

GENERAL PROVISIONS OF THE EUROPE (ASSOCIATION) AGREEMENTS

Elżbieta Kawecka – Wyrzykowska, Sándor Meisel

Introduction¹

Three countries of Central and Eastern Europe (Poland, Hungary and Czechoslovakia) initiated bold reforms of their political systems and economies in 1989. Practically from the very beginning, Central and Eastern European countries (CEECs) sought for closer relations with the then European Community (EC), both for economic and political reasons.

In the middle of 1990 all three countries (Czechoslovakia at this time was still one country) officially applied for a beginning of negotiations for an agreement of association, and the official negotiations with all three countries began in December 1990. Talks were concluded in autumn 1991 and on 16 December 1991 bilateral association agreements were signed between the European Communities and their Member States on the one hand and each of those three countries: Czechoslovakia, Hungary and Poland.²

¹ This chapter bases on the following chapters: Poland prepared by E. Kawecka-Wyrzykowska and Hungary prepared by S. Meisel, published in: *From Association to Accession. The Impact of the Association Agreements on Central Europe's Trade and Integration with the European Union*, ed. by K. Mizsei and A. Rudka, Institute for EastWest Studies, Warsaw, Prague, Budapest, Kosice, New York, 1995.

² Later similar association agreements were negotiated with other countries which started transformation, it is: Bulgaria, Estonia, Latvia, Lithuania, Romania, Slovenia. The full name of EA was the following: Europe Agreement establishing an association between the European Communities and their Member States, on the one part, and the mentioned countries that signed similar agreements, on the other part.

The Agreement with Czechoslovakia was renegotiated after the dissolution of the country as of 1 January 1993. At that time a new clause was added to agreements with Slovakia and Czech Republic, making association conditional on political requirement consisting in “Respect for the democratic principles and human rights established by the Helsinki Final Act and the Charter of Paris for a new Europe, as well as the principles of market economy” (Art. 6 of the Association Agreements). Those rules were to be respected by all parties to the Agreements. They were included also in the further Association Agreements signed by the European Communities with their European partners.

In other areas the coverage of the Agreements was almost identical. Differences applied mainly to slightly different timetables of trade liberalisation, of adjustment of national laws to the EU laws as well as timetables of implementation of other liberalisation commitments. The commercial parts of the Agreements entered into force on 1 March 1992 (on the basis of so called Interim Agreements) and the whole Agreements became applicable on 1 February 1994 (after ratification by respective partners).

All CEECs treated the EAs as a first step to full integration and stressed the agreements’ important role in their relations with the EU. This helped to achieve relatively soon the EC decision on membership criteria (during European Council in Copenhagen in June 1993). The Copenhagen meeting, though vaguely, stated formally the possibility of those countries joining the EC if they were willing and able to fulfil the necessary obligations, just broadly defined in the Summit conclusions.

Europe Agreements included the establishment of a political dialogue and the creation of a free trade area in trade in goods between the EC and a respective associated country. Some opening up of the partners’ markets was provided in the field of movement of workers, establishment of companies and supply of services, as well as in the area of movement of capital. Also, EAs included a set of commitments by the associated countries to approximate their legislation to that of the Community (some of them being compulsory for CEECs). As a first step in the process of the approximation of legislation the EAs stressed the necessity to harmonise laws directly related to trade. Provisions on economic and

cultural cooperation were rather general, identifying areas of possible mutual interest. Provisions on financial cooperation offered CEECs some stability in terms of access to financial support under PHARE (Poland-Hungary Assistance for Restructuring their Economies), access to loans of the European Investment Bank and support for special fund to stabilise their currency.

As regards provisions for trade liberalisation, they were different in case of non-agricultural products (industrial goods and raw materials) and agricultural products. The first group provided for creation of free trade area, i.e. elimination of all border barriers. This goal was achieved basing on the asymmetry, it is earlier and faster elimination of trade barriers by a stronger partner (EC) and slower and usually delayed opening up of markets of CEECs.

Liberalisation of trade in non-agricultural products

Regarding trade in non-agricultural products, all parties of the EAs committed themselves to observing the standstill principle, i.e., not introducing any new restrictions or not increasing already existing tariffs. Omission of this clause would make it possible to increase the scope of protection after the entry into force of the Agreements, which would violate the arrangements made earlier. In some exceptional cases defined in the Agreements, it was possible to raise the level of protection by using safeguard clauses. The basis for duty reduction was established in a way that allowed taking into account the outcomes of the Uruguay Round negotiations.

