of any fluctuations that may occur in the value of the currency between the time the debt was incurred and the time of payment.⁵³ 'The principle of nominalism precludes the argument that a payment of a monetary obligation has become impossible. Monetary obligations are "indestructible". If a currency system become extinct, the amount payable by the debtor will be ascertained to the recurrent link',⁵⁴ as indeed happened with advent of the euro in 1999. **1.41**

The State theory of money—recognized in modern constitutions⁵⁵—has been typically construed as a necessary consequence of the sovereign power over currency. With regard to **1.42**

⁴⁸ See Burdeau, above note 45, 236.

⁴⁹ See Mann, 5th edn, above note 35, 461 and Proctor, 6th edn, above note 34, 500.

⁵⁰ Mann noted that the right to replace a national currency in many respects flowed from the universal recognition of the principle of nominalism: Mann, 5th edn, above note 35, 272. The same point finds voice in the *lex monetae* principle; see Proctor, 6th edn, above note 35, 332–3.

⁵¹ See Treves, above note 46, 117: '[B]ecause any reference to a monetary unit automatically entails a reference to the rules that define it, the rules on legal tender and those involving the exercise of the powers of public authorities are territorial, in the sense that they can be enforced in the territory of the state of the country.'

⁵² Treves, above note 46, 112.

⁵³ See Proctor, 6th edn, above note 35, 16 and 225–8.

⁵⁴ Proctor, 6th edn, above note 35, 339–40.

⁵⁵ For example, see the US Constitution, Art 1, s 5, paras 5–6: 'The Congress shall have the power . . . 5. To coin money, regulate the value thereof, and of foreign coin, and fix the standard of weights and measures. 6. To provide for the punishment of counterfeiting the securities and current coin of the United States.' Though the power to issue currency has been transferred from the national to the supranational arena in the European Union since the advent of European Monetary Union, it is useful to recall that European constitutions have referred to the State prerogative over monetary affairs in clear terms. See eg the German Constitution (*Grundgesetz*), Art 73(4): 'The Federation has exclusive power to legislate in the following matters: 4. currency, money and coinage, weights and measures, as well as the determination of standards of time'; the French Constitution, Art 34 (Legislative Powers): '(1) All legislation shall be passed by Parliament. (2) Legislation shall establish the rules concerning: . . . the assessment bases, rates, and methods of collecting taxes of all types; the issuance of currency'; the Italian Constitution, Art 117(2)(e): 'The state has exclusive legislative power in the following matters . . . e) money, protection of savings, financial markets; protection of competition; currency system; state taxation system and accounting; equalization of regional financial resources'; the Spanish Constitution, Art 149(1)(11): 'The State—central government—has exclusive power

the acceptance of this theory in US law and doctrine, Wahlig points out that ‘*lex monetae* is also recognised (even if not under this designation) in the United States, in the guise of the “act of state doctrine” or also the “state theory of money”.’⁵⁶

- 1.43** The scope of *lex monetae* has been debated in the legal literature. As I further contend below, I support a broad interpretation of the State theory of money. Strictly speaking, it has been argued that *lex monetae* should be distinguished from *lex contractus* (or *lex causae*) which refers to the substantive law applied to a contract as a result of the parties’ choice of law,⁵⁷ an issue which was discussed with regard to the continuity of contracts in the context of European Monetary Union, following the substitution of national currencies by the euro. Under the theory of *lex monetae*, judges must recognize the validity of the monetary law of other States. A distinction can be drawn—as Jean Victor Louis points out—between a narrow concept of *lex monetae* limited to the definition of a currency in a given territory and its relationship with the currency it may replace, and a broader concept that covers the provisions adopted by a State with regard to the regulation of its currency.⁵⁸
- 1.44** According to Mann, each sovereign State possesses the exclusive sovereign power to determine what constitutes legal tender within its territory and what the nominal value of that currency is. The definition of legal tender acts as a legal barrier imposed by the authorities against the use of currency substitutes (such as foreign currencies and gold) to settle debts.
- 1.45** Mann considers that money, like tariffs or taxation or the admission of aliens, is one of those matters which, *prima facie*, must be considered as falling within the exclusive domestic jurisdiction of States.⁵⁹ This means that the State’s exclusive right to regulate its money would fall under Article 2(7) of the Charter of the United Nations, which states:⁶⁰

Nothing contained in the present Charter shall authorize the United Nations to intervene in matters which are essentially within the domestic jurisdiction of any state or shall require the Members to submit such matters to settlement under the present Charter; but the application of this principle shall not prejudice the application of enforcement measures under Chapter VII [which refers to ‘Action with Respect to Threats to the Peace, Breaches of the Peace and Acts of Aggression’].

- 1.46** Essentially, any reference to a monetary unit entails automatically a reference to the municipal laws that define it. But the rules on legal tender and those aspects of the law of the currency involving the exercise of powers by the State may only be enforced within the territorial boundaries of its jurisdiction.

over the monetary system’; the Greek Constitution, Art 80(2): ‘A law shall provide for the minting of issuance of currency’.

