INEKO

Institute for Economic and Social Reforms

Dušan Zachar (Ed.)

REFORMS IN SLOVAKIA 2003 – 2004

Evaluation of Economic and Social Measures

General Partner

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HESO PROJECT
-
EVALUATION OF ECONOMIC AND SOCIAL MEASURES

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REFORMS IN SLOVAKIA 2003 – 2004
Evaluation of Economic and Social Measures

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Bratislava
July 2004

The Slovak Republic faces the task to secure conditions for a long-term economic growth. A crucial precondition for an efficient implementation of economic measures is the knowledge of the status quo and of the impacts on the economy and the society as a whole to be expected from the relevant measures. Foreign experience with economic policies can only be adopted when adjusted to the conditions of Slovakia's economy, and attention has to be paid to both short-term and long-term prospects of the economic and social development.

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Acknowledgements

HESO Project (Evaluation of Economic and Social Measures) brings experts' opinions on the economic and social measures to the public. This survey originated thanks to many outstanding personalities who were taking part in quarterly evaluations. All members of the Experts´ Committee (see list on page 89) were doing it without any claim on financial reward. We are very grateful for their participation.

Our acknowledgement belongs also to fellow workers - Marián Matusák and Štefan Kolek who participated in the realisation of the HESO Project during the year 2003.

Eugen Jurzyca

Project Manager

Dušan Zachar

Project Coordinator and Editor of the Publication

Introduction

Non-profit organisations shall spend efforts to make the public familiar with the nature of economic and social processes in the country and abroad, and to eliminate, through economic research and educational activities, hindrances to long-term economic growth of the country. One of the objectives of non-profit organisations should be monitoring of perspective measures/reforms in order to push forward the economic and social transformation, as well as trying to influence public awareness and to increase public acceptance of measures and policies that speed up transformation toward a democratic, transparent political system buttressed by civil society and competitive market economy and lead to life quality improvements from a long-term perspective.

With this in mind, INEKO has launched the HESO (Evaluation of Economic and Social Measures) Project, which creates a platform, where reputable independent economists, analysts, journalists, academics, people from business community, representatives of trade unions, employers´ associations and NGOs express their opinions on quality and importance of different proposed and passed economic and social measures of legislature, executive power, as well as on decisions of public institutions on a quarterly basis. Without the necessity of studying a number of details, Slovak citizens have thus an opportunity to acquire a reliable overview of what economic and social measures and reforms are being prepared and put into practise and what opinion in their respect has been adopted by renowned experts. From the beginning of the HESO Project in April 2000 to the end of 2001, 71 specialists expressed their views upon 174 measures. In 2002 69 experts assessed 100 measures. In the period of 1/2003 – 1/2004, which is subject of this publication, 75 experts evaluated 114 various economic and social measures.

From their standpoints, we can read out, which measures significantly contributed and still contribute to the social and economic development of Slovakia, and which just hindered and hinder this process. Hence, a citizen can make better quality decisions, and more conveniently, on which reform activities he/she wants or does not want to support. The ambition and the major objective of the HESO Project is not to provide a comprehensive and detailed monitoring of the development in individual areas of our society, nor is it the provision of starting points for the action of competent authorities, but we aim at regularly providing our citizens with an opinion of professional community on often discussed, important, innovative, or unprecedented measures of economic or social character affecting the quality of their life. And thus we create better preconditions for political acceptance of structural measures - reforms - bringing forth systemic changes in the Slovak economy and society.

The publication you are holding in your hands maps the results of the HESO Project during the period of 1/2003 – 1/2004 in the Slovak Republic. It liaises with previous 2 publications, which covered results from the beginning of the project in April 2000. In the publication "REFORMS IN SLOVAKIA 2003 – 2004" you can find description and evaluation of selected important and/or interesting economic and social measures/reforms of the period January 2003 – March 2004 (information about all evaluated measures is placed on the HESO Project´s web site: *www.ineko.sk/projekt_heso.htm* (in Slovak only); less information is available on the project´s English web site, too: *http://www.ineko.sk/english/project_heso.htm*).

Methodology

Selecting Measures to Evaluate

Four times a year a list of 20-30 measures, which took place during last three months, is prepared. Everyone can suggest through our web page *(www.ineko.sk/projekt_heso.htm)*, which measure he/she wishes to be evaluated. INEKO makes final selection. Emphasis is laid on measures widely discussed in the public as well as on measures, which are, according to INEKO, rare, innovative and/or important for the economic and social development of the country. Evaluated measures include, among others: acts proposed and passed by the Parliament, measures adopted by the government (acts, regulations, privatisation decisions, strategy documents, policies) or decisions of public institutions (e.g. of the Central Bank, Antitrust Office, Telecommunications Authority or other market regulators). Characteristics (description) of the selected measures are prepared by INEKO. For this purpose INEKO uses information from original materials, documents as well as from media sources.

Evaluation Experts´ Committee

The evaluation Experts´ Committee consists of about 45-50 members for one quarter. The experts come from reputable economic newspapers, banks, consulting companies, business community as well as from academic institutions, trade unions, employers´ associations and think tanks (see list of all members of the Experts´ Committee on page 89). They represent leading or senior management positions in their organisations. The experts do not work in civil service and do not represent any political party. All of the experts attend the project for no reward. The opinions presented in the HESO-project represent solely those of the experts and do not necessarily reflect the views of their employers.

Evaluation Criteria

Experts evaluate all the selected measures in two categories: Quality and Importance for the society and economy. These do not affect each other.

Quality [-3; +3]
Experts evaluate the effect of a selected measure and give it a grade (see the range below). Often, there is a crucial difference between the real effects of a measure and the effects proclaimed by its author or administrator. Therefore, no matter what the measure presents to solve or improve, experts evaluate the impact and the effects they think the measure will bring to life.

