ANALYSEN UND BERICHTE

Conditionality of IMF and World Bank Loans: Tutelage over Sovereign States?[1]

By *Werner Meng*

I. The Problem

The international debt crisis nowadays is one of the most serious problems between developed states and developing states. Its outcome is also of utmost importance to many private banks. Claims for writing off part of the debt of the developing countries are more and more heard, and some developed states are already doing so at least as far as the least developed countries are concerned. The debt crisis has many facets. In this article, one aspect, namely the official relationship between two very important creditors, the International Monetary Fund (IMF) and the World Bank (IBRD), and debtor states is evaluated for its compatibility with public international law.

The main focus is on the principle of sovereignty and its corollary, the duty not to intervene in the domestic affairs of other states.[2] The question is whether conditions linked to new debts or debt rescheduling by both institutions do violate this duty or the special international law that governs all the activies of these organisations. For both are international intergovernmental organizations based on a founding treaty that contains

1 This article is an extract of the author's submission to the German-Polish Colloquium on Public International Law held at Poznan in the fall of 1987. The more detailed version will be published in the Reports of the Colloquium. The author gratefully acknowledges the assistance with some English language aspects of this paper provided by Dr. Peter Macalister-Smith.

2 Generally on this principle see Schröder, M., Non-Intervention, Principle of. R. Bernhardt (ed.) Encyclopedia of Public International Law, Inst.7 (1984) p.358–360; Oppermann, T., Intervention, in: R. Bernhardt (ed.), Encyclopedia of Public International Law, Inst.3 (1982) p.233–236; Vincent, R. J., Non-intervention and International Order (1974) (cited: Non-intervention); Verdross, A., Le principe de la non-intervention dans les affaires relevant de la compétence nationale d'un Etat et l'Article 2(7) de la Charte des Nations Unies, Mélanges offerts à Charles Rousseau, (1974) p.267–276; Ouchakov, N., La compétence interne des Etats et la non-intervention dans le droit international contemporain, Recueil des Cours 141 (1974 I) p.5–85; Schwebel, P. M., Aggression, Intervention and Self-Defence in International Law, Recueil des Cours, 136 (1972 II) p.411–497; Oppermann, T., Nichteinmischung in innere Angelegenheiten, Archiv des Völkerrechts, 14 (1969/70), p.321–342; Gerlach, A., Die Intervention (1967).

all their powers and that also restrains them. As subjects of public international law both organizations are bound by the general norms of public international law as far as they pertain to their lawful activities.

Originally, the activities of both organizations were not very similar. The IMF[3] was the cornerstone of the international monetary system drafted at the Bretton Woods Conference in 1944. It was not conceived as a bank concerned with ordinary lending for productive purposes. The IBRD,[4] on the other hand, also founded at the Bretton Woods conference, is a bank designed to give loans for productive purposes in order to assist the reconstruction and development of territories of member states. The international debt crisis has caused a closer parallel activity of both organizations in lending. This is particularly due to the progressive involvement of the IMF in financing the results of huge state deficits. There is nowadays a »cooperative debt strategy« between both organizations and private banks.

Debt may result in a certain dependence of the debtor upon the creditor. Private banks usually do not involve themselves in lending without examining the creditworthiness of the debtor. And they will not hesitate to resort to making either helpful proposals concerning the economic performance of their creditors or even conditions in that respect, if their financial risk is substantial. The same applies to the lending practice of IMF and IBRD. The more money they are lending to a state, the more binding and comprehensive are their economic conditions. This practice, called the »conditionality« of their loans, is nowadays facing more and more criticism.[5] Such criticism is focussing

3 Generally on the IMF as an institution see Chandavarkar, Anand G., The International Monetary Fund, IMF Pamphlet Series No.42 (1984) (cited: IMF); Gold, J., Legal and Institutional Aspects of the International Monetary System: Selected Essays, 2 Bände (1979/1984) (cited: Selected Essays); Gold, Sir J., International Monetary Fund, in: R. Bernhardt (ed.), Encyclopedia of Public International Law, Instal.5 (1983) p.108–115; Hooke, A.W., The International Monetary Fund. Its Evolution, Organization and Activities, IMF Pamphlet Series, No.37, 3.ed. (1983) (cited: IMF); Rettberg, J., Weltwährungsfonds mit Weltbankgruppe und UNCTAD als Bezugspunkte der internationalen Handels- and Entwicklungspolitik (1983) (cited: Weltwährungsfonds); Lowenfeld, A., The International Monetary System (1977); Stratmann, G., Der Internationale Währungsfonds (1972) (cited: IWF); Carreau, D., Souveraineté et coopération monétaire internationale (1970) (cited: Souveraineté); Gold, J., The International Monetary Fund and International Law. An Introduction, IMF Pamphlet Series, No.4 (1965) (cited: Introduction).