⁵⁶ See Bertold Wahlig, ‘European Monetary Law: the Transition to the Euro and the Scope of *Lex Monetae*’ in Giovanoli (ed), above note 46, 123. The act of State doctrine maintains that a nation is sovereign within its own borders, and its domestic actions may not be questioned in the courts of another nation.

⁵⁷ See Michael Gruson, ‘The Scope of *Lex Monetae* in International Transactions: a United States Perspective’ in Giovanoli (ed), above note 46, 434–5.

⁵⁸ See Jean Victor Louis, ‘The New Monetary Law of the European Union’ in Mario Giovanoli (ed), above note 46, 154.

⁵⁹ See Mann, 5th edn, above note 35, 462.

⁶⁰ Wahlig, above note 56, 123, points out that Hugo Hahn also considers the currency-issuing State’s exclusive right to regulate its money as covered by the Charter of the United Nations (signed 26 June 1945, entered into force 24 October 1945), 1 UNTS 16, Art 2, para 7.

With regard to the fate of national monetary law outside the boundaries of the State, Mann cites a few cases where it was held that the domestic monetary legislation applies only internally and does not affect contracts denominated in the currency if entered into before the enactment of the legislation. In his view, there cannot be any doubt that attempts to limit the international recognition of monetary changes must today be considered as obsolete and extravagant. Both national and international law recognize the right of the State to depreciate its own currency. Further, a State is within its rights to bring about the external devaluation of its currency.⁶¹ Mann also contends that there is much authority in support of the further right of the State to introduce exchange controls at its discretion with all its incidental ramifications.⁶² Of course, as discussed later in this book, such powers are curtailed if the State is part of a monetary union. The imposition of exchange controls by one of the Member States participating in EMU (Cyprus in 2013) is most controversial and raises significant legal and economic issues. **1.47**

With regard to the question of whether the issuer of a currency may prohibit the use of its currency by another country,⁶³ there is at present no basis in international law to support the view that the issuer may object to the currency being used by other countries. In the UK and in the USA, the courts have explicitly recognized the unfettered right of the sovereign (monarch or Congress) to grant legal tender status to specified foreign currencies, without requiring the consent of the issuer.⁶⁴ **1.48**

The ‘State theory of money’ contrasts with the ‘societary theory of money’, which considers that the attribution of the character of money derives from the usages of commercial life, and of practices in society in general, irrespective of the intervention of the State.⁶⁵ Another expression of the ‘societary theory of money’ is provided by Antonio Sainz de Vicuña, who advocates an ‘institutional theory of money’ in which money is not limited to ‘cash’, but encompasses a dematerialized concept (called ‘scriptural money’, which includes demand deposits with credit institutions). This is based on the small proportion of money physically represented in banknotes and coins, as compared with the generalized use of the banking system for holding money and for payments. The wide acceptance and use by society of scriptural money is based on an institutional framework of two pillars: (i) an independent central bank that ensures the stability of the purchasing capacity of money and its sound use as means of payment, and (ii) a legislative framework that supports such independence, the solvency and liquidity of credit institutions, and the reliability of scriptural money as **1.49**

⁶¹ See Mann, 5th edn, above note 35, 464–5. The same point is reflected in the sixth edition by Proctor, 6th edn, above note 35, 505–6.

⁶² See Mann, 5th edn, above note 35, 467, with references to the British, Canadian, and US authorities and the International Claims Commission.

⁶³ See generally François Gianviti, ‘Use of a Foreign Currency under the Fund’s Articles of Agreement’ (17 May 2002), at <<http://www.imf.org/external/np/leg/sem/2002/cdmfl/eng/gianvi.pdf>> (last visited 17 July 2014).

⁶⁴ See in the UK the *Wade* case ([1601] 77 ER 232) and in the USA, the *Tyson v United States* case (285 F 2d 19 (1960)). As Lee Buchheit pointed out to me in private correspondence, Ecuador’s surprise announcement in early 2000 that it had dollarized its economy was done without consulting the United States.

⁶⁵ See Mann, 5th edn, above note 35, 12–14. See also René Smits, *The European Central Bank. Institutional Aspects* (The Hague: Kluwer Law International, 1997) 194 n 186. The societary theory of money first appeared in the literature with Friedrich Carl von Savigny in the first half of the nineteenth century and has been developed further by Arthur Nussbaum in his treatise *Money in the Law—National and International* (Brooklyn: The Foundation Press, Inc, 1950).

means of payment.⁶⁶ He considers that the concept of legal tender is obsolete in view of the overwhelming use of scriptural money in today's economy, the limitation of the use of cash to the settlement of petty transactions, and the general need for consent by the creditor for the settlement of debts in cash. The concept of legal tender is thus limited to the official standardization of the design and the features of cash. The value of money is dependent, in a world of no absolute anchors, on such an institutional framework only.⁶⁷

- 1.50** Though the societary theory of money provides an important complementary approach to the legal study of money, as long as we have a system in which the State keeps an important role in money creation (with regard to the issue of currency), control of the money supply through monetary policy (a function entrusted to a central bank, usually with independence from political instruction, yet a State function), and a certain degree of control over the banking and financial system through regulation and supervision and oversight of payment systems, the State theory of money—broadly understood as the public legal framework in which the economic institutions of money and central banking operate—remains valid in my opinion.

