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# The Changing Dimensions of State Sovereignty under International Economic Law

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## ABSTRACT

*The objective of this research paper is to understand how the concept of State Sovereignty has emerged in International Economic law with a primary focus on the role played by major International Economic Institutions in shaping the dimensions of State Sovereignty to how it has evolved in the present day. This paper focuses on an elaborative approach on mainly the role played by the Bretton Woods Institutions and the World Trade Organization in evolving the Sovereignty of states consecutively with their complex interdependence. This paper attempts to explore two research questions, firstly, how the IMF, the World Bank, and the WTO have limited the Sovereign powers of a state in exchange for benefits that it provides to them, and secondly, how Sovereignty has been impacted in times of COVID and what the future might hold for the international community in terms of Sovereignty of States.*

**Keywords-** *Sovereignty, State Sovereignty, Bretton Woods Institutions, IMF, World Bank, World Trade Organisation, COVID-19, Globalisation.*

## I. INTRODUCTION

Sovereignty, in its most basic sense, can be described as the authority of a state to govern itself. “A Sovereign state can be defined as an authority that is supreme in relation to all other authorities in the same territorial jurisdiction and is independent of all foreign authorities”.<sup>2</sup> A sovereign is an authority that is the exclusive source of laws of its territory and one which is free from all foreign authority unless it has consented to the same.

Ever since World War II, many International Organizations have emerged for peacekeeping and international security. With these organizations, the concept of Sovereignty has also evolved in the sense that the importance and the need for international peace and security have ultimately led to States compromising certain aspects of their Sovereignty to achieve these goals collectively as a whole. In the economic sphere, the Bretton Woods Institutions and some other major international organizations such as the World Trade Organization, ICC, ICSID,

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<sup>2</sup> Robert Jackson, *Sovereignty: The Evolution of an Idea* p.no. 10-12 (Hoboken Wiley, 2013)

etc., have played a major role in shaping the nature of Sovereignty and its changing dimensions over decades.

## **II. THE IMPACT OF THE EVOLUTION OF THE BRETTON WOODS INSTITUTIONS ON SOVEREIGNTY OF STATES AFTER THE 2<sup>ND</sup> WORLD WAR**

The formation of the IMF and the World Bank were a result of the Bretton Woods conference in 1944 with the goal of reviving the shattered post-war global economy and facilitating and promoting peaceful world trade<sup>3</sup>, and therefore, the IMF and World Bank together are known as the Bretton Woods Institutions. These institutions were established when a group of states came together and delegated some of their sovereign rights to these institutions in order for them to perform certain specified functions for the common benefits of these states.<sup>4</sup>

Bretton Woods institutions have had quite an impact on shaping the concept of Sovereignty due to the functions they were meant to perform. Their functions are elaborately provided by their Articles of Agreement. Both these institutions have been conferred with separate duties and functions; however, it has been long debated whether they actually adhere to the Articles of Agreement that have been signed by the member states and which expressly indicate that these institutions shall not interfere with the sovereign rights of its member states. The purpose of the World Bank<sup>5</sup> is to handle the reconstruction of the war trodden areas and assist in infrastructural development, while that of the IMF<sup>6</sup> was to regulate foreign exchange and to manage and regulate the inconsistencies and problems in the balance of payments accounts of its member states. In other words, these institutions were conferred not only with the task of restoring international monetary relations but also to diagnose a crisis, if one arises, at an early stage and to prevent it.

Despite the inconsistency in their work, the Bretton Woods Institutions were successful in the formulation of a governance framework of the global economy and to accomplish security and stability through policy implementation, which facilitated globalization. However, in the 1970s, after the collapse of the fixed exchange rates system due to non-compliance of US for conversion of dollar into gold, the gradual shift of the global economy into a free market economy through the NPE (New Political Economy) Model was a challenging period for the

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<sup>3</sup>“What are the Bretton Woods Institutions?” Bretton Woods Project, <https://www.brettonwoodsproject.org/2019/01/art-320747/>(last visited Oct 14, 2021)

<sup>4</sup>Dr. Christian Wigwe, “*World Bank, International Monetary Fund and State Sovereignty: A Critical Review*”, 3 *Ikeja Bar Review* (2008)