Range:

-3	absolute disapproval
-2	moderate disapproval
-1	minor disapproval
0	no effect, status quo
+1	approval despite significant defects of a measure
+2	approval despite minor defects of a measure
+3	absolute approval

Importance for the Society and Economy [%]
Experts express opinion how essential and necessary the selected measure is for the society and economy, for the economic and social development. This category highlights the importance of reforming a given feature of a system in the country. The higher the score, the more important the measure is.

Experts' Comments on Evaluated Measures - Evaluation of the Experts' Committee
Experts are invited to mention the pros and cons of the measures they evaluate. A summary of comments on each evaluated measure sums up the Evaluation of the Experts' Committee.

Ratings

Rating of the Measure
To get the rating of the measure, the average quality grade of the measure is multiplied by a coefficient expressing the average value of the measure importance for the society and economy. Thus, the rating values of the evaluated measures come in range [-300; +300]. According to

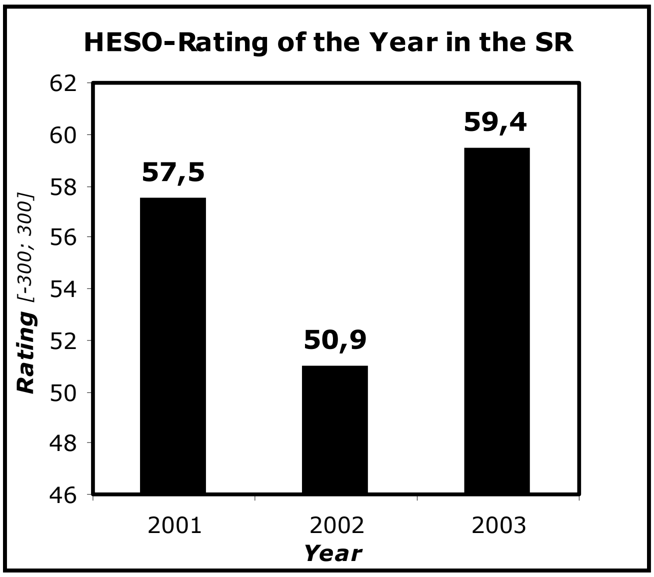
these rating values all measures are ranked in a chart. Rating of the measure indicates the contribution of the evaluated measure to the economic and social development of the country.

Rating of the Quarter [-300; +300]

Only the ratings of measures, which have been implemented or passed by legislative body, executive power or public institutions, are used to complete the rating of the quarter. The rating of the quarter is calculated as an average of all ratings of evaluated measures, which have been passed or adopted in relevant quarter. Often, there might be a time lag between a proposal and a passed measure. If an evaluated measure was drafted or proposed but not yet passed, it will not influence the final rating of the evaluated quarter. It will count only in the quarter in which it is put into effect. The rating of the quarter reflects Experts´ Committee´s opinion on quality and importance of all evaluated measures passed in relevant quarter and indicates the reform atmosphere of the relevant period.

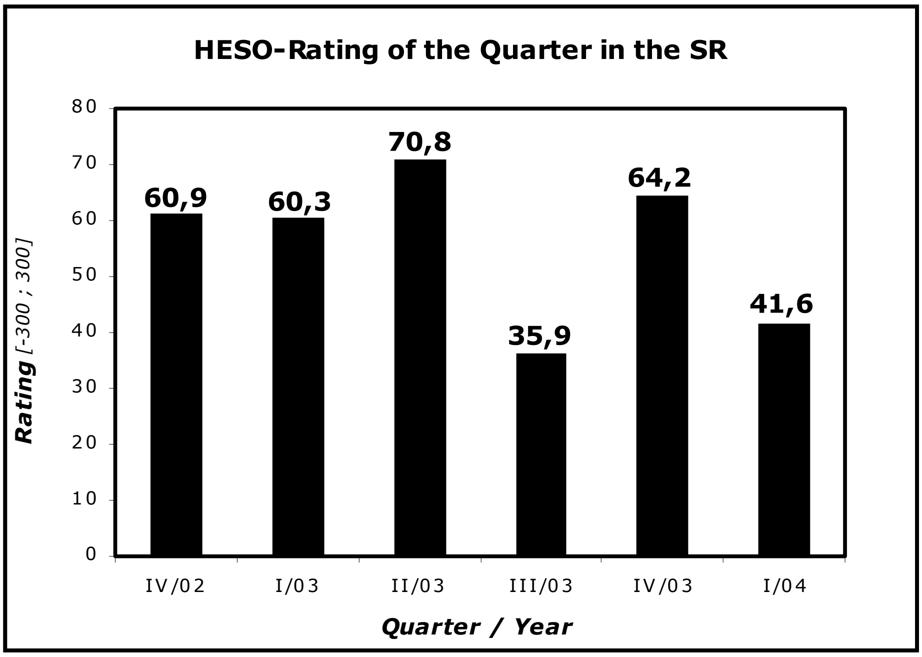
Summary

Following accession of the new Government grouping after the parliament elections in September 2002, and implementation of initial stabilising measures intended primarily to reduce public expenditures, or at least prevent their further rise and, on the other hand, partially increase public budget income (*see HESO 4/2002),* in 2003 a room for launching structural changes – reforms, and consequently meeting obligations ensuing from the relatively ambitious Memorandum of the Slovak Government has been opened. In 2003, the pro-reform commitment of government parties was reflected in the relatively successful adoption of formal rules in respect of the tax reform, pension reform, social benefits reform, labour market reform, business and investment environment improvement measures, and partial implementation of the public administration reform. The main benefit ensuing from adoption of reform measures during the first half of the electoral period is the possibility to rectify any defects of the reforms as they may emerge in the course of their practical application during the second half. However, in the middle of 2004, i.e. during the first half of the Government´s and Parliament´s four-year electoral period we can observe negative signals of what is referred to as political business cycle, and these are even accelerated due to the loss by the government coalition of its majority in Parliament. With approaching regular Parliament elections ministers will encounter increased difficulties in enforcing those reforms where the effect can not be expected to arrive tomorrow, or at least the day after, however, which bring about comprehensive, systematic changes improving life of citizens in a sustainable, though at the beginning unpopular manner. This "natural" phenomenon, inherent in second halves of incumbencies when politicians´ behaviours are driven by their desire for re-election, is combined with another risk factor relating to the ability to pass further reforms and political instability of Parliament. Thus, beside proposing and passing measures that are more favourable for voters (such as payment of the lump sum benefit of SKK 1000 to pensioners in order to compensate the impact of reforms) as the elections approach, reformers will have to provide for an equivalent of the "mandatory tenth", exceeding the usual extent, for deciding members of Parliament and various interest groups. Examples include the compromising judiciary reform and governance of the conflict of interests issue, refusal by Parliament of university study charges, and in the future a hazard of too extensive concessions in respect of the health care reform, or the fiscal decentralisation. However, everything can be quite different eventually...