E. The Attributes of Monetary Sovereignty

- 1.51** The notion of monetary sovereignty is not expressly recognized or defined as such in the Charter of the United Nations, nor in the Article of Agreement of the International Monetary Fund, nor in other key instruments of international law.⁶⁸

It has been argued in the legal literature that monetary sovereignty includes the power to issue the currency, to define the monetary unit and the notes and coins in multiples of that unit, to require that payments in such notes and coins must be accepted as legal tender, to decide whether or not the currency should be based on gold or silver, to depreciate and appreciate the value of the currency, to impose exchange controls, and to take other measures affecting the monetary system or monetary relations.⁶⁹ Zimmermann views monetary sovereignty in two ways; on the one hand, from the perspective of the 'supreme and irreducible authority of independent states' and, on the other hand, from the perspective of the 'various sovereign powers' (or attributes) that can be exercised by different levels of governance (notion of 'cooperative sovereignty'). According to this view, in a monetary union like EMU, what has been transferred from the national to the supranational level is the exercise of some sovereign powers or 'state competences', but not 'monetary sovereignty' per se.⁷⁰

In the economic literature, Nobel laureate Mundell, bearing in mind the functions of money, argues that monetary sovereignty comprises the right to determine what constitutes

⁶⁶ See Sainz de Vicuña, 'The Concept of Money in the XXIst Century', above note 37.

⁶⁷ Sainz de Vicuña, 'The Concept of Money in the XXIst Century', above note 37.

⁶⁸ See Burdeau, above note 45, 236–7.

⁶⁹ See Mann, 5th edn, above note 35, 461–2 and Treves, above note 46, 117.

⁷⁰ See Claus D Zimmermann, 'The Concept of Monetary Sovereignty Revisited' (2013) 24(3) *European Journal of International Law* 797. While I find this study well written and insightful, I disagree with his observation (799 n 10 and 800 n 11) that I somehow approach monetary sovereignty as a static, positive concept, as a mere catalogue of State competences. I contend that both sovereignty, in general, and monetary sovereignty, in particular, are dynamic concepts that change over time. Indeed, my research in monetary law in general, supports the evolving nature of such law.

the unit of account, the right to determine the means of payment—legal tender for the discharge of debt—and the right to produce money.⁷¹ He argues that the most important dimension of this monetary sovereignty is the right of a State to declare that which counts as legal tender.⁷²

In my view, monetary sovereignty includes:

1.52

- (1) The power to issue notes and coins. The prerogative of issuing currency (*ius cudendae monetae*) is a classic attribute of monetary sovereignty. This power is typically a monopoly power, exercised by a country's central bank.⁷³ A national currency is both a symbol and a tool of national identity. A currency, like a language, like a flag, can stimulate the cohesion among a group of people and build a nation. Indeed, following the break-up of the Soviet Union in 1991, the nascent republics were keen—as a manifestation of their newly gained independence and an assertion of their sovereignty—to issue their own currency and to establish their own central bank. There are other benefits related to the issue of currency, such as the potential for generating seigniorage revenues.
- (2) The power to regulate money (to dictate laws and regulations that affect the external or internal dimension of money), the banking system (regulation of credit), and the payment system (clearing and settlement).
- (3) The power to control the money supply and interest rates (monetary policy). This power is typically delegated to a central bank. The standard instruments of a market oriented monetary policy (open market operations, discount policies, and reserve requirements) also provide the central bank with a degree of flexibility in dealing with banking problems (including the power to act as lender of last resort, as further explained in Chapter 4).
- (4) The power to control the exchange rate and to determine the exchange regime (exchange rate policy). Responsibility for the formulation of exchange rate policy usually rests with the government, though its implementation is often entrusted to the central bank. The central bank often manages the official monetary reserves (both gold reserves and foreign currency reserves), which are generally owned by the government.
- (5) The power to impose exchange and capital controls. Though this imposition runs counter to the objectives of trade liberalization, it remains a tool of monetary sovereignty,⁷⁴ albeit a controversial one, opposed by the advocates of unrestricted capital movements or 'capital account convertibility' as further discussed in Chapter 13.⁷⁵

⁷¹ See Mundell, above note 9, 303.

⁷² Mundell, above note 9, 303–4.

⁷³ There is no compelling case for governments to monopolize the production of shoes, sausages, or steel. The experience of the centrally planned economies showed that monopoly decision-making in economic affairs obstructs the creation of wealth, not just for a few, but for all. Why should monopoly decision-making in money be an exception? I discuss this issue, and the proposals of the so-called 'free banking economists' that advocate competition in currency in Rosa M Lastra, *Central Banking and Banking Regulation* (London: Financial Markets Group/London School of Economics, 1996) 252–7.