4 Its official name is »International Bank for Reconstruction and Development« (IBRD). See generally Delaume, G. R., La Banque Mondiale et la mise en oeuvre du droit international économique, Société française pour le droit international (ed.), Colloque de Nice. Les Nations Unies et le droit international économique, (1986) p.311–326; Golsong, H., International Bank for Reconstruction and Development, in: R. Bernhardt (ed.), Encyclopedia of Public International Law, Instal.5 (1983) p.58–64; Payer, Ch., The World Bank. A Critical Analysis (1982) (cited: Word Bank); Tetzlaff, R., Die Weltbank: Machtinstrument der USA oder Hilfe für die Entwicklungsländer? (1980) (cited: Weltbank); Lazar, L., Transnational Economic and Monetary Law. Transactions and Contracts, vol.2 (1978 –) (cited: TEML); Syz, J., International Development Banks (1974) (cited: Banks).

5 From the numerous works which should be mentioned see Meessen, K.M., IMF Conditionality and state Sovereignty, in: T. Oppermann/E.U. Petersmann, Reforming the International Economic Order (1987), p.173–185 (cited: IMF); L'Hériteau, M., Le Fonds Monétaire International et les Pays du Tiers-Monde, (1986) (cited: FMI); Conklin, M./Davidson, D., The I.M.F. and Economic and Social Human Rights: A Case Study of Argentina, 1958–1985, Human Rights Quarterly 8(1986), p.227–269; Kranz, J., Le droit du Fonds monétaire international et les affaires internes des pays membres, German Yearbook of International

on the nature and content of these conditions, on the role of the debtor countries in the international economic order and on the inconsistency of conditions and concepts.
A very important point made by contemporary critics is that the organizations violate the duty not to intervene in the domestic affairs of the debtor states.[6] This raises the question whether public international law may protect debtors from certain actions of their creditors just as many national laws contain rules providing a certain protection of debtors from unjust harassment by their creditors. Such criticism will be in the center of this article. This requires first a brief survey of the lending practices of both organizations, then an evaluation of the general features of conditionality and finally an evaluation of its practice in accordance with the relevant rules of international law.

II. The lending practice of both organizations

a. *IMF*

The purposes of the IMF are laid down in Article I of its Articles of Agreement (IMFA). This provision makes clear that the IMF is not a bank. But it assumes tasks similar to a bank under art.I para.5 IMFA, under which it shall

> »give confidence to members by making the general resources of the Fund temporarily available to them under adequate safeguards, thus providing them with opportunity to correct maladjustments in their balance of payments without resorting to measures destructive of national or international prosperity«.

It is important to keep this principle in mind when dealing with the present questions: the only task of the IMF when lending its money to member states is to help in balancing the national finances. The Fund is not an institution involved in the transfer of capital for development aid. A deficit in the balance of payments of a state may lead to increasing international debts, because more currency is flowing abroad than into the country. This requires, at least in the long run, an adjustment of the export earnings or of the cost of imports or of both. A whole variety of economic measures affecting prices, income, currency value, customs and trade barriers and also restrictions for capital movements are possibly able to serve these purposes.
Which of these tools are feasible in a given situation is a strictly economic question, and this cannot be considered in a legal analysis. Here it is only important that the assistance

Law 29 (1986), p.111–136 (cited: Droit); id., Les pays socialistes, le Fonds monétaire international et la Banque mondiale, Archiv des Völkerrechts 23(1985), p.270–293 (cited: FMI); Körner, P. u.a., Im Teufelskreis der Verschuldung. Der Internationale Währungsfonds and die Dritte Welt (1984); Tetzlaff, Weltbank, passim.

6 L'Hériteau, FMI, p.110 ff.

of the IMF is designed to enable states to deal with such imbalances not under immediate pressure, but in an economically sensible and politically acceptable way. This increasingly places the Fund in a role of chief consultant of indebted states. The favor of being eligible for its help is accompanied by the duty to listen to its economic evaluations and to fulfill its conditions.

The first instance where political considerations can be linked with the Fund's activities is when a country is applying for membership, since this is a prerequisite to having access to the Fund's resources. This is a question that will not be dealt with here. It may be important with respect to the USSR's application to join the Fund, but given the global membership of both organizations it is not very important any more with respect to the debt crisis.

The second important influence of the IMF on member states exists when a state has the need to apply for a loan. The decisison-making process itself is not free from the political influence of other member states. The decisions about loans are made by the Executive Board. It consists of 22 directors, 6 of whom are nominated by single important countries,[7] the others being elected for a two year term by groups of member states. The directors cast the votes of the countries which elected or nominated them. Those votes are not equal, but weighted on the basis of the share of each country in the Fund.[8] This leads to a legal inequality of the influence of member states on the decisions of the Fund.

The executive directors who are nominated can be recalled by their countries. This leads to a factual influence of their home states on their voting behavior. While such dependency cannot be derived from IMF law, it is not on the other hand excluded thereby. The national laws of the United States of America[9] and of the Federal Republic of Germany[10] reveal an unconcealed influence of either the executive or the legislative branch on the voting behavior of the directors of these states. This seemingly has been accepted by all member states, since there is no recorded protest known against the exercise of such influence.