Note: Parliamentary Elections – September 2002

The Rating of the Year / the Rating of the Quarter *is an average of all ratings of evaluated measures, which are passed/adopted in relevant year/quarter. It reflects Experts´ Committee´s opinion on quality and importance of all evaluated measures passed in relevant year/quarter and indicates the reform atmosphere of the given period.*



Note: Quarter Ratings since the Parliamentary Elections of September 2002

In the **public finance** area we can observe gradual improvements in the use of public funds. The budgetary public finance deficit accounted for 3.6% of GDP in 2003, which was the least among Visegrad countries. However, for instance Baltic countries or Slovenia achieved a 50% lower deficit and Estonia even a public finance surplus. Various analysts suggest that given its current high economic growth dynamics, Slovakia should have an ambition to achieve lower public finance deficits. Many experts view 2004 State Budget as the best one over recent years in terms of its systemic character. They appreciate transparency of the budget as it treats both income and expense more realistically, and has a potential to force ministries to manage with limited resources. Another positive feature is the program budgeting, i.e. project-oriented budgeting process, though it has not been implemented to a sufficient extent yet, and the commitment to multiple-year programming and budgeting. The current national budget presents a step ahead towards rationalisation of government expenditures, however, it calls for a more significant change in the public expenditure structure. A too large portion of total expenditures remains re-allocated to interventions in market processes, while multiple budget positions are driven rather by political interests than the economic rationale. As an example, the multimillion subsidies to agricultural entities of the railway company can be highlighted. Thus, the fact that taxpayers will have to subsidise entities that failed to complete rationalisation with implications to their low competitiveness, inefficient economy, and excessive over-employment represents a rather negative feature. On the other hand, the Government´s aid granted to the public Slovak Television (STV), aiming at eliminating its indebtedness and covering salary claims of the dismissed 1200 employees, can be evaluated with a somewhat greater comprehension as the new Slovak Television company's director has assumed, and fulfils via the courageous Recovery Programme a commitment to stop generation by STV of further debts, and manage without further national budget subsidies. The current Government has gradually abandoned the policy of providing state guarantees, which is laudable, however, this form of state aid was too quickly replaced by offering various investment incentives, primarily to major foreign investors. The period from 1/2003 to 1/2004 was characterised by extensive investment incentives, which to a major extent related to the two historically largest foreign investments of automotive companies, PSA Peugeot Citroën in Trnava and Hyundai/Kia Motors at Žilina. A long criticised – not only by Slovak analysts – item is general government consumption expenditures accounting for almost one quarter of all national budget expenses. Despite the partially completed public administration reform, the number of public sector´s employees remains to be excessive. A positive feature is adoption by the Government of the Strategy for Public Finance Management Reform, and its commitment to enforcing hard budget constraints across the entire public sector.

The general **tax reform** can be evaluated as a benefit compared to the former situation. A majority of the changes should bring positive, dynamic effects on Slovak economy in upcoming years. Experts have appreciated the shift of focus from direct taxes to indirect taxes. The more equitable, transparent and streamlined tax system should have a positive influence on business and investment activities, and motivate participants in economic processes to behave in line with the saying "working pays, tax evasions don´t." The new Income Tax Act introducing flat tax of 19% is clearly the most appreciated component of the tax reform. Professional public perceives it as one of the most important and most pro-reform Government´s actions over recent years. The relatively low flat tax and streamlined tax system, free of excessive exemptions, tax relieves, and complicated statutory provisions will revitalise economy and facilitate healthy economic growth, stimulate business activities and both domestic and foreign investments, and the labour market; and they will divert taxable entities from tax evasions. Income Tax Act has increased international competitiveness of the country. It cancelled the immoral inheritance and gift taxes leading to multiple taxation, as well as taxation of dividends; this represents application of the single direct taxation principle. Within the frame of the tax reform, projected by the Ministry of Finance in a fiscally-neutral manner, after reduction of the gap between value added tax rates from 10% and 23% to 14% and 20% with effect as of 2003, the two different rates were cancelled as of beginning 2004, and a uniform VAT rate of 19% has been introduced. This should contribute to making the entire tax system more transparent, and tax collections more simple and limit tax evasion opportunities. All goods and services were made "equal" and, as a result, motivation of various interest groups to transferring selected commodities and services under the lower VAT rate was eliminated. When implementing the tax reform, Ministry of Finance withdrew from certain principles included in the original concept. The tax assignment option (allocation of 2% of income tax to non-profit organisations for public benefit purposes) has been retained; later on, due to inaccurate estimation of VAT income and unfavourable performance of the national budget, excise taxes were increased with effect as of an earlier, unplanned date, accompanied by tax relieves for wine and minor breweries. Furthermore, the Ministry agreed not to cancel property transfer tax and road tax yet, and retain the more advantageous tax treatment of savings held in supplementary private pension insurance companies. The tax reform and primarily the flat tax also contributed to a significant improvement of the international image of Slovakia. A positive result is that after introduction of the flat tax rate of 19% and extension of tax deductible items no tax-payer will pay a higher income tax than prior to the reform. The tax rate should gradually decline over time, which would bring Slovakia to even more advanced position within the region. The tax rate declination should not be accompanied by increases in indirect taxes. From a static perspective it seems that what a tax-payer saves on income tax they spend on a higher VAT, or higher excise taxes. Major critic´s objections related to the tax reform concerned the level of tax rates and the initial increase in tax encumbrance for a major portion of population, particularly the middle stratum which will carry most of the reform´s burden. They proposed reduction in the VAT and flat income tax rates; this should lead to cutting national budget expenses, which is desirable anyway. Professional public also called for bringing excise tax rates in Slovakia back to minimum limit levels set by the European Union, and not exceeding them.

