



# **REVIEW OF SLOVAKIA'S ACCESSION TO THE OECD**

## **LIBERALIZATION PROGRESS COMPARISONS BETWEEN SLOVAKIA, CZECH REPUBLIC, POLAND AND HUNGARY**

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Slovakia's accession to the Organization for Economic Cooperation and Development (OECD), a Paris-based grouping of the world's most advanced economies, has been a fixture on the top priorities list in Slovak government's economic and foreign policy agenda. Coming on heels of a spell of increased integration efforts in 1999 and Slovakia's eventual entry in OECD in 2000, this paper takes a brief evaluation of the process. In addition, it seeks to draw comparisons between the progress made in capital movement liberalization in Slovakia, Czech Republic, Hungary and Poland.

During the accession process, Slovakia had to assume and implement the obligations of membership in a number of areas and go through a series of examinations by several OECD committees (e.g. Working Parties on Taxes, Insurance Committee, etc.). However, from the National Bank of Slovakia's (NBS) point of view, it is most important to look at the issue of capital transactions and examinations carried out by the CIME/CMIT committees (Committee on International Investment and Multinational Enterprises, and the Committee on Capital Movements and Invisible Transactions) which have played a critical part on Slovakia's way to the OECD.

This paper breaks down into three parts, the first containing a short description of the OECD, followed by a section dealing with the process of Slovakia's accession to the OECD and featuring a liberalization schedule for restrictions to be removed over the next few years. The last part rounds up the state of liberalization in the Czech Republic, Hungary and Poland. An easy-to-read timetable of Slovakia's financial liberalization is also included.

<sup>1</sup>The OECD Convention, signed in Paris on December 14, 1960, and in force since September 30, 1961, is the fundamental document laying down the following provisions:

- the Organization's objectives and ways to achieve them;
- decision-making procedures;
- designation of the OECD Council as the Organization's supreme body;
- designation of the Secretary-General as the Organization's chief executive officer;
- the Convention's effective dates and accession of new members;
- the Organization's headquarters set in Paris;
- legal capacity, privileges, exemptions and immunities of the Organization.

There are several committees and working groups operating under the OECD Council, focusing on specific issues and drafting documents which, once approved by the Council, represent recommendations to member countries.

### **OECD History**

OECD is one of those international organizations, which require their member countries to observe a specific set of rules and strive for defined objectives. As the OECD<sup>1</sup> Agreement<sup>1</sup> says, the aim is to achieve the highest sustainable economic growth and employment and a rising standard of living in member countries, while maintaining financial stability, and thus to contribute to the development of the world economy. OECD member countries today produce two-thirds of the world's goods and services. This club of like-minded countries is open to any country sharing and respecting the above principles.

The forerunner of the OECD was the Organization for European Economic Co-operation (OEEC) formed in 1948 to administer post-war reconstruction aid under the Marshall Plan and the European Economic Cooperation Conference. Since then, the Organization's vocation has been to promote cooperation between its member countries and foster trade relations in Europe in general by discarding tariffs and other barriers to free trade. It was around the time of its establishment that the first notions of a customs union or free trade zone started to take shape.

The accession of the United States and Canada in 1961 turned the OEEC into a global group (OECD), this status reinforced by Japan, Australia and New Zealand which signed up later on. By admitting Mexico, a country that can still be considered a developing economy, OECD's focus expanded to countries seen as a possible source of additional benefits. On July 8, 1994, the OECD Council, at a ministerial level, initiated talks with the Visegrad 4 countries to see how they complied with membership obligations in anticipation of their accession in the near future.

### **Slovakia's Road to the OECD**

The Slovak government made its official application for OECD membership along with the other V4 countries on February 28, 1994. Five months later, on July 29, 1994, the OECD Council, at a ministerial level, decided to launch accession talks with Slovakia. Cooperation between Slovakia and the OECD has been underway since 1993 under the Partners in Transition program (in place since 1991 for former Czechoslovakia) designed to prepare candidate countries for their integration. Apart from assistance in designing its

**OECD member countries with respective dates of accession**

Belgium	30. 9. 1961	Switzerland	30. 9. 1961
Denmark	30. 9. 1961	Italy	30. 9. 1961
France	30. 9. 1961	Turkey	30. 9. 1961
Greece	30. 9. 1961	United Kingdom	30. 9. 1961
Netherlands	30. 9. 1961	USA	30. 9. 1961
Ireland	30. 9. 1961	Japan	28. 4. 1964
Iceland	30. 9. 1961	Finland	28. 1. 1969
Canada	30. 9. 1961	Australia	7. 6. 1971
Luxembourg	30. 9. 1961	New Zealand	29. 5. 1973
Germany	30. 9. 1961	Mexico	18. 5. 1994
Norway	30. 9. 1961	Czech Republic	21. 12. 1995
Portugal	30. 9. 1961	Hungary	7. 5. 1996
Austria	30. 9. 1961	Poland	22. 11. 1996
Spain	30. 9. 1961	Korea	12. 12. 1996
Sweden	30. 9. 1961	Slovakia	14. 12. 2000

economic policies, the OECD allowed Slovakia to attend its working groups meetings as an observer.