The EAs immediately removed almost all quantitative restrictions (QRs) on industrial imports from the CEECs, except for textiles, steel and coal. They also removed tariffs on over 50% of the EC imports from the region. Tariffs on most of other products were to be abolished over a two-to-five year period (in case of Hungary – lasting to 7 years), except for textiles and clothing. For 1995, the average (weighted) tariff rates for imports from CEECs were estimated at 1.2% for Hungary, 1.1% for Poland and only 0.7% for former Czechoslovakia.³

³ European Commission: “Trade liberalisation with Central and Eastern Europe”, European Economy, Supplement A. Recent economic trends, No. 7, July 1994; cited from: From Association to Accession, op.cit., p. 5.

Besides textiles and clothing, a few other groups of products (iron and steel, chemicals, furniture, leather goods, footwear, glass and vehicles) were treated as sensitive sectors, so trade of them was also to be liberalised at a slower pace. Moreover, exports of sensitive products from CEECs to EC were subject to liberalisation in the framework of preferential quotas (reduced import duty only for a limited amount of goods). The Copenhagen European Council (June 1993) decided to implement faster liberalisation in those categories. As a result, almost all of the non-agricultural exports of CEECs to the EC were practically liberalised as of the beginning of 1995.

The schemes of CEECs concession on non-agricultural products were much simpler. In Poland, with the entry into force of the Interim Agreement, Poland abolished tariffs on about 28% of the value of industrial imports from the EC, mainly raw materials and capital goods, especially technologically advanced equipment to stimulate the restructuring. Liberalisation of access to the Polish market for the remaining non-agricultural products started on 1 January 1995 (except for cars, which were liberalised only in 10 year period, i.e. till the beginning of 2002). Liberalisation of those products continued in five equal instalments (20% of the basic rate in each year), the last reduction taking place at the beginning of 1999.

The situation was different in Poland for automotive products for which 10 year transitional period for elimination of tariffs was provided for (supplemented with duty free quotas for EC cars exported to Poland).

Let's add that all reductions of customs duties were speeded up by the liberalisation on multilateral forum, as agreed in the Uruguay Round and introduced in several years, starting on 1 January 1995.

The process of duties elimination in the Hungarian non-agricultural imports may be divided into three parts. From the entry into force of the Interim Agreement until 1 January 1994, Hungary eliminated during three years in three equal phases the duties of the so-called "quick list". The share of the concerned products of dutiable industrial imports was about 15 per cent in 1991, but it diminished after the adoption of the EA. Imports of goods listed here were marginal both from the fiscal and structural points of

view. The criteria of being listed here were a relatively low level of duties and the minimisation of economic effects (i.e. these concessions were rather symbolic, with no substantial trade effect). Mainly machinery and chemical products, consumer goods, metal and metallic products were included in the so-called “normal list”. The duties on these products were to be eliminated between 1995 and 1997 in three equal steps. The share of these goods in the Hungarian industrial exports was about 20-25 per cent. The structure of the so-called “slow list”, containing products for which duties were to be eliminated relatively slowly and gradually, was similar to that of the normal list with the difference that textile and clothing and metallurgical products were mostly listed here. Part of them was also protected by quantitative restrictions. These duties were phased out by the end of 2000.

As far as the Czech Republic is concerned, imported industrial products were divided into three groups: non-sensitive, moderately protected and sensitive. The termination of tariff protection was differentiated as follows: for non-sensitive products from the date of the EA entering into force, for moderately protected commodities from 1 January 1997 and for sensitive products from 1 January 2001.

Liberalisation of trade in agricultural products

The provisions of the Europe Agreements concerning trade in agricultural products were very complex as they involved the most-protected area of the EC activity. The commitments were limited (small reduction, not full elimination of protection) and selective (they included a relatively short list of products and did not cover all products as it was the case with non-agricultural products). Some product groups were excluded from the concessions (e.g. wheat, sugar, most of the milk products, etc.).