Recently, both business undertakers and reputable international institutions such as World Bank, OECD, or World Economic Forum perceive the **business and investment environment** in Slovakia as increasingly improving. This is to a large extent due to the tax reform and the labour market reform, both facilitating more expedite creation of new jobs, improvement of competitiveness of businesses and the national economy as a whole, and achievement of higher sustainable economic growth rates, with eventual effect on enhanced standard of living of Slovak population. The business and investment developments are also contributed to by improving access to funds, which is primarily due to the ongoing reduction of interest rates, and availability of an extended range of loan products. One of key factors driving attractiveness of the business and investment environment is the extent of various bureaucratic barriers impeding business activities whether before or after entering, or when leaving a business. For instance, measures to improve the efficiency of the Companies Register making the registration process significantly faster and easier, or availability of the Real Estate Register on Internet clearly contributed to reducing these barriers. However, more significant improvement of the business and investment environment in Slovakia is impeded by chronic problems; these are often highlighted by business undertakers in various surveys as the major barriers to business activities, including ambiguous and frequently changed legislation, bureaucracy and corruption in dealing with authorities, and particularly poor functionality of judiciary and low enforceability of law. The ability to flexibly exercise one´s contractual rights, and thereby ensure sufficient protection of private ownership is the alpha and omega of a sustainable and sound economic growth. One of preconditions for the business development in regions of Slovakia is a good transport infrastructure. Also the current Government continues implementation of the motorway and expressway construction strategy, however, plans in respect of routing and funding road communications keep giving rise to many questions.

A positive feature is that Minister of Justice is aware of the inefficient **judiciary**, corruption, and poor enforceability of law, and proposes and adopts measures to address these issues. He exercises the power to initiate disciplinary proceedings against judges more often. In May 2004, the first judge in Slovakia was condemned by a court of first instance of corruption. The Minister would probably wish the progress in these problematic areas to be more expedite. The question is what he as Minister with the given powers is able to influence, and where his influence on the independent judiciary ends. He surely may initiate changes aiming at regulating the legislative framework for areas falling within the ambit of the Ministry of Justice, and this is gradually done. New principles have been implemented in Slovak law (zero-tolerance principle to corruption and other serious crime offences in legal professions, continuing market opening, commitment to deregulation of legal professions, duty to actively disclose judge´s property statements on Internet), measures to improve efficiency of judiciary (the Judicial Management Project – electronic registry for all courts, higher judicial officials, personal liability for damages paid by the state for losses consequential upon delayed proceedings caused by judges); a new, optimised organisation of courts, new institutes (institute of co-operating, so-called key witnesses and probation and mediation officers), and authorities (Special Prosecutor Office and Special Court to Fight Corruption and Organised Crime), alternative methods of off-court dispute settlement (mediation), and more stringent sentences (so-called "Three-Strikes-and-Out" Principle, unconditional life imprisonment (without parole), asperation principle).

Social policy was characterised by an extensive reform of the entire social system. Parliament approved Government bills launching the long-expected, and due to non-sustainability of the system inevitable pension reform. Social Insurance Act changed the Pay-As-You-Go Pension Scheme to a system with a stronger benefits-to-contribution tie where the individual merit reflects in the pension benefit amount to a larger extent than previously (i.e. higher amount of contributions paid = higher pension). The retirement age was raised to 62 years, and statutory automatic pension adjustments in accordance with the average nominal monthly wage of employees in economy of the SR and inflation were introduced. Old-Age Pension Savings Act established the Fully-funded Pension Scheme as an equally strong second – so-called capitalisation – pillar where people will keep savings for their future pensions with private pension funds, with a possibility to include the sum saved into inheritance. Families with children will receive a flat amount of child allowance of SKK 500 per child and a tax bonus of SKK 400 per child, reflecting the negative tax principle. Thus, employed parents will receive higher benefits from the state than previously. The approach to providing other social benefits was converted to a more targeted one. More stringent requirements in respect of registration of unemployed were introduced with a view to combating illegal employment practices. New active labour market policy instruments were introduced, including various incentive and activating allowances. The Ministry of Labour, Social Affairs and Family has promptly responded to commotions among the Roma in East Slovakia triggered by the stricter social policy by changing some benefits, modifying the manner of paying out social benefits, and extending activating job opportunities (minor, primarily public jobs); the Ministry of Interior initiated fight against usury. Business undertakers welcome adoption of the new Labour Code rectifying the most striking deformations acquired through the re-codification executed during the previous electoral period, and shifting Labour Code to some extent towards market principles in terms of employment-related legal relationships. Hiring and dismissing labour force is more flexible. Labour law must be flexible and variable so that parties to employment contracts are able of responding to current market situations and behaving in a rational and economically reasonable manner. However, the process of amending Labour Code should continue with a view to greater liberalisation and elimination of unnecessary limitations in relationships between employers and employees, as a liberal, and therefore flexible labour market contributes to increasing employment. Success in the form of a significant decrease in sickness absences resulted from the measure introducing the employers' obligation to pay sickness insurance benefits in first 10 days of employee's temporary sickness leave.

