Capital Flow Management and the Trading System

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IMF v. GATT/WTO legal framework

	IMF	GATT/WTO
Exchange rates	Shift from par-values to choice of exchange arrangements (soft and not enforced rules)	References to the IMF Articles
Exchange restrictions	Rules clearly prohibiting their adoption, with a few exceptions (IMF Art. VIII)	Reference to IMF rules and determinations to assess restrictions (GATT Art. XV)
Capital controls	Use of capital controls permitted (IMF Art. VI) + IMF surveillance over financial stability	Limits on capital controls in GATS + fragmentation in trade/investment treaties

Capital account liberalization as a by-product of the GATS principal goal

Art. XI:1 (Payments and Transfers):

after undertaking market access and NT commitments for specific service sectors, a State has to liberalize the connected current and capital movements

Footnote 8 to Art. XVI (Market Access):

capital controls on both inflows and outflows are prohibited for financial services provided under Mode 1, and for all services provided under Mode 3

Footnote 8 to Art. XVI (Market Access)

- if a Member undertakes a market-access commitment in relation to Mode 1 and if the cross-border movement of capital is ***an essential part*** of the service itself, that Member is thereby committed to allow such movement of capital

- if a Member undertakes a market-access commitment in relation to Mode 3, it is thereby committed to allow related transfers of capital ***into its territory***

CFMs may constitute a breach of:

- Market access (Art. XVI + Footnote 8)*, when the measure amounts to a ban or to a quantitative limitation*
- National treatment (Art. XVII), *when the measure accords less favorable treatment to foreign service suppliers*
- Domestic regulation (Art. VI)

GATS Safeguard Clauses

- **Art. XI:2**: capital controls can be introduced ***at the request of the IMF***
- **Art. XII:1**: in the event of a ***BoP crisis*** and once a list of ***requirements*** is met, Members are allowed to introduce ***controls on capital outflows*** (unclear whether applicable also on inflows)
- **FSA Art.2(a):** Members are allowed to introduce ***prudential*** *measures* irrespective of their specific commitments

The Scope of the GATS

The GATS does not define a “service”, but it excludes from its scope “services supplied in the exercise of governmental authority”, among which there are:

- activities conducted by a central bank or monetary authority or by any other public entity in pursuit of *monetary or exchange rate policies* (Art. 1 of Annex on Financial Services).

The GATS *ex ante* coordination clause with the IMF legal framework

GATS Art. XI:2

“Nothing in this Agreement shall affect the rights and obligations of the IMF members [...], ***including*** the use of exchange actions which are in conformity with the IMF Articles, provided that a Member shall not impose restrictions on any capital transactions inconsistently with its specific commitments regarding such transactions, ***except*** under Art. XII [the BoP clause] or ***at the request of the IMF*****.”**

The GATS BoP Clause (1)

Art. XII:1

"In the event of serious BoPs and external financial difficulties or threat thereof, a Member may adopt or maintain restrictions on trade in services on which it has undertaken specific commitments, ***including on payments or transfers for transactions related to such commitments***."

The GATS BoP Clause (2)

Art. XII:2

The restrictions shall:

- ***not discriminate*** among Members,
- ***be consistent with the IMF Articles***,
- avoid unnecessary damage,
- not exceed those ***necessary*** to deal with the circumstances,
- be ***temporary*** and ***phased out*** progressively.

The GATS Prudential Carve-Out

FSA Art.2(a):

"Notwithstanding any other provisions of the Agreement, a Member shall not be prevented from taking measures for ***prudential reasons***, ***including*** for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system. ***Where such measures do not conform with the provisions of the Agreement, they shall not be used as a means of avoiding the Member's commitments or obligations under the Agreement***."