If directors are not nominated, but elected, the influence of their states is weaker. But such directors are free to consult those states and to follow their opinion in a given case. But the practical voting structures are in this respect more relevant. The Executive

7 Art. XII Para.3 lit b IMFA.

8 Each Member holds a basic amount of 250 votes and additionally one vote for each part of its quota that relates to 100 000 special drawing rights. On April 20, 1986, the states that do not nominante a director but elect one in a group had a voting weight of 53,68 %, the rest belonged to the six states nominating a director, i.e. the USA, the UK, the Federal Republic of Germany, France, Japan and Saudi-Arabia, cf.IMF.Annual Report 1986, IMF (ed.) (1986). The USA have the largest block of 19,29 % of the total votes Cf. generally Gold, J., Voting and Decisions in the International Monetary Fund (1972) (cited: Voting); id., Voting Majorities in the Fund. Effects of the Second Amendment of the Articles, IMF Pamphlet Series, No.20 (1977) (cited: Majorities).

9 21 U.S.C. §286 c-9, e-11 §286-b, §286-aa.

10 Gesetz betreffend das Abkommen über die Internationale Finanz-Corporation und betreffend Gouverneure und Direktoren in der Internationalen Bank für Wiederaufbau und Entwicklung, in der Internationalen Finanz-Corporation und im Internationalen Währungsfonds vom 12. 7. 1956, BGBl.1956 II, S.747.

Board decides in loan matters without any change on a proposal of the Managing Director. This proposal has been negotiated with the applicant country. The possibility of arbitrary influences on decisions is decreased by this procedure. However, it is possible for a state or a group of states, like the »Group of Ten« of industrialized states, which has an absolute majority of votes,[11] to block a decision, since generally the Board wants to reach a consensus. This can and does to a certain extent influence the conditions of loans.

This is even more possible since the rules on the prerequisites of loans given by the Fund are not very detailed. Even the term »loans« is somewhat misleading in this respect.[12] There are drawing tranches and special facilities. Technically the drawing on both consists in buying the amount of foreign currency needed against the debtor's own currency. This operation has to be reversed after a specified time. But, in economic terms, this operation amounts to the grant of a loan in hard currency.

The drawing on tranches of the Fund's resources are either drawings on the reserve tranche of 25 % of a country's quota or on four credit tranches each of the same 25 %. The currency purchases by this operation may not exceed 200 % of the quota.[13] The Agreement makes clear that the use of the tranches is only to rebalance instabilities in a member country's balance of payments or its reserve position or developments in its reserves.[14]

The resort to the reserve tranche is free, since it is not really a drawing on loan facilities.[15] The drawing on the first credit tranche is allowed for liberally, »provided that the member itself is making reasonable efforts to solve its problems«.[16] The applications for drawings beyond that »require substantial justification«.[17] Here the area of real »conditionality« starts.[18]

But nowadays the heavily indebted countries are drawing on much higher amounts granted in the framework of a whole variety of additional special facilities, like the »Enlarged Facility«,[19] the policy of »Enlarged Access«,[20] and the »Structural Adjust-

11 Cf. Gold, Selected Essays, vol.1, p.17.

12 Art.V Para.3 lit.b IMFA, cf. Carreau, Souveraineté, p.405. Generally about the financing activities of the Fund see Lelart, M., Les opérations du Fonds Monétaire International (1981); Gold, J., Financial Assistance by the International Monetary Fand. Law and Practice, IMF Pamphlet Series, No.27 (1979) (cited: Assistance).

13 Art.V sec.3 b IMFA.

14 Art.V sec.3 b (ii) IMFA.

15 Art.V sec.3 c IMFA.

16 Annual Report of the Executive Directors 1962, p.31.

17 Ibid.

18 Cf. Gerster, R., The IMF and Basic Needs Conditionality Journal of World Trade Law, 16, (1982), p.497–517; Gold, J., Conditionality, IMF Pamphlet Series, No.31 (1979) (cited: Conditionality); Guitián, M., Fund Conditionality. Evolution of Principles and Practices, IMF Pamphlet Series, No.38 (1981) (cited: Conditionality); Pirzio-Biroli, P., Making Sense of the IMF Conditionality Debate, Journal of World Trade Law, 17 (1983), p.115–153.

19 Decision No.4377–(74/114), SDIMF, p.32 ff.

20 Decision 6783–(81/40), SDIMF, p.46 ff.

ment Facility«.[21] Such facilities are given for a special purpose and usually for a longer loan period.

All those facilities and the upper credit tranches are only granted if a country is willing to enter into a so called »Stand-by Arrangement«.[22] This practice started in 1952[23] and is provided for in Art.XXX (b). IMFA. A debtor country must undertake to follow certain economic steps to ensure the recovery of the balance of payments. This assurance is given in a »letter of intent«. It is the basis or the Fund's decision on the loan. The IMF sets up »performance criteria«, i.e. a final goal and intermediary goals to be reached by a debtor country.