The adopted stabilising measures such as introduction of flat payments for health care related services (co-payments for outpatient and inpatient visits, for ambulance transport and for drug prescriptions) and a new drug policy in the **health care sector** have slowed down the debt growth by almost a half to SKK 4.8 bn in 2003. The excessive demand for health care was reduced: excessive visits decreased, and the growth of drug expenditures was decelerated while, according to data of the Ministry of Health, availability of health care services has not been impaired. The rate of corruption perception declined. Implementation of an innovative method of health care sector´s debt settlement by the state-owned joint stock company Veriteľ (Creditor), which represents an advance compared to previous attempts for "eliminating indebtedness" of health care institutions, though accompanied by various ambivalent opinions, should be followed by systematic measures and the essence of the health care reform in 2004. A package of 6 reforming laws intended to determine inter alia the scope of health care covered by public health insurance, enhance competition and set forth rules for new sector´s players, transform health insurance companies to joint stock companies, and establish Health Care Surveillance Authority should be brought to Parliament for approval in autumn 2004. This concept should be followed by network measures (such as definition of health care professions, functions of professional chambers, transfer of powers and responsibilities to hospital managements, introduction of a differentiated system of remuneration).

A new law in respect of regional **educational systems** (primary schools, secondary schools and school institutions) was successfully adopted, introducing multiple reform features into the school funding system. The Pupil-Based Budget, i.e. application of the "money follows pupils" principle should ensure more transparent use of funds, drive higher efficiency of regional educational systems, and ccntribute to increased competition among entities operating schools. It is essential that the new system should replace the former system which has been recently characterised as a practice of ad-hoc covering unfunded operating costs according to a current national budget situation. Failure of the Ministry of Education (Parliament?) lies in its unsuccessful attempts to adopt university study fees.

After decentralisation of a majority of powers by their transfer from state administration to local and regional self-governments within the frame of the **public administration** reform, the local state administration was re-arranged, and as a result a network of Offices of Specialised Local State Administration were established, intended to facilitate a more efficient and economically reasonable performance of authorities, and bring their services closer to citizens. Politically difficult was the process of eliminating District State Administration Offices, and establishing less staffed Local State Administration Offices and their detached offices. Efficient performance of public administration in terms of better accessibility to citizens and lower cost levels compared to previous arrangements is considered by experts the most important objective of the public administration reform. However, many critics claim that the new system lacks any guarantees for reduced bureaucracy, staff and expenses. They perceive the reform as a change for the change itself, accommodating officers rather than citizens for whom the new organisation of local state administration is not quite transparent compared to the previous situation, and who therefore do not benefit from the change. In the near future steps towards fiscal decentralisation will have to be taken since without them the public administration reform can not be deemed completed; moreover, it is desirable to consider change of the territorial and administrative division of Slovakia so that administrative units correspond to natural regions. As regards the system of remuneration of civil and public servants, some changes intended to tie remuneration to quality of work were implemented. Fixed rates in the civil service were eliminated, i.e. now salaries paid to public servants do not depend on years worked. An increasingly larger portion of public servants will not receive salaries pursuant to fixed table rates, but salaries will be subject to agreements based on standard employment contracts made under Labour Code.

The Slovak Republic (SR) achieved significant **foreign policy** successes related to the integration. Ratification of access treaties, and the integration with the North Atlantic Treaty Organisation (NATO) and the European Union (EU) itself mean conclusion of one chapter of Slovakia´s modern history. With the NATO membership Slovakia gained prospects of a stable economic and social development, not to mention assurance of stability of the state´s security as a factor of key importance for the future. Visible economic implications of the membership will reflect in increased confidence in the country on the part of foreign investors due to safe allocation of their resources, contributing to investment attractiveness of Slovakia. The integration of the SR with the EU is perceived by majority of professional public as a positive step of historical significance from which all generations and population strata will benefit over a long-time horizon. The key aspect will be, however, how soon the population will understand that the integration with the EU is not a target able to bring solutions as such, but means a way to enhanced welfare. Negotiations did not result in favourable terms for Slovakia in all areas (the most striking issue is the transition period in respect of free migration of persons), however, without the integration Slovakia would be unable of influencing the EU´s policy towards higher competitiveness of the European area. A very important factor bearing on success of the EU project will be whether the new member states bring new wind, or at least gust of sound views promoting ideas of market economy free of excessive regulation, redistribution and policy harmonisation, as well as free migration of goods, services, capital and labour in realtion to third-party countries.

EVALUATION OF SELECTED MEASURES

(Division of the measures according to subject related topics. Most of the measures influence directly or indirectly more than one field at the same time, they have intersectoral character. Evaluated measures are arranged into several groups, according to the field, which they influence mostly and rather directly.)

Public Finance

Strategy for Public Finance Management Reform (More Transparency, Hard Budget Constraints, Program Budgeting, Mid-Term Macroeconomic Framework)

During its meeting on 23 April 2003, the Cabinet approved the Strategy for Public Finance Management Reform – an initiative of the Ministry of Finance (MF). The purpose of the Reform is, consistent with other changes to the public finance revenues and expenditure, to maintain permanently sustainable development of the public finance and to meet the criteria for real, as well as nominal, convergence, which will allow Slovakia to join the Economic Monetary Union (EMU) within a medium term. After the Reform has been put into practise, Slovakia should have a modern public finance management system, which should be cost-effective for taxpayers' and transparent for citizens. The Strategy has distinguished three areas of aims and tasks: reinforcing transparency of public finance, strengthening strategic planning in allocation of resources and in transition to result-oriented budgeting, and creating a system that would help develop a stable medium-term framework of the public finance. The strategy stems from international experience that is summarised and generalised in the documents prepared by the OECD, IMF, EU institutions and others as well as from a contemporary level of experience in managing public finance in Slovakia. After the implementation of the Reform, Slovakia will have, in the MF's opinion, a modern public finance management system that will establish links between strategic political priorities and the economy's possibilities in the medium term. It will also allow translating political priorities into expenditure priorities and, eventually, produce a public finance budget. This will subsequently establish tighter links between the individual constituents of the public budget such that the same transparency rules and the same hard budget constraints be valid at all levels and in all parts of the public administration. An important element is the strengthening of internal and external supervision ex post *as well as* ex ante*.*

The main changes associated with the reform implementation are forecasted to have been carried out by mid 2006, when a respective legislative framework as well as institutional capacities, including human resources, for the new public finance management system should have been created. However, tuning the system will be, in the Ministry's opinion, a long-term process (as it is in other countries reforming their public finance). The comprehensive reform of the public finance includes reforms of public expenditure (healthcare, education, pension system), public revenues (tax reform) and public finance management. The reform should create a basis for a resulting decrease in citizens' tax and social security burden. The document approved has defined the strategy in the last mentioned area, i.e. in public finance management. The strategy stems from the commitment expressed by the Government in its Memorandum to decrease the public finance deficit to 3% of the GDP by the end of their current mandate. Predictable and macroeconomically sustainable development of the public finance gives a firm basis for a successful macroeconomic stability. In order to achieve this position, we need a Mid-Term Macroeconomic Framework that would be well-discussed and creditworthy and will contain an analysis of potential fiscal risks.