⁷⁴ Treves, above note 46, 115–16, points out that following the imposition of controls on capital movements by Malaysia (one of the States involved in the Asian Crisis in the late 1990s) the International Monetary Fund's directors broadly agreed 'that the regime of capital controls— which was intended by the authorities to be temporary—had produced more positive results than many observers had initially expected'. Monetary sovereignty with regard to the control of capital movements had shown its strength.

⁷⁵ With regard to capital account convertibility, see Cynthia Lichtenstein, 'International Jurisdiction over International Capital Flows and the Role of the IMF: Plus ça change?' in Giovanoli (ed), above note 46.

- 1.53** Does monetary sovereignty include the power to discriminate against foreign nationals (or in favour of their own nationals)? This is a thorny issue, because though *de jure* it can be argued that this alleged power runs counter to the principles of international law,⁷⁶ de facto it remains true that sovereign States do within their territory enact laws that prejudice against foreign nationals, implicitly or explicitly. Freezing orders—of assets—unilaterally imposed are an example of the coercive power of the State within its own territory, when security or political considerations prevail.⁷⁷ Other examples of unilateral decisions taken by sovereign States—often in flagrant violation of their international obligations—include the confiscation of monetary assets (expropriation without compensation) and the repudiation of external debt obligations.
- 1.54** Mann argues that monetary sovereignty needs to be exercised by the State in accordance with the principles of customary international law: ‘While normally the State is entitled at its discretion to regulate its monetary affairs, there comes a point when the exercise of such discretion so unreasonably or grossly offends against the alien’s right to fair and equitable treatment or so clearly deviates from customary standards of behaviour that international law will intervene.’⁷⁸

Monetary laws must be in accordance with public international law. As Mann explains, ‘monetary laws are fully capable of giving rise to legal disputes concerning international law within the meaning of Article 36(2) of the Statute of the International Court of Justice.’⁷⁹ This Article reads as follows:

The states party to the present Statute may at any time declare that they recognise as compulsory *ipso facto* and without special agreement, in relation to any other state accepting the same obligation, the jurisdiction of the Court in all legal disputes concerning:

- (a) the interpretation of a treaty;
- (b) any question of international law;
- (c) the existence of any fact which, if established, would constitute a breach of an international obligation;
- (d) the nature or extent of the reparation to be made for the breach of an international obligation.

- 1.55** In the *Case of Certain Norwegian Loans*,⁸⁰ cited by Mann, the Court held that ‘the question of conformity of national legislation with international law is a matter of international law.’⁸¹

⁷⁶ With regard to the ‘non-discrimination obligation in customary international law’, John Jackson remarks: ‘From time to time it is argued that countries are obliged under customary international law to extend non-discriminatory treatment to other nations. Prior to World War I, there was no such obligation.’ As summarized by Professor Georg Schwarzenberger, customary law of the time recognized that: ‘Freedom of commerce is a purely optional pattern of international economic law.’ See John Jackson, William Davey, and Alan Sykes (eds), *Legal Problems of International Economic Relations*, 3rd edn (St Paul, MN: West Publishing Co, 1995) 443.

⁷⁷ See Treves, above note 46, 118. Treves also refers to freezing orders in implementation of sanctions imposed by the UN Security Council.

⁷⁸ Mann, 5th edn, above note 35, 472–3. Proctor argues for a distinction between the internal and external aspects of monetary sovereignty, and argues that the external aspects may be more amenable to challenge by other States: Proctor, 6th edn, above note 35, 501–2.

⁷⁹ Mann, 5th edn, above note 35, 468.

⁸⁰ *Case of Certain Norwegian Loans (France v Norway)* [1957] ICJ Rep 9.

⁸¹ See Mann, 5th edn, above note 35, 468–9.

F. The Erosion of Monetary Sovereignty

The monopoly power enjoyed by the State with regard to the issue and regulation of money within its territory has been eroded or limited by a number of considerations in recent years. Some of those limitations are consensual, a voluntary surrender of monetary sovereignty, and some others have not been agreed by the State/s, but are the result of globalization, the information revolution, and of economic and financial developments in the last three decades. **1.56**

The erosion of monetary sovereignty is related to the erosion of the general sovereignty of the State. Though nation States remain the main actors in the international community, power today is no longer the exclusive domain of the nation State.⁸² Centripetal and centrifugal forces have diffused the power of the nation State, and today a variety of actors, including international organizations, multinational corporations, regions, local communities, and the civil society also exercise power. **1.57**

The State no longer monopolizes the supreme and exclusive power to control affairs in a given territory. If we look at the different types of power that the State can hold: political power, military power, economic power, we realize that even if some States still reign supreme within the territory of their jurisdiction in the political and military arena (though in the case of a federal state, political power is shared, and in the case of a military alliance or a defence organization, sovereignty is pooled, as with the North Atlantic Treaty Organization (NATO)), in the economic arena few States can claim to be sovereign nowadays. States need to comply with their international economic commitments, regarding trade, investment, finance, and others.