As a general rule, the EC granted concessions to CEECs in the form of tariff quotas for defined products with gradually increasing levy or tariff reduction over the coming years. These concessions were valid for defined quantities of products imported from the Visegrád countries. The preferential quotas were increasing from the entry into force of the agreements by yearly 10% over 5 years.

The administration of the tariff quotas in many cases was bureaucratic and sometimes non-transparent.

On the import side the scheme of concessions granted by the associated countries was different. For its part, Poland introduced a one-off reduction of tariffs covering 250 agricultural products. The tariff reduction by 10 percentage points (usually from 35% to 25%) was implemented on the day of the Interim Agreement's entry into force. Products subject to liberalisation in Poland were mostly products not competing with domestic production (e.g. oranges, bananas, rice etc.).

In Hungary the scheme of agricultural import concessions accorded to the EC suppliers followed that on the export side. Nevertheless, the product coverage of the concessions was more limited and the volume of the preferential quotas remained lower than on the export side. The pace of increasing these quotas was only the half as compared to their quotas in the EC.

According to the Hungarian experience, concessions established in the EAs could produce two types of effects. On the one hand reduction of import charges could result in rising selling prices. On the other hand, because the concessions are usually shared by the exporter and importer (in practice, most of it went to the importer), these concessions were able to heighten the interest of importers to buy products from the CEECs, thus to maintain or increase the level of trade. In reality, the reduction of the import burden was not perceptible in the export prices of the most Hungarian products. In many cases even a price decrease was registered or, if prices increased, they did not reflect the amount of the duty and levy reductions. Generally speaking, the concessions were not able to significantly increase the volume of exports either. In the Hungarian imports, since the concessions were limited, the EA scheme itself did not substantially influence imports.

One should also mention the experience of agricultural trade in relation to the protection measures that were taken by both sides. While in the trade of industrial products the EC applied a relatively open treatment towards CEECs products, there were no substantial changes in the Community's restrictive regime in the trade of agricultural and food products (because in spite of the concessions, the EA left untouched the agricultural system of the parties).

Moreover, as a contrast to the industrial sector, limited agricultural liberalisation did not enforce strong adjustment impulses to the agriculture in the CEECs. That became a must only in the period of the accession.

Safeguard clauses

Contingent protection measures (anti-dumping and anti-subsidy clauses and general safeguard clauses) as well as other protection providing rules were contained in the EAs. Most of them referred to standard GATT/WTO safeguard clauses and could be applied by both partners. They included the following.

- The general clause. This allowed actions where “... any product is being imported in such increased quantities and under such conditions as to cause or threaten to cause ... serious injury ... or serious disturbances...”⁴ for domestic producers of similar or directly competitive goods. This provision was based on Art. XIX. of the GATT. It allowed, however, for wider use of protection against imports than the GATT clause. Both parties to the Agreement could invoke this clause not only when imports caused serious injury to domestic producers but also when such imports caused or threatened to cause “... serious disturbances in any sector of the economy or difficulties which could bring about serious deterioration in the economic situation of a region”.
- Clause on protection against disruptions of agricultural products⁵. Protective measures with respect to agricultural goods which were subject to concessions under the EA could be introduced if imports of such goods resulted in serious disturbances to the markets of the other party. In this case, contrary to the general clause, a causal relationship between liberalisation and injury to domestic producers had to be established.

⁴ Art. 30. of the Europe Agreement signed by Poland. The numbering of the Articles may vary according to the Agreements, the wording, however was similar in all EAs.

⁵ The text reads that “if, given the particular sensitivity of agricultural markets, imports of products originating in one Party, which are the subject of concessions (...) causes serious disturbances to the market in the other Party, both Parties shall enter into consultations immediately to find appropriate solution. Pending such solution, the party concerned may take the measures it deems necessary.”