The strategy argues that recent changes resulted from external pressures associated with the accession negotiations rather than from the expression of internal necessity to improve the public finance management. The changes made to individual areas were isolated, without having links between each other, and had a rather technical and methodical character without creating an institutional framework - personal, organisational and information capacities. The changes were rather initiated by people's enthusiasm than by a systematic approach. The public finance management reform is a long-term process. Therefore, the Strategy's aim is to identify individual elements that need to be reformed, their relations, and their links in terms of time and contents. Its aims also include the definition of priorities and a time schedule for the implementation of individual reform steps, including the identification of the areas with the strongest need for strengthening the institutional framework. The MF is concerned that in the absence of set priorities, a time schedule, and continuing changes in the public finance management system, and without linking these changes within a consistent reform, the Government and the Parliament will continue being affected by permanent fiscal distress and will be faced with the risk of unexpected events that will need to be addressed immediately. Hence, without being aware of medium- and *long-term risks and impacts of the measures adopted, the Government and the Parliament will have to make only short-term (annual) decisions.*

Transparency of public finance*. The aim of the Amendment to the Act on Budgetary Rules is to more strictly determine the entities using public finance. Having implemented the Amendment, the particularly problematic area remaining will be the register of semi-budgetary organisations administered by the Statistical Office of the Slovak Republic, since there are significant shifts occurring at present in the structure of these organisations particularly as a consequence of the transfer of authorities to local self-governing authorities. Despite this, it will be necessary to make an inventory and to develop a system for updating the register of semi-budgetary organisations such that all changes are keyed in without delay. It is important to make these changes not only for the correct definition of the public administration, but also for proper functioning of the State Treasury System, which provides services to semi-budgetary organisations. One of the obligations ensuing from Slovakia's membership in the EU is to report the fiscal position of the general government in accordance with the ESA 95 methodology. It will therefore be necessary to project the existing methodology into the State Treasury System that is under preparation, which will allow more precise reporting and will decrease its administrative workload. After several years of preparations, in 2003 the project and legislative framework of the State Treasury System and the State Debt Management Agency have reached the implementation phase. The Strategy argues that the costs incurred on both projects so far, as well as the importance of both institutions in the public finance management system, make it clear that it is necessary to place emphasis on precision and consistency rather than on time. It is necessary to ensure that the State Treasury System will not become a budgeting tool only, but also a source of information that responds to the Government's analytical needs. In this connection, it will also be necessary to define the relations between the State Treasury System, the State Debt Management Agency and the Ministry of Finance in terms of powers, methodologies, procedures and legislation. Eventually, the Ministry should retain the powers regarding the formulation of the policies, intentions and aims, whereas the execution should be fully under the authority of the State Treasury and the Agency. It will however be necessary to make a decision whether the State Treasury and the State Debt Management Agency will, in line with the initial intention, remain two independent bodies of the state administration, being financed from the state budget, or be transformed into an independent organisation established based on a special act.*

The Strategy also deems it necessary to, consistent with the public administration decentralisation, comprehensively deal with ***the relation of the central Government and the state budget to municipality budgets and Self-Governing Regions****, which should also address the decision regarding the level of decentralisation of revenues (redistribution vs. own revenues) and of expenditure (restricted-use expenditure vs. freedom in the application of regional policies according to political priorities at this level). Although the issue of self-governments' deficits and debts has partly been addressed by existing legislation (the Act on Budgetary Rules), it will be necessary, as a part of the fiscal decentralisation, to further strengthen the application of hard budget constraints at the level of self-government such that no uncontrolled deficits and debts may arise and that no outside-the-budget or quasi-fiscal activities may exist.*

The necessity for ***hard budget constraints*** *is also actual in connection with the social security funds (Social Insurance Agency, health insurance companies) and with other public institutions. While the issue of uncontrolled deficits of the social security funds have partly been dealt with (the funds are obliged to submit their draft budgets to the Ministry of Finance and these draft budgets must further be approved, together with the State Budget Act, by the Parliament), this is not the case of public institutions. In the MF's opinion, the ultimate aim of the reform will be to ensure that the main parameters that determine the sustainability of the state budget – deficit indicator (ESA 95) and public debt indicator- are fully controlled by the National Council (Parliament) and that the transparency and permanent public finance sustainability principles are equally applied to all public administration constituents.*

The space for performing the ***outside-the-budget and quasi-fiscal activities*** *has been substantially reduced in the Cabinet's previous functional term by decreasing the number of state funds, by their inclusion in the budget (see HESO 4/2000, 4/2001) and particularly by the privatisation of the banking sector and major industries. The Strategy lists the current risks in this area, which are:*

- *the Railway Company and the Railways of the Slovak Republic, which both need to be financially consolidated; it will be necessary to implement measures that will stop these two companies from generating further debts;*
- *the Slovak Electricity Company, where it is necessary to deal with the existing state guarantees and with frozen investment;*
- *health insurance system (or health sector as such), where the reform must be projected such that the new system does not generate future debts; in the health insurance system, it is also necessary to quantify existing debts and define the method of how they will be written off;*

- *state guarantees granted, where it is necessary to make an inventory (including not only state guarantees granted by the Government, but also by the National Property Fund, various other funds, and guarantees provided to the Slovak Consolidation Agency); it will also be necessary to evaluate the return on the realised state guarantees, assess the risks of unrealised state guarantees and increase efficiency of the debt collection system of realised state guarantees.*

Although, in the previous election period, adopting the Act on State Debt and State Loan Guarantees (see HESO 2/2002) substantially limited the space for granting state guarantees, the Strategy deems it important to develop and implement such a system that will, in the future, make it impossible to grant guarantees to projects other than those co-financed from abroad and with guaranteed return.