As I have already discussed, a national currency can be an expression, a symbol of national identity and national pride. However, there is nothing sacrosanct about money nor about monetary sovereignty. In a way, there is nothing unique about this process. Other symbols of national identity (even if not so closely associated with the notion of sovereignty as money is) have also lost their sparkle in recent years: airlines used to be seen as a matter of symbolic pride for the citizens of a State. No longer: the advent of privatization and the upheaval in the airline industry in recent years have changed that perception. **1.58**

Voluntary or consensual limitations of monetary sovereignty

The advent of European Monetary Union

At a regional level, the most clear example of consensual limitations of monetary sovereignty is the establishment of EMU in 1999. The adoption of a single currency, the euro, and the creation of the European System of Central Banks with responsibility to formulate and implement the monetary policy of the Community have been described as 'the most profound limitation to monetary sovereignty ever to be agreed by sovereign states'.⁸³ Member States participating in EMU agreed to transfer sovereign rights to the European **1.59**

⁸² See Kenichi Ohmae, *The End of the Nation-State* (New York: Simon and Schuster, 1996) and Susan Strange, *The Retreat of the State: The Diffusion of Power in the World Economy* (Cambridge: Cambridge University Press, 1996).

⁸³ See Treves, above note 46, 116.

Union. Of course, the surrender of monetary sovereignty does not imply the erosion of national sovereignty in other respects. It is a limited surrender, a non-exclusive transfer of sovereign powers. The members of the Euro zone retain their national sovereignty in those domains where no other consensual limitation has been agreed.⁸⁴

- 1.60** Member States participating in EMU have given up their national currencies. I contend that the bearer, the holder of monetary sovereignty is not the ECB, but the Member States of the European Union that have adopted the single currency (the euro area as such does not have legal personality).⁸⁵ The Union's 'exclusive competence' in monetary policy is exercised by the ESCB as I explain in Chapter 7.

However, the language of the Treaty with regard to the exchange rate policy and the external aspects of the euro is characterized by a notorious lack of clarity, as further discussed in Chapter 9.⁸⁶

- 1.61** Other 'attributes of monetary sovereignty' (as spelt out above) have remained at the national level during the first years of the life of EMU, though 'banking union', discussed in the second part of the book (Chapter 10), represents a further transfer of monetary sovereignty to the ECB, with the ECB playing the key role in banking supervision—according to the Single Supervisory Mechanism (SSM) Regulation—in the participating Member States.

- 1.62** There is no provision in the Treaty which permits the revocation of EMU. However, the new Article 50 of the Lisbon Treaty foresees the possibility of exiting the EU altogether.⁸⁷

⁸⁴ The European Court of Justice ruled in the *Costa v Enel* case that 'by creating a Community of unlimited duration, having its own institutions, its own personality, its own legal capacity and capacity of representation on the international stage and, more particularly, real powers stemming from a limitation of sovereignty or a transfer of sovereign powers from the States to the Community, the Member States have limited their sovereign rights, albeit within limited fields, and have thus created a body of law which binds their nationals and themselves.' See Case 6/64 *Costa v Enel* [1964] ECR 585, 593 para 9.

⁸⁵ This is in line with the established doctrine of monetary sovereignty, where the State, as representative of the will of the people, is the holder of such sovereignty, even if the exercise of some of its prerogatives—such as the monopoly of note issue—is the responsibility of the central bank. Regarding the constitutional position of the European Central Bank, which I further discuss in Chapter 7, see eg Chiara Zilioli and Martin Selmayr, 'The European Central Bank: an Independent Specialized Organization of Community Law' (2000) 37 *Common Market Law Review* 591 and René Smits, 'The European Central Bank in the European Constitutional Order', Inaugural Lecture at the University of Amsterdam (4 June 2003), subsequently published as René Smits, *The European Central Bank in the European Constitutional Order* (Utrecht: Eleven International Publishing, 2003).

⁸⁶ See Kathleen McNamara and Sophie Meunier, 'Between National Sovereignty and International Power: what external voice for the Euro?' (2002) 78 *International Affairs* 849.