Only if a country does reach an intermediary goal it is eligible to draw on the next tranche or instalment of the facility. The criteria are ordinarily quantifiable, like the amount of internal loans, the savings rate, the budget deficit and the currency reserves. In addition, the principal directions of economic policy may have to be pledged, like the avoidance of protectionist tariff barriers. If a country is not able to meet some pledged criteria it may in time consult the Fund in order to consensually adapt the program and thus preserve its eligibility to draw on the next tranche.

It is a long-standing practice of the IMF that such Stand-by Arrangements are not concluded as international agreements.[24] The letter of intent is a unilateral pledge of the country to reach the criteria. If a country fails, this is not a breach of an international contract. It only loses the right to draw on the next instalment. On the other hand Art.XXX (b) IMFA makes clear that such arrangement is »a decision of the Fund by which a member is assured that it will be able to make purchases from the General Resources Account in accordance with the terms of the decision during a specified period and up to a specified amount«. Consequently the arrangement entails a qualified right to obtain the loan by virtue of IMF law. The creditworthiness of a country will not be screened further during the period of the same loan if the criteria are met and if the money is not used abusively. In this manner it is sought to secure stability and predictability that are necessary for the economic recovery of a national economy.

b. *The World Bank*

The decision-making process in the World Bank is very similar to that of the IMF. The problems of political influence are thus parallel in both organizations. The main differ-

21 Annual Report 1986, p.46. Decision No.4240–(86/56) SAF of 26. 3. 86 in Appendix III to the Annual Report.

22 See the »Guidelines on Conditionality« in the Annex to Decision No.5056–(79/38) of 2.3. 1979 agreed by the Executive Board. Generally Gold, J., The Legal Character of the Fund's Stand-By Arrangements and why it matters, IMF Pamphlet Series, No.35 (1980) (cited: Standby).

23 Decision No.155–52/57) of 1.10. 1952.

24 Decision No.2603–(68/132) and No.6056–(79/38), Ziff.3: »Stand-by arrangements are not international agreements, and therefore language having a contractual connotation will be avoided in stand-by arrangements and letters of intent«. Gold, Standby, p.12 says, that the IMF is lacking »animus contrahendi«.

ence between the organizations lies in their different task and in the different legal status of their loan arrangements. The World Bank is a genuine international bank. Its original purpose was the fostering of reconstruction of economies destroyed by the Second World War. Nowadays, the Bank is one of the important financing institutions in the development sector. Part of its loans are given for investment purposes, but in this article the loans given for national adjustment programs are of paramount interest.

It is in this area that cooperation of Fund and Bank become ever closer. They are both involved in the same business, namely financing the readaptation of national balances of payments combined with tackling the economic problems which constitute the roots of imbalances. Since 1977 the Bank has been considerably involved in such lending.[25] The formal external requirements are similar to those of the IMF: letters of intent are required and performance criteria are established. But the basic difference is that the Bank enters into contractual relationships with its debtors. Without such a contract no claim whatsoever of a member state can exist to draw on the resources of the Bank. One limit found in Art.III sec.3 of the IBRDA is that the total amount outstanding of guarantees, participations in loans and direct loans shall not be increased at any time, if by such increase the total would exceed one hundred percent of the unimpaired subscribed capital, reserves and surplus of the Bank. Furthermore, the Bank must be satisfied that under the prevailing market conditions the borrower would otherwise be unable to obtain the loan on reasonable conditions.[26] There are other prerequisites mentioned in the Agreement, but the most important one seems to be found in Art.III sec.4 (v): »In making or guaranteeing a loan, the Bank shall pay due regard to the prospects that the borrower, and, if the borrower is not a member, that the guarantor, will be in position to meet its obligations under the loan; and the Bank shall act prudently in the interests both of the particular member in whose territories the project is located and of the members as a whole.« This means that the Bank has to consider the creditworthiness of the debtor state in the long term like any other Bank.

The pledged performance criteria are not the main contractual duties of the state. In this respect, too, the situation is similar to that in the IMF. If the criteria are not met, this is not a breach of contract, but it only triggers the blocking of drawing on further sums of the loan.

c. *Coordination between IMF and the World Bank*

The parallel activities of both organizations entail organizational consequences;[27] their conditionality is aiming in the same direction or at least at mutual compatibility. Sometimes they send common evaluation missions to countries or at least they coordinate the

25 See the General Conditions Applicable to Loan and Guarantee Agreements of October 27, 1980.
26 Art.III sec.4 (ii) IBRDA.
27 Lazar, TEML, S.3.9.6. ff.; IBRD.Annual Report 1986, p.44.

activities of separate missions. Representatives of the other organization participate in the sessions of the Executive Councils if there are projects dealt with that need coordination. Both organizations support each other in the evalution of their programs. They use their respective particular experiences together. The World Bank is especially experienced in microeconomic analysis, while the IBRD is more specialized in macroeconomic questions. The coordination is obvious in the common ministerial committee, the Development Committee.[28]

If countries need loans for structural adjustment, in most cases the adjustment program is supported by an IMF arrangement and by a policy-based lending of the World Bank. This is why the conditionality of both organizations can be dealt with together. Nevertheless, one should mention that the aim of the conditions in both cases is somewhat different. The IMF is more interested in the macroeconomic measures restoring the balance of payments, while the World Bank is more concentrated on the quality and effectiveness of development plans and investment measures.