At the time when the Strategy was being prepared, the State Budget comprised 49 Chapters, half of which totalled to only 3% of the budget. The structure was, in the opinion of the document's drafters, inefficient because it increased the administrative costs. Furthermore, and most significantly, the structure did not provide a sufficient opportunity to half of the Chapters to present their aims and intentions in the budget preparation process, since they were not directly represented in the Cabinet's meetings. As a result, omissions caused by inadequate communication between the Chapter administrators and the Cabinet were only corrected in the sessions of the National Council, or of its committees. Hence, it was necessary to ensure that each Chapter of the State Budget was represented in the Cabinet's meetings discussing the State Budget. The MF will try and push through the ***decrease of Budgetary Chapters****.*

The Strategy also states that one of the main trends in the budgeting modernisation in developed countries is a transition to top-down budgeting, stemming from strategic aims and current Government's priorities. The ultimate aim is to create such a planning and public expenditure control system that will ensure the highest possible effects for taxpayers. The tool to strengthen strategic planning and management is ***Programme Budgeting****. A programme (target-oriented) budget combines the Government's priorities with budgeted expenditure, shows data that help increase efficiency and places emphasis on the purpose for which the funds are used. Introducing a relation between the Government's tasks and activities as well as the state's priorities and available resources results in a system aimed at the target (efficiency in expending budgetary funds).*

The aim of the Programme Budgeting is to:

- *improve the budgeting and decision-making process by clarifying the purposefulness of expending public resources in connection with expected results (effects) and by creating prerequisites for measuring efficiency of the resources used, i.e. the transformation from financing capacities to financing services and assets;*
- *increase the budgetary chapters administrators' responsibility in purposeful and efficient use of funds during the preparation, implementation and supervision of a budget;*
- *prepare a budgetary system that would be transparent for the public and that would make it possible to assess its purpose and final effect of the use of public funds.*

The Programme Budgeting was used for the first time in a testing project for the preparation of four chapters of the 2002 budget. In 2003 the number of chapters was increased to 9 and, in 2004, all Budgetary Chapters are to be prepared by means of programme structures.

The Strategy makers concluded that the approach to the preparing the programme structures and to setting intentions and targets of individual programmes has remained formal and is regarded as an additional burden on the staff at ministries' Budget Divisions. Mainly, the implementation took place at the level of Budget Divisions without any major involvement of superiors from specialised divisions and particularly without involvement of the ministerial political leadership. Nevertheless, the Program Budgeting is becoming an important instrument for achieving a number of Government aims in the area of budget preparation and implementation (support to a managerial approach to the management of individual Budget Chapters, reinforcement of competition for resources in the budget preparation phase, programme structure allowing the use of means from the European Funds within a single budget structure, which is a starting point for the preparation of a multiple-year budget and hence for interconnecting an annual budget with a mid-term macroeconomic framework through a multiple-year budget). The Ministry has also considered using the programme structure as the main vehicle for allocating budget resources as early as 2005. The current experience shows that full implementation of the Programme Budgeting, and hence the achievement of the aforementioned aims, will not be possible without directly involving the political leaderships at the ministries, as this is the only level where it is possible to translate the Memorandum of the Government as well as the acts and the ministries' priorities into identifiable results that will illustrate professionalism and efficiency of the public sector. The Programme Budgeting will be able to achieve its aim only if it becomes a tool for the implementation of the priorities of the Government as a whole and of the political leadership of the ministries. Showing the results of the use of taxpayers' means, the budget's programme structure, also encompasses an important political dimension. It is a suitable instrument for the communication between the Government and the public and it also increases transparency in the *relation Government - general public. The Ministry of Finance intends to allow transfers of funds within individual programmes, while only the limits regarding the capital and current expenditure (including wages and salaries for the whole Chapter) will remain compulsory. Furthermore, it will be possible to rollover unused funds within the programme to the following years. A part of the expected budget resources should have been allocated in the 2004 budget preparation phase through the limits set for individual chapters. Their actual allocation was expected to have been discussed and approved by the Cabinet, based on the priorities and quality of other projects and programmes, in the second phase of the budget preparation in August and September.*