<sup>5</sup> World Bank Encyclopedia Britannica, <https://www.britannica.com/topic/World-Bank> (last visited Nov 17, 2021)

<sup>6</sup> An Introduction to the International Monetary Fund (IMF) Investopedia, <https://www.investopedia.com/articles/03/030703.asp> (last visited Nov 17, 2021)

social and philosophical standing of these institutions.<sup>7</sup> The World Bank and the IMF practically implemented the NPE Model through their policies of “Structural adjustment loans” and “Structural Adjustment Policies”, respectively which were further stabilized through the institution of the World Trade Organization.<sup>8</sup> The liberalization of global trade worked mainly to the advantage of the industrialized countries, and other states were severely affected, which led to deindustrialization and thus hyper-globalization.

### III. THE WORLD TRADE ORGANIZATION AND STATE SOVEREIGNTY

World trade is mainly facilitated through a treaty-based mechanism that is ultimately governed by the WTO. When a treaty is signed, the state parties involved transferring a certain amount of decision-making authority towards an international institution.<sup>9</sup> Even though this treaty-based mechanism limits the sovereign powers of states, it has been largely accepted since the benefits of cooperative action are much larger than an isolated exercise of Sovereignty.

In the context of a globalizing world in which states acting alone cannot achieve important governance goals, only the process of treaty-based cooperative action can overcome this growing inability to achieve those goals. When it comes to economic affairs, these are often driven by global economic structures such as international companies, international markets, and distribution networks, which individual states acting alone cannot effectively manage or regulate. Cooperation through a treaty institution may be the only way out. This has been the core of international trade for more than half a century and, therefore, the essential foundation of the GATT and WTO system.<sup>10</sup>

### IV. STATE SOVEREIGNTY IN THE COVID-19 ERA

COVID-19 originated in China at the beginning of 2020, and within the next few months, it spread to the whole world and took the shape of a global pandemic. Most of the countries across the world took strict containment measures to deal with the spread of the virus by imposing lockdowns. If we look beyond the scope of health and humanitarian issues, the pandemic also brought a major challenge for the economies around the globe, the repercussions of which are still being faced by most developing economies.

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<sup>7</sup>Maria Eleni Voutsas & George Borovas, *The Role of the Bretton Woods Institutions in Global Economic Governance*, 19 *Procedia Economics and Finance* , 37-50 (2015)

<sup>8</sup> *ibid*

<sup>9</sup> Oona Hathaway, *International Delegation and State Sovereignty*, 71 *Law and contemporary problems* , 115 (2008)

<sup>10</sup>Chapter III: Sovereignty Wto.org, [https://www.wto.org/english/thewto\\_e/10anniv\\_e/future\\_wto\\_chap3\\_e.pdf](https://www.wto.org/english/thewto_e/10anniv_e/future_wto_chap3_e.pdf) (last visited Oct 15, 2021)

According to Richard N. Haass,<sup>11</sup> “Historically, Sovereignty has been associated with four main characteristics: First, a sovereign state is one that enjoys supreme political authority and monopolies over the legitimate use of force within its territory. Second, it is capable of regulating movements across its borders. Third, it can make its foreign policy choices freely. Finally, it is recognized by other governments as an independent entity entitled to freedom from external intervention. These components of Sovereignty were never absolute, but together they offered a predictable foundation for world order. What is significant today is that each of these components - internal authority, border control, policy autonomy, and non-intervention - is being challenged in unprecedented ways.<sup>12</sup>“

As per an OECD report,<sup>13</sup> The pandemic has resulted in the most serious economic crisis ever since World War II. From employment to imports and exports to tourism, every sector of every economy has taken a hit after the pandemic. Every country has dealt with the pandemic in its own territory how it saw fit. Lockdowns can be seen as one common measure adopted by most countries. Lockdowns have caused many issues in the economic growth and maintenance of different countries. During the lockdown, all businesses were forced to stop operations for as long as the pandemic was under control. Every kind of business was closed down, even the ones that were owned by foreign investors, which caused huge losses to the investors. In this scenario, the question of the liability of the host state towards the losses incurred by the investor-state comes forth. From a wider perspective, it cannot be denied that lockdown is merely a discretionary measure and the closure of businesses was ultimately the decision of the governments of all the states that had imposed it.