III. The conditionality

In the upper credit tranches and the additional facilities the performance criteria are chosen according to the particular situation and problems of the member states concerned. The criteria concern macroeconomic as much as microeconomic variables. They usually belong to a comprehensive structural adjustment and economic recovery program. Only the poorest countries are conceded long-range loans with a low level of conditionality despite their indebtedness.

The IBRD evaluates loans like a bank. The recovery of capital, interest and credit cost is the final goal. Thus it is not astonishing that the conditions are very similar to that of the Fund.

Even if the conditions are adapted to the particular cases, some basic features are common to them.[29] They are in conformity with the basic economic principles furthered by both organizations, namely market economy structures. Debtor countries must pledge that they will refrain from foreign currency restrictions and from import restrictions.[30] One principle of the World Bank is to refuse loans to governments who have expropriated foreign property without sufficient compensation.[31] One feature that shows up in the World Bank agreements is the prescription of appropriate procurement procedures

28 IMF: Resolution No.29/9 of the Board of Governors, SDIMF, p.385.
29 Lazar, TEML, p.3.10.24; IMF Annual Report 1986, p. 43 ff.; Tetzlaff, Weltbank, p.222.
30 This might be different with countries having a centrally planned economy like the COMECON countries, see Pissulla, IWF, p.63 and 78.
31 Rettberg, Weltwährungsfonds, p.424.

and of the participation of appropriate technical advisors.[32] The politically most contested conditions concern the reducing of the demand for imported goods and the expansion of the exporting sector. This implies all kinds of influences on the exchange rate, the quantity of money, the loans and savings policy, and, if existing, on the administration of prices and on the effectiveness of the use of resources. The same applies to the more general principles of economic policy like removing exchange restrictions and trade barriers.

The purposes of the conditions are clear: in the long run the deficit in the balance of payments must be reduced. This economic axiom entails consequences in any society. An imbalance is caused by an excess of expenditures in foreign currencies over revenues in those currencies. The remedies for this situation require severe changes in the patterns of consumption and production in an indebted country. This brings about considerable hardship for those who were favored by the old patterns of behavior. This is especially explosive socially if it requires a cut in subsidies that are motivated by reasons of social assistance or generally by the intention to redistribute wealth in a society. A program required as a condition by a creditor organization may make the people pay economically for the mistakes of their political leadership.

The economic value of the conditions combined with IMF and World Bank loans is often vigorously contested by politicians and economists.[33] The success of conditionality as practised by these organizations is increasingly turning out as negative. On the other hand, there are economic arguments denying that this lack of success is caused by the application of the wrong conditions. The industrial countries are held responsible for not opening their markets to products from the debtor countries.

It is hardly possible to prove that the conditionality of both organizations is economically completely unsound or ineffective. The law of the institutions is clear in this respect: they decide under which conditions they give their loans. If they deem certain economic conditions appropriate for restructuring programs it usually is part of their margin of appreciation to require such conditions before granting a loan. It is their responsibility and they have to enforce it[34] in order to meet their obligations under their institutional law. Nevertheless, the question has been raised whether the margin of appreciation is not narrowed by norms of public international law.

32 See generally Guidelines: Procurement under IBRD Loans and IDA Credits, IBRD (ed.) (1985),

33 Lazar, TEML, p.3.10.24; Payer, Word Bank, passim.

34 While the lost of the eligibility to draw on further instalments of the loan is an effective enforcement leverage one should not underestimate the importance, that a country's standing in both organizations has for its standing towards private banks.

IV. The limits of conditionality in international law

An evalution of the limits of conditionality under general international law and the special law of the organizations has to begin with the rather discouraging statement that there is hardly any international forum in which any such limits could be enforced. The International Court of Justice is not appropriate since the IMF or the IBRD cannot be a party of a proceeding before that court,[35] with the exception of their ability to apply for an advisory opinion under Art. 96 (2) of the U.N. Charter. Obligatory arbitration exists only with regard to members who have left the organizations.[36] There is an obligatory procedure of interpretation within the primary law of both organizations.[37] It would be conceivable to disputes about the legality of secondary norms of the organizations within this decide procedure. But is has to be acknowledged that it has not played an important role in the practice of both organizations. Politically the interpretation procedure does not seem to be considered very helpful by the member states. It remains doubtful whether this procedure would be used to scrutinize the legality questions of conditionality.

On the other hand, this should not prevent the search for substantive international-law limits of conditionality. Even if such limits cannot be enforced by courts, they are an important element in disputes between debtor countries and the organizations.

