OECD Codes of Liberalisation

NEW GOVERNANCE ARRANGEMENTS

July 2012

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OECD invites non members to join the Codes with full rights and duties

On 28 June 2012, the OECD Council adopted a landmark decision on governance of the Codes of Liberalisation. Full decision-making powers have been delegated to the Investment Committee which will be enlarged to include non members willing and able to meet the standards of adherence; all adherents will have equal rights and obligations.

The Codes are the only multilaterally-backed instruments promoting the freedom of cross-border capital movements and financial services while providing flexibility to cope with situations of economic and financial instability. For 50 years adhering countries have used the Codes to support reform, to co-operate to reap the full benefit of open markets and to avoid unnecessary harm from restrictive measures.

Since the 2008 financial crisis, there has been a renewed interest in capital and exchange controls. While such measures may be effective in the short run, they also entail risks. These include risks of counter-measures by other countries and a fragmentation of the international financial system. International co-operation is essential to avoid undesired collective outcomes as countries move to deal with global imbalances and financial turbulence. With their procedures for transparency, accountability, consultation and dialogue, the Codes make a unique contribution to maintaining and advancing international co-operation.

The Codes of Liberalisation of Capital Movements and of Current Invisible Operations (hereafter the Codes) are now open to adherence by all interested countries. This is a major evolution and one which would increase international co-operation in an area in which such co-operation is vital. This document describes the role of the Codes, the benchmarks for adherence, the governance of the Codes, and the procedures to follow to join the Codes.

ROLE OF THE CODES

Free circulation of capital, investment and services across national frontiers is a motor for economic growth, employment and development. It encourages competition and economic efficiency to the benefit of consumers and provides financial resources and technological innovation to companies. It benefits the host country and the country of origin, developed and developing countries alike. But achieving free movement of these flows requires liberalisation which usually is attained progressively and which must take account of the economic and financial situation of each country and its stage of development.

To meet these objectives, countries within the OECD created fifty years ago a balanced framework for international economic and financial co-operation and gradual progress towards liberalisation: the Code of Liberalisation of Capital Movements which also covers direct investment and establishment, and the Code of Liberalisation of Current Invisible Operations which covers cross-border services.

Building on a cooperative and consultative process, the Codes have assisted in creating an environment in which all member countries, including the less advanced among them and those going through temporary economic difficulties, have been able to pursue their national policies while progressively eliminating unnecessary barriers to the free circulation of capital and services. At the same time, the Codes have served as a yardstick by which the liberalisation efforts of adhering countries can be assessed and compared over time.

Capital flows are an integral component of international finance. They allow for savings to be channelled from surplus countries to deficit countries, where returns to investment are typically higher. However, these flows can also pose important challenges to open economies. Excessive inflows can lead the economy to overheat and fuel credit and asset price bubbles. Sharp reversals in capital inflows are disruptive.

In the current world economic environment, individual countries may be tempted to take unilateral measures or counter-measures that may damage the international system that has served the world well for decades. While concern about protectionism is usually directed mainly to trade measures, capital controls may have similar consequences as they affect international markets and exchange rates. In this difficult period, the Codes can guide the actions of national authorities dealing with cross country capital flows and trade in services. The Codes process provides multilateral support for the maintenance of open regimes and identifies the circumstances in which restrictions may be introduced, subject to the principles of non-discrimination, transparency, proportionality and accountability.

International investment spurs prosperity and economic development in home and recipient countries. Policy co-ordination helps governments resist protectionist pressures and develop effective policies to respond to genuine concerns raised by foreign international investment.

Balance of rights and obligations

Obligations include:

- Notification of all measures having a bearing on the Codes;
- Standstill for liberalisation for most capital movements, all international financial and other services covered by the Codes, and any current payments and transfers;
- Regular examination by the Investment Committee of remaining restrictions with a view to their elimination;
- Need for an invocation of the Codes' derogation clauses to be accepted by the other adherents;
- Acceptance to enter into consultation if another adherent feels adversely affected by domestic arrangements;
- Abide by the most-favoured-nation principle.

Rights include:

- Benefit from liberalisation measures of others;
- Not to be discriminated against;
- To be notified of and consulted on other adherents' measures;
- To consent to modification of other adherents' reservation lists;
- To examine the position of candidates for adherence to the Codes;
- Agree, or veto, proposed interpretations and amendments of the Codes.

BENCHMARKS FOR ADHERENCE

The Codes establish commitments for all adherents in three main policy areas:

- Foreign direct investment, including general policies and sectoral policies.
- Other capital movements, both long-term capital movements (items on List A) and short-term capital movements (items on List B).
- Cross-border trade in services, including banking, insurance and other financial services.

A country wishing to adhere to the Codes will be reviewed and assessed on its merits, in light of the specific circumstances of the country, including its level of economic and financial development and taking into account the provisions of the Codes. All adherents are expected to meet a satisfactory standard.

Adherent countries are expected to fulfil the following three core principles:

NON-DISCRIMINATION: Grant the benefit of their liberalisation measures to all other adherents and apply remaining restrictions in a non-discriminatory fashion.

TRANSPARENCY: Report up-to-date information on barriers to capital movements and trade in services which might affect the Codes' obligations and the interests of other adherents.

STANDSTILL: Avoid taking new restrictive measures or introducing more restrictive measures except in accordance with the Code's provisions or established understandings regarding their application.