One of the critical questions that had to be answered on Slovakia's way to the OECD was whether it was ready to assume the obligations in the field of international investments and free movement of capital and services in the extent required from a future OECD member. All the matters related to these two areas are addressed by the Committee on International Investments and Multinational Enterprises (CIME) and the Committee on Capital Movements and Invisible Transactions (CMIT). The findings of Slovakia's first assessment by the CIME/CMIT in July 1996 have been reported in a document entitled „Conclusions of the Chairman of a Joint CIME/CMIT Meeting with the Slovak Republic held on July 2 – 3, 1996., (hereinafter the “Chairman's Conclusions,“), in which the committees noted that the number and extent of objections to OECD's Liberalization Codes was too large for a would-be OECD member.

The degree of liberalization Slovakia had attained by July 1996 is clear to see from the liberalization timetable shown in the financial liberalization schedule (direct investments in EU countries only). The truth is that actual liberalization action was not taken until December 1, 1996, a little later than the September 30, 1996, promise made during the first examination.

The Slovak government's resolution No. 775 entitled “Specific Action Proposed to Implement the Chairman's Conclusions on the Joint CIME/CMIT Meeting with the Slovak Republic held on July 2 – 3, 1996,“ adopted on November 19, 1996, set out specific steps that had to be taken if the country were to pass the second examination by the CIME/CMIT. In years that followed, most of the proposals outlined in the resolution failed to materialize, or were just partly fulfilled. It was because Slovakia missed the deadline its top officials committed to at meetings with the OECD that made several member countries turn skeptical and demand more bulletproof guarantees than they would normally require from other recently admitted newcomers.<sup>2</sup>

Even though Slovakia has duly delivered the room

documents<sup>3</sup> at regular CIME/CMIT meetings, the OECD Secretariat would not authorize Slovakia's second CIME/CMIT examination before it sent an Official Response to the Chairman's Conclusions. The Official Response, taking 3 years since the 1st examination to be passed by the government (December 1, 1999), considerably speeded up accession talks. The CIME/CMIT meeting of April 27, 2000, with an agenda including Slovakia's 2nd examination, reviewed and appreciated its progress based on practical and legislative changes adopted by the Slovak government, and proposed to the OECD Council to accept Slovakia for a full member (subject to the resolution of an outstanding disagreement with clause H/1 – Films – in the Liberalization Codes). Eventually, the disputed issue had been settled just hours before Slovakia was offered to become OECD's 30th member (July 28, 2000) at negotiations over audiovisual products with France and the European Commission facing off the United States.

The accession process also involved assessments of tax and environmental policies, as well as an examination by the Trade Committee. Even though the full battery of tests have been completed in the 1995 – 1998 period, an update was required due to a long period passed until talks resumed.

Before the final decision could be made to invite Slovakia to join the OECD, the OECD Council had to discuss Slovakia's position regarding not only the Liberalization Codes, but some other norms too, including decisions, recommendations and other instruments in force. The resulting assessment, summarized in a so-called Memorandum, was subsequently reviewed by Slovak authorities and the Council for Cooperation with the OECD in April 2000.

With OECD's invitation handed out to Slovakia, it was the Slovak government's turn to declare its agreement on accession to the OECD Convention. The Agreement on Invitation for Slovakia to accede to the OECD Convention, signed on September 28, 2000, in Paris by the Slovak foreign minister and OECD's Secretary-General, contains both the Slovak Government's Stance on assuming Slovakia's obligations under OECD membership and the OECD Council's invitation for Slovakia to join the Organization. For Slovakia to accede to the OECD Convention, the act had to be approved by the Slovak National Council (October 26, 2000) and ratified by the Slovak president. It was not until the moment of accession to the Convention and the moment the ratification deed was deposited with the official depositary (the French government) on December 14, 2000, that Slovakia officially became OECD's 30th member.

<sup>2</sup>At the same time, OECD members started to pay greater attention to macroeconomic stability of candidate countries and their ability to implement reforms in the liberalization process. Following the accession of Mexico, Czech Republic, Hungary, Poland and Korea, several failures to live up to their promises prompted the OECD to tighten the criteria for new candidates (e.g. Czech Republic's received a critical review in CIME/CMIT's compliance check carried out two years after it had joined the OECD in 1995).