One has to start from the basis already mentioned: neither in the IMF nor in the World Bank has a state a strict right to obtain a loan under the law. In the Bank there is no right at all[38] while in the Fund[39] such a general right within the credit tranches is conditioned by the requirement that such drawing has to conform to the Agreement and to the policies adopted under it. Those policies are adopted by the Fund under Art.V sec.III(a). It »may adopt special policies for special balance of payments problems, that will assist members to solve their balance of payments problems in a manner consistent with the provisions of this agreement and that will establish adequate safeguards for the temporary use of the general resources of the Fund«. Those policies are now embodied in the Guidelines of 1979.[40]

35 Art.34 para.1 Statute of the International Court of Justice, in: Acts and Documents concerning the Organization of the Court, No.2 (1947–1978).

36 Art.XXIX lit. c IMFA, IX lit c. IBRDA.

37 Art.XXIX IMFA, IX IBRDA.

38 Art.III para.4 IBRDA.

39 Art.V para.III lit b. IMFA.

40 Annex to Decision No.6056–(79/38) of 2. 3. 1979: »Guidelines on conditionality for the use of the Fund's resources and for stand-by arrangements«.

a. *Limits in the Articles of Agreement*

It has already been mentioned that both agreements contain certain economic conditions for the grant of loans. Such conditions may be specified by the secondary law of the organizations and by the agreements and arrangements of the organizations. What is particularly interesting here is the question whether political conditions or economic conditions with far-reaching political implications may be prohibited under public international law.

The most important norm in this respect is found in Art.IV para.10 IBRDA: »The Bank and its officers shall not interfere in the political affairs of any member; nor shall they be influenced in their decisions by the political character of the member or members concerned. Only economic considerations shall be relevant to their decisions, and these considerations shall be weighed impartially in order to achieve the purposes stated in Article I.« At first sight this limit is very extensive. On the other hand, the term »economic considerations« is not defined. The increasing interdependence of economics and general policy has led to a blurring of the difference between the two. The political stability of a country and the efficiency of its government very often influence the flow of goods and especially capital into the country. This brings with it the prospects to make successful development or economic policy.

There are hardly any means of structural adjustment within a country that will be absolutely neutral in general policy. A change in consumption and production patterns is politically and socially relevant. Thus Art.IV para.10 is necessarily neither clear nor an effective tool for differentiation.

The law of the IMF does not contain a similar rule. This may be due to the fact that from the beginning the Fund's role was seen to be closer to general politics while the Bank has only in recent times developed in this direction.

b. *Limits in the secondary law of both organizations*

The IMF Guidelines on conditionality are the main limits in this organization.[41] Paragraph No.4 of the Guidelines states that in »helping members to devise adjustment programs the Fund will pay due regard to the domestic, social and political objectives, the economic priorities and the circumstances of members, including the causes of their balance of payments problems.« No.8 directs the Managing Director to »ensure adequate coordination in the application of policies relating to the use of the Fund's general resources with a view to maintaining the nondiscriminatory treatment of members.«

The formula in No.4 is much more flexible than Art.IV para.10 IBRDA. It accepts the

41 Decision No.6056-(79/38) with annexed »Guidelines on conditionality for the use of the Fund's resources and for Stand-by Arrangements«.

political effects of Fund measures and it guides the organizations into considering such effects. However, it does not mean that the IMF can dictate purely political changes to a country. Art.I and the whole system of this agreement show that the IMF can only act in the economic sphere in order to remedy difficulties with a national balance of payments. Any conditions which are imposed have to foster that goal. It would be illegal under IMF law for the organization to ask for additional, unnecessary political pledges from a country combined with its loan policy. The system of the rules shows that it is illegal to deny access to the resources of the Fund only because a country belongs to a block with a nonmarket economic system or because it is following general political concepts that are not cherished by the majority of the Fund's members.

The problem of delimiting economics and general policy may also arise in the opposite sense. Some critics reproach to the Fund that it does not pay sufficient attention to the consequences of its conditionality for the distribution of economic goods in the country. No.4 of the guidelines cited above obligates the Fund to consider such consequences. But here once more this duty is not very effective: there is no guideline as to what value should be given to this point, whether it is more important than other points, or what should be the outcome of the balancing of conflicting points.

The non-discrimination rule of No.8 also is an important guideline. But one cannot deny that the adaptation of programs of recovery to the circumstances of every single country is necessary and that there hardly will exist equal or even sufficiently comparable situations which could only give rise to claims under the prohibition of discrimination. Thus it can be concluded that the secondary law of the organizations does not contain effective barriers against conditions which are politically relevant if their goal is only aimed at removing the balance of payments difficulties of the debtor state.

c. *Limits under general public international law*

In recent years some countries and writers increasingly reproached both organizations that their conditionality violates the duty not to intervene in the domestic affairs of the debtor states.[42] It is clear that a state may, by an international treaty or by unilateral pledges, accept obligations in matters that normally belong to its domestic jurisdiction. Then, the beneficiaries of such obligations may claim their fulfilment without violating the duty not to intervene.[43] But this is only true, if the obligation is accepted without the use of force or duress, against Art.52 of the Vienna Convention on the Law of Treaties[44] and against general public international Law, for this would make the obligation null and void.