As per customary international law, all sovereign states have the right to regulate all activities within their territory, and States exercise their sovereign authority by way of legislations, decrees, orders, regulations, etc.<sup>14</sup> During the lockdown, all businesses were forced to stop operations for as long as the pandemic was under control. Every kind of business was closed

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<sup>11</sup>This article is a script of remarks of Richard N. Haass to the School of Foreign Service and the Mortara Center for International Studies, Georgetown University, Washington DC. The author has talks about three different scenarios: stopping genocide, fighting terrorism, and preventing the spread of weapons of mass destruction, and has highlighted that with rights come obligations and sovereignty is not absolute but, conditional; Richard N. Haass, *Sovereignty: Existing Rights, Evolving Responsibilities* (US Department of State) (2003)

<sup>12</sup> In the area of trade policy, there are many specific instances of avoidance of sovereignty of member states. An example was the criteria for membership of the GATT and now, the WTO. It was not, and is not, limited to a "sovereign entity," but instead to a "State or separate customs territory possessing full autonomy in the conduct of its external commercial relations..."; see *supra* note 6

<sup>13</sup> Organization for Economic Co-operation and Development (OECD), *Tourism Policy Responses to the coronavirus (COVID-19)* (2020), [https://read.oecd-ilibrary.org/view/?ref=124\\_124984-7uf8nm95se&title=Covid-19\\_Tourism\\_Policy\\_Responses&\\_ga=2.224020763.1087617307.1637002173-46274685.1634236212](https://read.oecd-ilibrary.org/view/?ref=124_124984-7uf8nm95se&title=Covid-19_Tourism_Policy_Responses&_ga=2.224020763.1087617307.1637002173-46274685.1634236212) (last visited Nov 15, 2021).

<sup>14</sup> Samantha Besson, *Sovereignty* Max Planck Encyclopedias of International Law [MPIL] (2011).

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Under emergency circumstances, when a state passes a regulation or legislation, it is with a view to curb the situation within the bounds of its territory, and such decisions are usually made while prioritizing the welfare of the citizens of that state and not business losses to some investors. If viewed from this lens, a host state cannot be asked to compensate an investor merely because of an emergency policy-making decision that was made for the welfare of its territory.<sup>15</sup>

As per ARSIWA<sup>16</sup>, the criteria for a regulatory measure to be non-compensatory is that it must:

1. be bonafide
2. be for a public purpose
3. be non-discriminatory
4. adhere to due process
5. be proportionate to the public purpose intended
6. comply with fair and equitable treatment where applicable
7. not amount to an abuse of rights;
8. Not give a direct benefit to the state.

The application of the above criteria must be such that the effect of the measure should amount to the complete destruction of the investment in question, preferably permanently. Alternatively, a state can also raise defences on the basis of its municipal laws if it provides for the same, on the grounds of national security or health emergency, etc. otherwise, the principles of customary international law can be referred to as mentioned above. Conclusively, it can be stated that when the dust settles around COVID-19 in the future, the effectiveness of measures of States will come in the clear.

## **V. CONCLUSION**

State Sovereignty has been defined and challenged in various unprecedented ways in the past

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<sup>15</sup> refer supra note 13

<sup>16</sup> Draft articles on Responsibility of States for Internationally Wrongful Acts

few decades. It can be seen that the perseverance of Sovereignty with a subsequent goal of global peace and security is where most international organizations converge. From the era of Bretton Woods Institutions to the World Trade Organisation, State Sovereignty has been the centre of global policy and regulation. In the earlier decades, with the rise of globalization, the Bretton Woods Institutions and the World Trade Organisation performed their functions very well by tackling various economic challenges and by maintaining world peace. However, ever since COVID-19 struck the global economy, the policy precedents set by the previous crisis can be considered to be irrelevant as what is faced by the world now was completely unexpected, and the global economy has experienced a crisis different from anything that our economy has ever experienced.

There have been many debates on what the future of the global economy must look like, but at present, no theory or logic is conclusive as we now face the third wave and the third time when most of the countries across the world are witnessing a complete lockdown. In the present scenario, what is different from the first phase of COVID-19 is that most countries have developed a pattern of policy regulations that is unique to each economy, and most states have formulated a unique coping mechanism best suited to themselves and their citizens. As for what the future holds for the global economy, it is as uncertain as it can be.

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