In addition, adherents are expected to:

- avoid the lodging of 'precautionary' reservations under the Codes (reservations should be limited to existing restrictions);
- maintain an open and transparent regime for FDI including in key sectors (restrictions should be limited and concern sectors where restrictions are not uncommon in OECD countries);
- liberalise other long-term capital movements, including equity investment and debt instruments of a maturity of one year or more as well as commercial credit and other capital operations relating to international trade; and establish a timetable for liberalising remaining controls on short-term capital movements.
- avoid restrictions on payments or transfers in connection with international current account transactions; the candidate countries must comply with all IMF Article VIII requirements;
- relax restrictions on cross-border trade in services, particularly banking, insurance and other financial services;
- ensure fair and transparent implementing practices and proportionality of the measures relative to the stated objective pursued.

The number and scope of reservations as well as any transition periods would be considered on a case-by-case basis.

Adherence procedure

Interest

- The interested country writes to the OECD Secretary-General, explaining the reasons for its interest. While it is technically possible to adhere to both Codes or to only one, it is expected that non members will adhere to both Codes.
- Upon recommendation by the enlarged Investment Committee (i.e. including non member adherents), the country may be invited to undertake a comprehensive review of its proposed position under the Codes.

Review

- The Secretariat prepares a report on the country's position, based on information provided by the applicant country and through staff missions.
- The enlarged Investment Committee examines the applicant's position under the Codes, taking into account the circumstances of the applicant, including its level of economic and financial development.
- The review process may take 12-18 months or longer if legislative changes are required. The country concerned is responsible for financing the review process.

Invitation

- An invitation to adhere to the Codes is made on the basis of the enlarged Investment Committee assessment of the applicant country's position and by a concurrent decision of both the enlarged Investment Committee and the OECD Council.

Adherence

- The adherence process concludes with a legally binding exchange of letters between the Secretary-General and the country's government setting out rights and obligations of the country as an adherent to the Codes, including its list of agreed reservations.

GOVERNANCE OF THE CODES

The Codes are governed by the OECD Investment Committee which considers all matters concerning the operation of the Codes. The Committee acts as a forum for discussion and exchange of information, considers questions of interpretation of their legal provisions, reviews country measures and assesses their conformity with the Code obligations.

Advisory Task Force on the Codes of Liberalisation

In order to manage the heightened inter-national co-operation and policy dialogue that the Codes are now generating, a new body has been created – the Advisory Task Force on the OECD Codes of Liberalisation. The Task Force, which gives special attention to issues arising in financial markets and financial services including insurance, held its inaugural meeting at OECD headquarters in Paris on 25 April 2012.

The OECD Council has decided to enlarge the Investment Committee to include participation of countries adherents to the Codes, but which are not OECD members, with equal rights and responsibilities. The enlarged Investment Committee has been given the authority to take all final decisions concerning the Codes of Liberalisation.

Should the existing text of the Codes need to be amended, the amendment decision would need to be agreed both in the enlarged Investment Committee and in Council. This "double consensus rule" also applies to the decision to invite an additional country to adhere to the Codes. Accordingly, no decision regarding the Codes can be made without the consent of adherents that are not members of the Organisation ■

The Codes of Liberalisation Online
www.oecd.org/daf/investment/codes

Access the full texts, latest adhering country reservations, data, research and analysis.

For more information about adhering to the Codes, please contact:

Mr. Angel Palerm
OECD Investment Division
+331 45 24 76 48
angel.palerm@oecd.org

High-level Seminar on Capital Flow Management and Liberalisation: The Role of International Co-operation

9 October 2012 - Paris, France

This seminar will bring together high-level officials, experts and private sector stakeholders from OECD and non-OECD countries. Its objective is to advance shared understandings on policies to make the most of cross-border capital flows in support of growth and development and on the value of international co-operation, including the OECD Codes of Liberalisation, in the current context of serious global financial turbulence.

The seminar will be opened by Angel Gurría, Secretary-General of the OECD and Stanley Fischer, Governor of the Bank of Israel, former First Deputy Managing Director of the IMF.

<table>
<tr><th colspan="2">DRAFT PROGRAMME</th></tr>
<tr>
<td>SESSION I. Making the most of capital flows
What are the recent trends in global capital flows? What new risks and opportunities do they create, in particular for emerging economies?
What macroeconomic, structural and other policies are best suited to make the most of cross-border capital flows in support of sustained growth and to increase economies’ resilience to capital flow volatility?
Do policies affecting capital flows have multilateral implications? Is international co-operation important to avoid unfavourable collective outcomes from individual country measures?</td>
<td>SESSION II. Tailoring capital flow management and liberalisation strategies to national circumstances
What factors have been driving liberalisation efforts?
Which pre-conditions for orderly liberalisation?
Short-term versus long-term capital flows, interest-bearing instruments versus equity investments, capital inflows and capital outflows. How to sequence liberalisation?
In the event of reintroduction of restrictions, how to make them least disruptive on normal business operations?</td>
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<td>SESSION III. The Codes of Liberalisation as instruments of international co-operation
What are the benefits of the Codes for adhering countries and international co-operation?
How do they contribute to increased transparency?
How is mutual accountability being achieved?
How much space for pursuing domestic policies under the Codes?
How do the Codes accommodate different levels of development?
What are the terms and conditions for adherence by new countries?</td>
<td>SESSION IV. Looking to the future
Is there a need for improving clarity and consistency in the international architecture governing capital flows? What can be done?
Is the network of international agreements robust enough to avoid a possible destructive escalation of capital controls and counter-measures in the event of serious shocks affecting the global economy, such as contagion of debt crises and currency wars?
What are the implications of a system with adherents and non-adherents to the Codes?</td>
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Find out more at www.oecd.org/daf/investment/codes