The main question therefore is: Is the denial or refusal of a loan by IMF or World Bank

42 L'Hériteau, FMI, p.110.
43 Meessen, IMF, p.178: »volenti non fit iniuria«.
44 Of 23. 5. 1969, UNTS No.1155 (1980), p.331–512 = BGBl.1987 II, p.757.

a use of force by economic means? Is such use for force prohibited by public international law?[45] The latter question is very much contested in doctrine and practice. But even one of the most far-reaching formulations of such a prohibition of economic force, Art.32 of the Charter of Economic Rights and Duties of States,[46] prohibits only such force that envisages to obtain from another state the subordination of the exertion of its sovereign rights. This cannot be construed to entail a duty for international organizations to give loans to other states. The denial of a loan is not a use of force. There is obviously no duty to pay money to somebody else without having promised to do so. The present public international society is far from having accepted a legal duty even to pay social aid to poor states without talking about economic aid.

If such loans are combined with conditions, they do not amount to a use of force. States which do not want to fulfill such conditions are free not to do so and to decline those pressures. The law of both organizations guarantees this freedom. If recipient states do not decline these conditions because of their financial reasonableness, the acceptance cannot be ascribed to any exertion of force in the sense recognized in public international law.

Another limit may be seen in the prohibition of an abuse of rights or of a détournement de pouvoir.[47] It is contested whether such principles exist in general public international law[48]. But there are emanations of the basic ideas of such principles in the IMF law, namely the binding character of »policy decisions«, the prohibition of discrimination, the prohibition to use wrong facts when deciding and the duty to preserve political neutrality[49]. So it is not necessary to go back to the general principles, if they exist. The same is true of the World Bank law, especially the rule of Art.IV para.10.

45 Kewenig, W. A., Die Anwendung wirtschaftlicher Zwangsmaßnahmen im Völkerrecht, in: Berichte der Deutschen Gesellschaft für Völkerrecht, vol.22 (1982) p.7–35; Dicke, D.C., Die Intervention mit wirtschaftlichen Mitteln im Völkerrecht (1978); Bowett, D.W., International Law and Economic Coercion, Virginia Journal of International Law 16 (1976), p.245–259; Lillich, R.B., Economic Coercion and the »New International Economic Order«, Virginia Journal of International Law 16 (1976), p.233–244; Paschos, G., Die wirtschaftliche Intervention im Völkerrecht der Gegenwart. Diss. Heidelberg 1974 (1974).

46 Resolution of the U.N. General Assembly No.3281(XXIX) of 12. 12. 74.

47 Cf. generally Kiss, A.C., Abuse of Rights, in: R. Bernhardt (ed.), Encyclopedia of Public International Law, Inst. 7 (1984), p.1–5; id., L'abus de droit en droit international (1953); Laun, Richard, Das »détournement de pouvoir« im Völkerrecht, Mélanges en l'honneur de Gilbert Gidel, (1961) p.437–453; Voss, A., Rechtsmißbrauch im Völkerrecht (1940); Trifu, S., La notion de l'abus de droit dans le droit international, Diss. Paris (1940); Schlochauer, H. J., Die Theorie des abus de droit im Völkerrecht, Zeitschrift für Völkerrecht 17(1933), 373–394; Leibholz, G., Das Verbot der Willkür und des Ermessensmißbrauchs im völkerrechtlichen Verkehr der Staaten, Zeitschrift für ausländisches öffentliches Recht und Völkerrecht 1 (1929), p.77–125; Politis, N., Le problème des limitations de la souveraineté et la théorie de l'abus des droits dans les rapports internationaux, Recueil des Cours, 6 (1925 I), p.1–121. On the application of the prohibition on the activities of the Fund see Stratmann, IWF, p.216 ff.

48 Neuhaus, R. K., Das Rechtsmißbrauchsverbot im heutigen Völkerrecht (1984); Roulet, J.-D., Le caractère artificiel de la théorie de l'abus de droit en droit international public. Diss.Neuchatel (1958) state, that there is no prohibition of an abuse of rights in public international law are. Judge Alvarez (Corfu Channel: Merits, ICJRep.1949, p.4,48 and Anglo-Iranian Oil Co.: Preliminary Objection, ICJRep.1952, p.93,133) is very cautious about such a principle.