<sup>3</sup>Documents delivered at OECD meetings.



## Financial Liberalization in Slovakia

Slovakia has pursued a step-by-step strategy in financial liberalization based on generally accepted principles: a prior liberalization of the long-term to short-term flows within capital and financial accounts, preference of inflows to outflows, foreign direct investments to financial credits, and the liberalization of the most risky items as the last.

In July 1996, as the 1st CIME/CMIT examination was underway, Slovakia vowed to scrap restrictions on capital movements by end-2000. At that time, the CIME/CMIT found that in case of Slovakia the remaining number of reservations to OECD's Liberalization Codes was excessive. In December 1996, Slovakia did ease its grip on direct investments in OECD member countries, long-term financial credits (credits granted to non-residents based in OECD member country with maturity over 5 years, credits received from non-residents with maturity over 3 years), trade credits, and real estate acquisition by residents in OECD member countries. After this initial liberalization spree, Slovakia's accession process slowed down and it was obvious the deadline for total capital liberalization (2000) would be missed.

An amendment of the Foreign Exchange Act, taking force in April 1998, marked yet another step towards full liberalization, allowing branches of foreign banks to acquire real estate in the Slovak Republic necessary for their operations. However, there still was a 10-year retention period limiting foreign bank branches desiring to sell or let the property. Other items liberalized included issues and introductions of foreign securities to the domestic market, provided the issuer was incorporated in an OECD member country and its securities were traded on a main foreign stock exchange, as well as OECD government bonds. At the same time, residents were allowed to trade in these securities. April 1998 saw the abolition of a surrender requirement according to which domestic legal persons were obliged to sell off any foreign currency acquired to authorized foreign exchange entities.

Keeping up its increased OECD accession momentum from 1999, in early 2000 Slovakia adopted another amendment to the Foreign Exchange Act and a new related implementing decree. Based on this legislation, the country was able to lift the remaining restrictions on medium and long-term capital transactions: financial credits and securing of obligations with maturity over 1 year, issue of domestic debt securities abroad with maturity over 1 year, as well as real estate acquisitions in the Slovak Republic for all branches of foreign financial institutions (banks, insurance companies, securities dealers and collective investment companies). Transaction with foreign securities, liberalized in April 1998 for OECD countries, were also opened to issuers from non-OECD countries.

The Foreign Exchange Act amendment helped streamline the law-making procedure by extending the application of the aforesaid decree to all operations, except for domestic real estate acquisitions. This means that any future liberalization

actions (other than those related to real estate) will only require a revision to the decree, not to the Foreign Exchange Act itself.

Further capital liberation came on January 1, 2001, when the latest Foreign Exchange Act amendment and a related Implementing Decree went into force, releasing financial credits and securing of obligations with maturity up to 1 year. The latest move also freed real estate acquisitions in the Slovak Republic (foreign direct investments) as required under the European Accession Agreement. Under the Accession Agreement, in effect since February 1, 1995, „The Slovak Republic shall grant the rights to acquire, use, rent and sell real property, where necessary for the conduct of the economic activities for which they are established, to branches and agencies established in the Slovak Republic of Community companies at the latest by the end of the sixth year following the entry into force of this Agreement.“ Under this provision, however, the right to engage in real estate operations is limited to EU-based companies. Slovakia has committed to extend its obligations assumed under the said agreement to non-EU OECD members too (Slovak government resolution No. 214 of March 19, 1996)<sup>4</sup>.

In addition to real estate acquisitions, direct foreign investments are still restricted in the energy<sup>5</sup> and aviation<sup>6</sup> sectors. Further restraints applying to lotteries and similar games<sup>7</sup> have been addressed by an amendment to the Act on Lotteries and Similar Games, which became effective on January 1, 2001, dropping the required government stake in casino operators, and removing the ceiling on foreigners' participating interest in lottery and casino operators. A revised Stock Exchange Act and Securities Act, taking force on November 1, 2000, abolished the restrictions on direct foreign investments in the stock exchange and the Securities Center.<sup>8</sup>

Further liberalization action is planned over a period of 3 years. A liberalization move slated for the end of 2001 is set to extend the right to conduct foreign securities operations to issuers whose securities are traded on OTC markets. A more

<sup>4</sup>A similar situation occurred in the liberalization of direct outgoing foreign investments. After the said agreement took effect, liberalization of direct investments in EU countries was extended to all OECD members by a decree to the Foreign Exchange Act adopted on December 1, 1996.

<sup>5</sup>Energy industry business licenses may only be granted to natural persons residing or legal persons incorporated in the Slovak Republic (restriction to be retired on December 31, 2003).