⁸⁷ Treaty of Lisbon Amending the Treaty on European Union and the Treaty Establishing the European Community, 13 December 2007, OJ C 306/1 ('Lisbon Treaty'), Art 50 reads as follows:

1. Any Member State may decide to withdraw from the Union in accordance with its own constitutional requirements.
2. A Member State which decides to withdraw shall notify the European Council of its intention. In the light of the guidelines provided by the European Council, the Union shall negotiate and conclude an agreement with that State, setting out the arrangements for its withdrawal, taking account of the framework for its future relationship with the Union. That agreement shall be negotiated in accordance with Article 218(3) of the Treaty on the Functioning of the European Union. It shall be concluded on behalf of the Union by the Council, acting by a qualified majority, after obtaining the consent of the European Parliament.
3. The Treaties shall cease to apply to the State in question from the date of entry into force of the withdrawal agreement or, failing that, two years after the notification referred to in paragraph 2,

Furthermore, it can be argued that there are legal mechanisms that already exist in EU law for one or more Member States to leave the Eurozone under Article 352 TFEU (thus the orderly consensual departure—or a ‘temporary exit’—of one or more periphery States remains a legal possibility, according to some commentators).⁸⁸

The wording ‘irrevocably fixed’ adopted by the Maastricht Treaty suggests that EMU is ‘a trip with no return’, but the Member States retain—as a residual attribute of their sovereignty—the possibility of reversing the current status quo by unanimous agreement (ie, by signing a new Treaty to that effect).⁸⁹ Furthermore, in the exercise of sovereign rights, individual Member States of the euro area may choose to ignore the obligations of the Treaty (notwithstanding the illegality of this action) and abandon the monetary union. The latter has been proposed by several commentators following the sovereign debt and financial crises in several Member States of the euro area. History teaches us that countries have ignored and repudiated international obligations before. Revolutions and *coups d’état* are notorious examples of such repudiation. And the USA itself ignored the Articles of Agreement of the International Monetary Fund (IMF) when it de facto abandoned the par value regime in 1971, as further discussed in Chapter 12.⁹⁰

1.63

International obligations: The IMF Articles of Agreement

At the international level, the most relevant example of consensual limitations to the monetary sovereignty of States is the Articles of Agreement of the International Monetary Fund.⁹¹ These limitations were greater with the par value regime under the original Articles

1.64

unless the European Council, in agreement with the Member State concerned, unanimously decides to extend this period.

4. For the purposes of paragraphs 2 and 3, the member of the European Council or of the Council representing the withdrawing Member State shall not participate in the discussions of the European Council or Council or in decisions concerning it.

A qualified majority shall be defined in accordance with Article 238(3)(b) of the Treaty on the Functioning of the European Union.

5. If a State which has withdrawn from the Union asks to rejoin, its request shall be subject to the procedure referred to in Article 49.

For an analysis of Article 50 and other legal scenarios, see generally Phoebus Athanassiou, ‘Withdrawal and Expulsion from the EU and EMU: Some Reflections’, ECB Working Paper No 10 (December 2009), at <<http://www.ecb.int/pub/pdf/scplps/ecblwp10.pdf>> (last visited 17 July 2014). This is also discussed in Chapter 7.

⁸⁸ See Tolek Petch, *Legal Aspects of the Eurozone Crisis* (London: Slaughter and May, 2012) 158–9, para 4.32:

There are four cumulative requirements before recourse may be made to Article 352. First, action by the EU must be necessary. Secondly, that action must be within the framework of the policies defined in the Treaties. Thirdly, it must be necessary to attain one of the objectives set out in the Treaties. Finally, the Treaties must not have provide the necessary powers.

⁸⁹ See Treves, above note 46, 116 and Christoph W Herrmann, ‘Monetary Sovereignty over the Euro and the External Relations of the Euro Area: Competences, Procedures and Practice’ (2002) 7 *European Foreign Affairs Review* 4. For an opposite view, see Zilioli and Selmayr, above note 85, 604.

⁹⁰ Zimmermann, above note 70. In response to ‘the question as to whether, absent an express treaty rule authorizing a unilateral withdrawal, a member state of a supra-national organization may nevertheless assert its sovereignty by withdrawing from the organization’ (815), Zimmermann suggests that any Member State (Greece for example) ‘may always decide to breach the rules of the monetary union and leave’ and also that, in line with the ruling by the German constitutional court in the Maastricht case, ‘[e]ach member state of a monetary union in its capacity as one of the “masters of the treaty” may recover the conferred powers by simply leaving the union’ (816).

⁹¹ See Treves, above note 46, 113.

of Agreement than they are nowadays. Since the collapse of the Bretton Woods regime (*de facto*), and the Second Amendment to the Articles of Agreement (*de jure*), IMF Member States reaffirmed some of the attributes of their monetary sovereignty with regard to the conduct of exchange rate policy.⁹² However, IMF members must still comply with the obligations under Article IV and Article VIII of the IMF Articles of Agreement, where the jurisdiction (regulatory powers) of the Fund applies, as I further explain in Chapter 13.⁹³

- 1.65** Andreas Lowenfeld⁹⁴ suggests that the regime of conditionality of the International Monetary Fund in the use of its resources is changing the traditional boundaries between the domestic jurisdiction of the States and the international community. Lowenfeld points to the ever increasing level of examination of a large variety of domestic policies in the IMF programmes of structural reform: ranging from national budgets, taxes, interest rates, and exchange rates to subsidies, wage policies, competition law, corporate governance, and even accounting practice and legal reform. These domestic policies are subject to scrutiny, negotiation, and commitment. The eagerness to get or maintain the IMF (conditional) financial assistance may lead the legitimate political institutions in the country to design the economic reform programme without a full analysis of its potentially negative social implications.⁹⁵ Lowenfeld suggests that in some cases the ‘jurisdictional barrier between the international organization and the sovereign states’ has been overstepped or breached, and that a new understanding regarding the relationship between the IMF (and other international agencies) and the countries that need financial assistance is needed.⁹⁶