49 Stratmann, IWF, p.218.

Finally, some writers derive the principle of proportionality from the prohibition of an abuse of a right[50]. Such derivation is not necessary, if there is a general claim to access to the resources like under IMF law to the credit tranches. For this entails the treaty obligation to act in good faith and thus not to inflict more severe conditions on the applicant than necessary for securing that the money is paid back. So here too there is no need to resort to doubtful constructions of general public international law. But on the other hand it is doubtful per se whether such a good faith obligation is really an effective help against political influences given the broad margin of the organs involved. In the World Bank, where there is generally no claim to a loan, there is no evidence in the law that proportionality could bring about such a claim.

d. *Effectiveness of the legal limits*

But even given the general problems of delimiting politics and economics, the few limits which have been found may serve at least to prevent gross violations of the duties of both organizations. Thus they play a role already in the decision-making process for a loan. On the other hand politics are in some respect even increasingly important.

One example is that states differ about the importance of the human rights record of an applicant state as a determinant of the loan policy towards that state. The denial of such loans because of human rights violations for example has been discussed in the US Congress[51]. And when the World Bank gave a loan to Chile in December 1987, the U.S., France, Spain, the Netherlands and Belgium abstained in the Executive Board, because they wanted to make clear their repudiation of the country's deficiencies in human rights and democracy. Italy and the Scandinavian countries openly opposed the loan for those political reasons. On the other hand, the Federal Republic of Germany voted in favor of the loan stressing the duty of the Bank to be politically neutral. It was interesting to note that many developing countries voted in favor with a similar motivation[52]. This shows their interest in avoiding the exercise of political influence by powerful states trough economic pressure.

Similar considerations apply to the discussion about loans by both institutions to Portugal before the independence of her colonies and to South Africa preserving apartheid. When the U.N. asked for a refusal of loan applications, the World Bank answered by stressing its duty to be politically neutral[53]. The legal assessment of those cases depends on whether human rights violations, colonialism and apartheid are considered as being violations of international law and whether they are considered to be such violations »erga omnes«. Only then would it be conceivable for global international organizations

50 Stratmann, IWF, p.219.
51 Gold, Rule of Law, p.62.
52 Kölner Stadt-Anzeiger of 18. 12. 1987; Die Welt of 16. 12. 1987; Neue Ruhr-Zeitung of 18. 12. 1987.
53 Syz, Banks, p.162.

to be entitled to disregard as a reprisal, their own obligations toward a member state. But another gate is still open for purely political considerations in both organizations. Art. VI of their respective relationship Agreements with the United Nations[54] states that the organizations recognize that members of the U.N. may have a duty to observe within the organs of IMF and IBRD decisions of the Security Council in matters concerning the preservation of international peace and security under Art.48 (2) of the U.N. Charter. Furthermore, they accept the obligation to pay due regard to resolutions concerning sanctions under arts.41 and 42 of chapter VII of the Charter. In such cases, thus, political considerations are acceptable and they are legal since Art.103 of the Charter gives such obligations a higher rank than the duties under IMF or IBRD law.

V. Conclusions

Although some limits have been found to the discretion of both organizations in deciding on the conditions of loans, it has become clear that the particular features inherent in international monetary policy make it extremely difficult to enforce any such limits. Economic and financial considerations will usually prevail over strictly legal ones. This may lead to the statement that conditionality is a »trap« for indebted countries. But it is hardly credible that the law could really contribute to avoiding such a problem. This can only be done by creating conditions within the international economy that are reliable and effective and that give the indebted states a fair chance to get rid of their burden by paying back the debts in a foreseeable time period.

54 Agreement Between the United Nations and the International Monetary Fund. Agreement Between the United Nations and the International Bank for Reconstruction and Development, in: Agreements between the United Nations and the Specialized Agencies and the International Atomic Energy Agency, UNDoc. ST/SG/14.

ABSTRACTS

Conditionality of IMF and World Bank Loans

By *Werner Meng*

Many critics of the role of industrial countries in the international debt crisis are focussing on the role of the International Monetary Fund and the World Bank. If a country needs money to bridge deficits in its balance of payments, these organizations will only give credits if the debtor country agrees to conditions on restructuring the national economy. Such conditions may be very hard for the countries and their citizens.
This practice of conditionality is criticised with regard to its economic wisdom, and sometimes also for its lawfulness. The article describes basic features of the lending practice and then concentrates on the pertinent international law questions. Is there any legal limit to the freedom of the creditor to require specific measures of economic restructuring? The author concludes that such limits cannot be found in international law. The second question concerns the influence of general policy considerations on the credit decision. Here there are some limits within the law of the organizations and even a few in general international law, but their effectiveness is very doubtful. Thus conditionality is not so much a legal problem but more a question of sound economic policy.

Central America: External Debt and International Financial Relationships

By *Mechthild Minkner*

Since the escalation of the debt crisis in Latin America, an extended number of global and case studies have been undertaken. Like the concrete efforts of the creditors to resolve the crisis, these studies concentrate on the highly indebted countries. Not much attention has been paid to the small debtors such as the Central American countries and their special situation, since they neither agreed on a common policy toward the creditors nor do they pose a danger to the banks and the international financial markets. The external debt of the Central American nations – in absolute and relative terms insignificant in comparison with the big debtors – represents a serious problem to the region. Together with the social unrest and the political and military conflicts it is firmly part of the perilous state of the region.