<sup>6</sup>Aviation licenses may be granted to a domestic airline provided that, if a legal person, foreign persons hold less than 50% of its assets, or if a natural person, he/she has Slovak nationality and permanent residence in the Slovak Republic (no specific liberalization deadline set in this particular sector).

<sup>7</sup>Previously, lotteries and similar games could only be operated by legal persons incorporated in Slovakia with no foreign stakeholders. A casino license was only available to legal persons, in which the state, or a partly state-owned legal person, held no less than 51%.

<sup>8</sup>Foreign investors and legal persons incorporated in Slovakia with a foreign capital participation in excess of 50% of registered equity capital were only allowed to acquire stock exchange shares with nominal value not exceeding one-third of its registered capital. Foreign participation in the Securities Center capital was not allowed to surpass 25%.



extensive liberalization sweep scheduled for end-2002 should leave securities transactions and financial derivatives absolutely unrestricted. The end of 2003 should bring about a liberalization of deposit transactions, cancel the transfer obligation, and free up foreign currency operations.

As soon as that treatment is complete, Slovakia's capital and financial account is bound to be fully liberalized in relation to OECD countries. Some restrictions will remain in domestic real estate acquisition for entities yet excluded from liberalization. Depending on Slovakia's EU accession process, these operations should be liberalized as follows:

- with effect from the date of Slovakia's accession to the EU, but no later than January 31, 2005 – acquisition of ownership rights to real estate located in Slovakia required for business operations by non-resident individual entrepreneurs from the European Economic Area (EEA)<sup>9</sup> and OECD;

- with effect from the date of Slovakia's accession to the EU, but no later than January 31, 2005 – acquisition of ownership rights to real estate located in Slovakia by EEA and OECD companies and nationals, except for real estate subject to a transitional period<sup>10</sup>.

## Financial Liberalization in Slovakia

### February 1, 1995

- direct investments in European Union member states

### December 1, 1996

- direct investments in OECD member countries
- acquisition of real estate by residents in OECD member countries
- export and import of banknotes and coins denominated in the Slovak or a foreign currency - reporting requirement for sums in excess of SKK 150,000 (travelers) or SKK 20,000 (postal items)
- financial credits granted by residents to non-residents based in an OECD member country with maturity over 5 years
- financial credits received by residents from non-residents with maturity over 3 years

### April 1, 1998

- issues of foreign securities on trading in Slovakia or their introduction on domestic market, provided that the issuer is

<sup>9</sup>The EEA consists of the 15 EU member states and Iceland, Norway and Liechtenstein. Since the EU has concluded free capital movement agreements with the non-EU EEA members, it requires candidate countries to liberalize their capital transactions with these countries as well (note: Liechtenstein is not an OECD member).

<sup>10</sup>In negotiation chapter 4 – Free Capital Movement – Slovakia demands:

- a 5-year interim period starting on the date of its EU accession applicable to the acquisition of ownership rights to real estate used as secondary residence by EEA citizens;
- a 10-year interim period starting on the date of its EU accession applicable to the acquisition of farm and forest land used as secondary residence by EEA citizens and companies.

based in an OECD member country and its securities are traded on a main foreign stock exchange, or if the securities are government bonds of an OECD member country

- permission for residents to trade with the aforementioned securities
- abolishment of surrender requirement
- branches of foreign banks – acquisition of the right of ownership to real estate located in the country, which is indispensable as operational premises for the conduct of the business activities if such real estate is acquired under a general contract (transfer of such real estate to another person allowed after 10 years from the date of its acquisition)

### January 1, 2000

- securities operations mentioned under the April 1, 1998, extended to non-OECD countries
- issues of domestic debt securities abroad with maturity over 1 year
- financial credits granted by residents to non-residents based in an OECD member country with maturity over 1 year
- financial credits received by residents from non-residents with maturity over 1 year
- sureties, guarantees and financial back-up facilities with maturity over 1 year
- non-resident financial institutions (banks, insurance companies, securities dealers and collective investment companies) – acquisition of the right of ownership to real estate located in the country, which is indispensable as operational premises for the conduct of the business activities

### January 1, 2001

- acceptance and granting of financial credits with maturity under 1 year
- sureties, guarantees and financial back-up facilities with maturity under 1 year
- non-resident based in EU or OECD member country with the organizational unit established in the country for the conduct of the economic activities – acquisition of the right of ownership to real estate located in the country, which is indispensable as operational premises for that organizational unit

## Future liberalization actions

### 2001

- securities operations in OTC markets

### 2002

- liberalization of financial derivatives and remaining restrictions on securities

### 2003

- abolition of the transfer requirement and liberalization of foreign currency operations

*To be continued in No. 3/2001*