Other limitations of national monetary sovereignty

- 1.66** The erosion of the traditional notion of sovereignty is also linked to the demise of national frontiers in today’s global financial markets,⁹⁷ despite the trend towards de-globalization (or re-nationalization or re-domestication) that some financial markets and institutions have experienced following the global financial crisis that commenced in 2007 and reached its zenith in 2008.
- 1.67** Sovereignty as a supreme power is typically exerted over the territory of the State: principle of territoriality. It is therefore unsurprising that globalization and the cross-border movement of persons, capital, goods, or services limit the scope of unfettered sovereignty.⁹⁸ The growth in cross-border private capital flows (the volume of such flows, for instance in the foreign exchange market, clearly dwarfs what national central banks and even international organizations can do) is an example of a *de facto* erosion of monetary sovereignty. Arguably,

⁹² Following the *de facto* abandonment of the par value regime and until the entry into force of the Second Amendment (effective 1 April 1978), this reassertion of sovereignty was done in breach of the rules. See Treves, above note 46, 114. I further discuss the nature and operations of the International Monetary Fund in Part III.

⁹³ From the point of view of the consensual limitations of monetary sovereignty, Charles Proctor mentioned, in his comments to this chapter, the dispute between the USA and China over the valuation of the renminbi. In his opinion, this dispute emphasizes that—though the issue and management of a currency falls under the domestic jurisdiction of a State—the adoption of an exchange rate policy occurs within a framework of international law which may involve obligations to other States.

⁹⁴ See Andreas F Lowenfeld, ‘The International Monetary System and the Erosion of Sovereignty. Essay in Honor of Cynthia Lichtenstein’ (2002) 25 *Boston College International and Comparative Law Review* 257.

⁹⁵ The issues surrounding the conditionality of the International Monetary Fund are discussed in Chapter 13. See also Rosa M Lastra, ‘IMF Conditionality’ (2002) 4(2) *Journal of International Banking Regulation* 167.

⁹⁶ Lowenfeld, above note 94.

⁹⁷ The term ‘erosion’ is borrowed in this context from Treves, above note 46, 117.

⁹⁸ See Helen Stacey ‘Relational Sovereignty’ (2003) 55 *Stanford Law Review* 2029, 2040–51.

the ability to have a truly independent monetary policy diminishes with the growth of cross-border capital flows.⁹⁹

Cohen refers to the ‘deterritorialization’ of money, to express the reality that the circulation of national currencies is no longer confined within the territorial frontiers of nation States.¹⁰⁰ Indeed, the extensive use of the US Dollar and other reserve currencies are examples of this reality, an issue which is further discussed in Chapter 12. The problem with this reality is also one of accountability, since central banks, such as the Federal Reserve System, whose influence is international, remain accountable to national constituencies.¹⁰¹ **1.68**

The growth in Eurocurrency markets entails a partial loss of monetary sovereignty.¹⁰² In the presence of ‘transnational money markets’, the lack of coercive power of the State beyond its territory means that ‘the state does not have the power effectively to regulate credit in its currency by banks outside its territory.’¹⁰³ However, to the extent that bank transfers in a particular currency involve clearing and settlement in the country of origin of the currency, the mechanisms of control are reasserted and the notion of erosion of sovereignty may be questioned.¹⁰⁴ **1.69**

As was pointed out earlier, the government has the monopoly over the issue of currency only—ie, notes and coins in circulation—but not over other assets that individuals might hold instead of currency and that are contributing to the blurring of the definition of money and to a de facto erosion of monetary sovereignty. Commercial banks have an important role in the process of money creation: current accounts (demand deposits) are used as means of payment. Demand deposits constitute the major part of the narrow definition of the money supply (M1).¹⁰⁵ This characteristic of bank liabilities provides the rationale for many monetary and banking laws and regulations. **1.70**

The role of banks and other private financial institutions in the creation of money cannot be underestimated. There have also been radical proposals, which are not further analysed here, suggesting the reliance on ‘private money’. Hayek and other economists in the ‘free **1.71**

⁹⁹ See David Llewellyn, *International Financial Integration: The Limits of Sovereignty* (New York: John Wiley & Sons, 1980) 198.

¹⁰⁰ See Benjamin Cohen, ‘Life at the Top: International Currencies in the Twenty-First Century’, Princeton University Essays in International Economics No 221 (December 2000) 1–2:

Currencies may be employed outside their country of origin for either of two purposes: for transactions between nations or for transactions within foreign states. The former purpose is conventionally referred to as ‘international currency use’, or currency ‘internationalization’; the latter is described as ‘currency substitution’ and can be referred to as ‘foreign-domestic use’. The top international monies are widely used for both purposes.