- Anti-dumping measures clause. It allowed either party to counteract dumping. In order to qualify for anti-dumping measures interested companies had to submit sufficient evidence concerning the existence of dumping and material injury or a potential injury to their already established industries through the effects of unfair competition.
- Clause on protection against shortages or a direct threat of shortages in the domestic market caused by excessive export or re-export of certain goods to a country outside the scope of the countries covered by EAs. This allowed for the imposition of restrictions on exports in cases where there is a serious shortage, or threat thereof, of a product essential to the exporting country.
- Clause on protection against balance of payments disturbances provided for the possibility of introducing import restrictions in order to remedy the balance of payments. However, any restrictive measures could not be applied to transfers related to investment, in particular to the repatriation of the amount invested or re-invested and of any kind of revenues from the investment.
- Clause permitting the introduction of bans and restrictions under GATT rules, justified for instance, on grounds of public morality, public security, historic values etc.
- Clause allowing to resort to extraordinary measures. The aim was to prevent the disclosure of information vital for fundamental security interests and to maintain public security in times of international tension which might threaten peace. This clause allowed parties also to extraordinary measures relating to the production of, or trade in, arms, munitions or war materials, provided that such measures do not impair the conditions of competition in respect of products not intended for military purposes.

There were also a few clauses specific for CEECs which could be used only by those countries (for a limited period of time) as weaker partners. The first two clauses – out of those mentioned below – could be applied to trade in goods and the third one to trade in establishment of new undertakings.

- (a) So called restructuring clause allowing associated countries to apply increased import duties to protect infant industries (i.e.

- new industries with a potential for development) or certain sectors undergoing restructuring or facing serious economic and social difficulties (in particular – a high unemployment or a risk thereof);
- (b) Clause on balance of payments restrictions, which permitted CEECs, in exceptional circumstances, to apply exchange restrictions connected with the granting or taking up of short- and medium-term credits (restrictions should be applied in a non-discriminatory manner).
 - (c) Clause relating to establishment of companies. The clause provided for the possibility to introduce temporary restrictions in some sectors against the establishment of Community companies and nationals, if certain industries (i) underwent restructuring, (ii) faced serious difficulties including social ones, (iii) faced a serious risk of drastic reduction of the total market share held by CEECs' companies or nationals in a given sector or industry in their countries, (iv) were newly emerging industries in associated countries.

In all of the above mentioned cases, the increased protection could only be applied for a limited, previously defined period.

Another specific provision was included in the article on competition and state aid. It stated that any public aid, which distorted or threatened to distort competition by favouring certain undertakings, was incompatible with proper functioning of the Agreement. But the “Parties recognise that during the period of five years after the entry into the force of the Agreement, any public aid granted by CEECs shall be assessed taking into account the fact that they shall be regarded as an area identical to those areas of the Community described in Article 92(3) of the Treaty establishing EEC”, i.e. as a region in which the standard of living is low or the level of unemployment is high.

Rules of origin

The rules of origin constituted an important shortcoming of the EAs. These rules in the EAs were at the beginning quite restrictive as they generally required at least 60% of local (including all CEF-TA countries) or EC content for imported goods to receive pref-

erential tariff treatment. Such requirements not only directly limited growth of imports from third countries but also had a negative impact critical for the economic growth and restructuring of their economies. The restrictive effects of the rules of origin were evident in the case of broad cooperation with EFTA member states, originally excluded from the cumulation. During the talks on association the cumulation of origin with EFTA countries was an important request of Hungary (especially taking into account the traditional trade with Austria, non-EU member at that time). In the early 1990s it was far more important for Hungary than the cumulation with other Visegrád countries. Nevertheless, the EC categorically refused it, of course, this problem later was eliminated with Austria's EU membership. The rules of origin also restricted inflow of FDI from outside the EU into the region. A few years later, the EU decided for diagonal cumulation of rules of origin, extending "local" content to include all free trade agreements with all European free trade partners.

Approximation of laws

Approximation of the Central and Eastern European countries' laws to the EC *acquis communautaire* was recognised as a major precondition for their economic integration in the Community. The approximation of laws covered in particular the following areas: customs law, company law, banking law, company accounts and taxes, intellectual property, protection of workers at the workplace, financial services, rules on competition, protection of health and life of humans, animals and plants, consumer protection, indirect taxation, technical rules and standards, transport and the environment.

In several areas legal adjustment of laws to the EU laws was compulsory. These areas included first of all: public procurement, competition laws, trade procedures (as these were part of EC uniform commercial policy).