¹⁰¹ See Ralph Atkins, ‘ECB Needs a Timely Response to Fed’s QE Tapering Move’ *Financial Times* (26 June 2013): ‘As Richard Fisher, President of the Dallas Federal Reserve told the Financial Times in London this week, even central banks whose influence extend way beyond their shores remain accountable to national constituencies. “It is an oddity in a globalized world”, he admitted.’

¹⁰² Initially, Eurocurrency financial instruments (Eurodollar deposits, Eurobonds . . .) were denominated in dollars; the prefix ‘euro’ is due to the fact that the markets originated in Europe. Eurodollar deposits are deposits denominated in US dollars and held outside the jurisdiction of the United States.

¹⁰³ See Treves, above note 46, 117.

¹⁰⁴ See Mann, 5th edn, above note 35, 199–201, and Treves, above note 46, 117.

¹⁰⁵ As acknowledged, the central bank can influence the banks’ reserve position by raising and lowering interest rates (through open market operations and discount policies) and by modifying the reserve requirements.

banking school' have advocated the 'denationalization of money', opening up the provision of currency to competition both from the private sector and from foreign issuers of currency.¹⁰⁶

- 1.72** The power to issue currency is a sovereign prerogative, but one that can become an empty concept if the government is incompetent in the management of its currency or if there is a loss of confidence in such conventional money. Citizens will then figure out some way of devising a substitute currency—relying upon a foreign currency or establishing a parallel currency or a virtual currency. Failing that, the society reverts to barter. A sovereign can punish people who counterfeit the sovereign's own currency, or who use an alternative currency without the sovereign's permission, but a sovereign is less able to control the proliferation of faux currencies if society loses faith in the government's declared legal tender. In practice, the other limits of monetary sovereignty are thus defined by monetary incompetence.¹⁰⁷
- 1.73** The experience of inflation can be viewed as an 'abuse of sovereignty'.¹⁰⁸ Inflation makes people turn to other forms of payment, for example, foreign currencies. The public authorities have various ways of obtaining command over real resources: expropriation, taxes, bond issues, and the issue of currency.¹⁰⁹ In a market economy taxes and bond issues are preferred. However, the temptation to print money to finance government expenses remains a powerful argument to depoliticize the management of money; hence the support in the latter part of the twentieth century for central bank independence, analysed in Chapter 2.
- 1.74** The degree to which a currency is a good store of value in international monetary relations ('hard currencies' and 'soft currencies') is an economic consideration that can also limit in practice the effectiveness of monetary control. Depreciation (the loss in value of a currency vis-à-vis other currencies under a system of flexible exchange rates) and devaluation (the loss in value of a currency vis-à-vis other currencies by official intervention under a system of managed exchange rates) can lead to a de facto erosion of national monetary sovereignty.
- 1.75** The choice of exchange regime adopted by a State clearly affects the external value of the currency. Under a fixed exchange rate system, a national central bank only enjoys control over monetary policy if it is the central bank which sets monetary policy for the whole area. In the words of Robert Mundell, 'when a country opts for fixed exchange rates . . . it sacrifices policy sovereignty in the field of money.'¹¹⁰ In the case of a currency board arrangement (discussed in Chapter 2), monetary sovereignty is greatly reduced. In the case of dollarization, there is a surrender of monetary sovereignty.

¹⁰⁶ See Friedrich A von Hayek, *Denationalization of Money* (London: Institute of Economic Affairs, 1976). Hayek's first writing on this subject dates back to 1937, *Monetary Nationalism and International Stability* (reprint, New York: Augustus M Kelly, 1971). For further references on this issue, see Lastra, above note 73, 252–7.

¹⁰⁷ I thank Lee Buchheit for this observation.

¹⁰⁸ See Robert Mundell, 'Monetary Unions and the Problem of Sovereignty' (2002) 579 *Annals of the American Academy of Political and Social Science* 123, 127. Monetary sovereignty is also restricted under a system of fixed but adjustable exchange rates, because countries need to cooperate and engage in supranational decision-making.

¹⁰⁹ See Charles Goodhart, *Money, Information and Uncertainty*, 2nd edn (London: Macmillan, 1989) 44.

¹¹⁰ See Mundell, above note 9, 292–3. Mundell differentiates between policy sovereignty, which refers to the ability to conduct policy independent of commitments to other countries, and legal sovereignty, which refers to the ability of a State to make its own laws without limitations imposed by any outside authority.

G. Concluding Observations

One of the key attributes of sovereignty is the power to issue and regulate money. This is referred to as monetary sovereignty, a dynamic concept which has been redefined in recent decades through consensual and non-consensual limitations. The evolving nature of this concept—in line with the evolving nature of monetary law—finds its latest manifestation in the de-globalization (or re-nationalization) that some financial markets and institutions have experienced following the global financial crisis. The contours of the powers of the State keep on changing. **1.76**

Preview - Copyrighted Material
<http://www.yudiskshop.com>