Let us say something more about competition rules. The Europe Agreements prescribed the (immediate or gradual) application of the Community competition legislation. This was a deeply integrative element of the EAs. Rules prohibiting the restriction and

distortion of competition and the abuse of a dominant position generally were in line with the CEE countries' emerging market economy type competition legislation governing the behaviour of companies. On the other part, the adaptation of the regulations of public (state) aid was much more problematic, at least for Hungary. It was possible to take over these rules only step-by-step as due to technical reasons, secondary legislation could have been incorporated in the domestic legislation only gradually. On the other hand, renouncing state aid immediately risked to cause serious problems in the short run for Hungary, a country that just had entered the period of modernisation and restructuring. The problem was finally resolved as a result of the negotiations on membership.

By the legal harmonisation the EA created a new institutional framework for integrating the CEECs into the EU, speeding up the process of creation of modern laws, adjusted to market economy conditions.

Movement of labour

This was one of the weakest points resulting from the Europe Agreements. During the negotiations, CEECs negotiators requested the free movement of labour. The motivation behind this request (in the case of Hungary) was not to find a solution for the domestic employment problems, but the acquisition of the West-European industrial culture. The EAs offered, however, only very limited access to the EC market for workers from CEECs. This took place in form of self-employment (the right of citizens of CEECs to undertake a job in the EC without a work permit, but only job on their own and not to look for a job in EC firms). Moreover, national treatment (treatment not less favourable than that accorded to domestic workers) was offered to persons already legally employed or engaging in business on a self-employed basis in the EC. In fact it was legal confirmation of the existing right, which was especially important for Poland, to a lesser extent to the other countries, because of a great number of Polish citizens already being employed in the EC and also because of the lower migration potential of other V4 countries' workers. The EAs declared that the parties mutually guaranteed the social benefits and stability

of pensions to which their citizens were entitled. Also, key personnel from CEECs could be employed by CEECs companies operating in the EC without any restrictions on the part of the EC countries. Provisions on key personnel also applied to EC nationals working in CEECs.

Right of establishment and supply of services

The main instrument of eliminating restrictions on establishment of companies was national treatment, i.e. treatment of foreign companies and nationals no less favourable than that accord to their own companies and nationals. On the day of entry into force of the EA, each member state of the EC accorded national treatment for the establishment of companies from CEECs. Some sectors were however excluded from national treatment (e.g. purchase of agricultural land, natural resource, air transport services, legal services). CEECs enjoyed in this field the asymmetry of concessions.

In the field of cross border services, as a general rule, the Europe Agreements did not contain substantial steps aiming at liberalising this type of services. The aim was only gradual, asymmetric abolishment of the existing barriers, respecting the level of development in each other's service sector. Practically, no real development took place in this respect till the accession to the EU.

Movement of capital

Regarding movement of capital, CEECs and EC members have committed themselves to ensure full liberalisation of payments in convertible currencies arising out of trade between them, supply of services and movement of workers (on current account balance). Such liberalisation applied only to payments connected with transactions which were liberalised pursuant to the Agreement. From the entry into force of the EAs all parties undertook to ensure free movement of capital relating to direct investment, including liquidation, repatriation and any profit thereof. Also, parties should refrain from introducing new impediments to the movement of capital. As regards investments connected with the estab-

lishment of companies in the partner countries, the freedom of movement of capital was to be ensured by CEECs and EC by a latest stage (i.e. within five years). In the case of serious balance of payments difficulties, parties could adopt temporary restrictive measures (except for on transfers related to investment).

Financial cooperation

The association agreements concluded between the EC and different partners (e.g. Greece, Turkey) in the 1960s and 1970s provided for a defined financial assistance from the part of the Community in the form of financial protocols. The original expectation of the CEECs was to have a similar provision included in the agreements. The EC was not ready to accept the concept of longer term financial protocols. Thus, a big compromise of the Europe Agreements was to establish only the forms and conditions of potential financial assistance and of financial obligations of the EC (first of all continuation of PHARE assistance) without a financial protocol detailed in years or figures.

References

- K. Mizsei and A. Rudka, ed. (1995): *From Association to Accession. The Impact of the Association Agreements on Central Europe's Trade and Integration with the European Union*, ed. by Institute for EastWest Studies, Warsaw, Prague, Budapest, Kosice, New York
- European Commission (1994): "Trade liberalization with Central and Eastern Europe", *European Economy, Supplement A. Recent economic trends*, No 7, July