*The task of the **Mid-Term Macroeconomic Framework** is to synchronise the economic policy priorities (and associated public budget expenditure priorities) with limitations posed by macroeconomic development reflected in basic parameters of the fiscal framework. Hence, the Mid-Term Macroeconomic Framework sets the Government's mid-term fiscal targets in key indicators such as, e.g., total revenues, expenditure, deficit, debt and expenses incurred on debts (including the identification and quantification of potential risks). The Mid-Term Macroeconomic Framework should also formulate mid-term targets on the expense side, consistent with the targets in revenues and deficit. The expenses should be further broken down to liabilities arising from the existing and future activities of the Government. The task of the Mid-Term Macroeconomic Framework is to ensure that the Government and the Parliament avoid permanent fiscal distress and that the individual decisions taken by the Government, as well as annual budgets, do not jeopardize the sustainability of the country's macroeconomic development. Additionally, it should identify current decisions' future fiscal impacts. The MF believes that a stable and credible mid-term macroeconomic framework is pivotal for achieving fiscal stabilisation, for maintaining macroeconomic stability, for maintaining an optimum mix of monetary and fiscal policy, and for transitioning from a passive to active anti-cyclical macroeconomic policy. Additionally, it will help stabilise the business environment by creating a transparent basis for making mid-term predictions. In connection with the accession process, the Ministry of Finance has thus far been preparing the so-called Pre-accession Economic Programme, which provided a basis for the Mid-term Financial Forecast, a document submitted to the Parliament as an annex to the draft Act on the State Budget. However, the Pre-accession Economic Programme did not become a topic of wider political discussions, but was rather regarded as a technical instrument. The membership in the EU will, however, impose on us a duty to annually update the so-called Convergence Programme. It is expected to set convergence criteria (for the entry in the EMU) in a mid-term time horizon and will contain a consistent idea about the method to achieve them. The Strategy argues that an insufficiently elaborated system of formulating strategic aims at the political level is the first weak point of the Mid-term Macroeconomic Framework. It also admits that, although the MF has its own methodological tools for making macroeconomic prognosis, they are not sufficient. The Ministry, therefore, receives forecasts for macroeconomic parameters from multiple sources, but these are not consistent and do not make it possible to flexibly simulate alternative political decisions in real time. Finally, as there is no multiple-year budget, the links between the mid-term framework and annual budgets are very loose. The transition from the mid-term macroeconomic projection to a multiple-year budget primarily requires that the targets in terms of expenditure arising from the Government's multiple-year planning have been established and that these targets are regularly assessed in terms of their purposefulness and the effective use of public resources. The transition to a multiple-year budgeting is therefore conditioned by a real implementation of the Programme Budgeting. Additionally, in order to create and update the Mid-Term Macroeconomic Framework, it is necessary to implement a system that will allow informational and procedural interconnection of the preparation of macroeconomic prognoses and their projection into a mid-term macroeconomic perspective and then also into the parameters of a multiple-year budget. In other words, the creation of a stable and realistic Mid-term Macroeconomic Framework requires the following:*

- *to develop a mechanism for formulating and approving economic priorities at the level of the political decision-making process;*
- *to create such a system of macroeconomic forecasting at the Governmental level that would produce trustworthy and conservative prognoses of the future macroeconomic development and would also ensure the interconnection of macroeconomic parameters with public finance parameters,*
- *to finalise the mechanism of the creation of a mid-term macroeconomic prognoses that will allow Slovakia to meet its duties after acceding the EU and that will simultaneously suffice to the needs of the domestic decision-making process at the level of the Budgetary Chapters;*
- *to create and implement a methodology of the preparation of multiple-year budgets, including a transparent decision-making mechanism regarding the Government's activities and expenditure associated therewith.*

The central unit that will have the authority to produce macroeconomic prognoses for the public administration and that will be accepted by public institutions will be the Institute for Financial Policies (IFP) of the Ministry of Finance of the Slovak Republic. The Institute's responsibilities will include the presentation and public justification of the prognoses produced. The IFP will also *elaborate on the documents that the Slovak Republic, as a member state of the EU, will be obliged to generate for the European Commission. Furthermore, together with the Budgetary Policy Section and the Public Expenditure Section of the MF, the IFP will prepare the Mid-Term Macroeconomic Framework. The task of the Budgetary Policy Section will be to prepare multiple-year budgets reflecting (and limiting) the expenditure priorities of individual Chapters.*

Time Schedule*. Apart from legislative changes, the reform of the public finance management will need institutional capacities for its implementation. Therefore, the Reform will include the analysis of the budgeting process with respect to: organisational structure, human resources, and procedures and decision-making mechanisms of the MF as well as other selected ministries. It will also address the budgeting process optimisation in all its stages. The Public Finance Management Reform is a project that will not only affect the Ministry of Finance, but the whole public administration. The Minister of Finance has therefore formed a Managing Committee with the authority to supervise the reform process, to ensure co-ordination of relevant individual entities and institutions, as well as to interconnect those elements that are included in the Reform but has so far been prepared independently (e.g. the State Treasury System project, Programme Budgeting). By late June 2003 a detailed implementation plan should have been prepared.*

Priorities for 2003:

- *to create prerequisites for the reinforcement of strategic planning and for the transition to the Programme Budgeting in all Chapters;*
- *to decide on the powers and relations between the State Treasury System, the State Debt Management Agency and the Ministry of Finance; to build up the State Treasury System and the State Debt Management Agency such that they can exercise their key powers;*
- *to develop institutional capacities at the Ministry of Finance for the implementation of the Public Finance Management Reform;*
- *to finalise the Reform's implementation project such that the implementation phase may commence in the second half of 2003,*
- *to create a methodological apparatus for making macroeconomic prognoses at the Ministry of Finance,*
- *to elaborate the initial version of the methodology to include multiple-year budgeting.*

Priorities for 2004:

- *to further elaborate the Programme Budgeting methodology, in particular, the methods for formulating targets at individual levels of the programmes and the methodology for the success evaluation,*
- *to develop and implement a system for the Convergence Programme preparation,*
- *to make a test multiple-year budget.*

The Public Finance Management Reform *will be financed by multiple resources. A substantial part of the Reform (e.g. the Programme Budgeting, methodological apparatus for macroeconomic budgeting, multiple-year budgeting methodology, accounting, training for the State Treasury System staff and others) will be co-funded by the IBRD and World Bank through a loan and by the state budget. The loan will also be accompanied by technical assistance. This loan directly burdened the 2003 state budget with Sk 54m. The funds used in 2004 are forecasted at Sk 120m, while co-financing from the state budget will come along. The implementation of the project of the State Treasury System and the State Debt Management Agency is also supported by the PHARE project. Another project that will carry on with the current one is under preparation. The training activities, particularly during the Programme Budgeting implementation project, has also been supported by the USAID, who mediated a technical support provided by experts from the US Treasury. In the opinion of the MF, the tools for ensuring effective implementation of budgeted means and bigger transparency in financial management, in other words, the main economic benefits in strengthening the fiscal control institutional mechanisms are immeasurable. The Ministry thinks, in fact, that the benefits will be incomparably larger than the costs incurred. Other benefits of the project include financial revenues from minimum free balances of the state institutions and elimination of loss due to insufficient debt and assets management. The fiscal impact of the Reform will include the improvement of the Government's resources management and higher effectiveness of Governmental transactions. Moreover, stronger institutional structures allowing effective definition of priorities in using public resources will provide the Government with the ability to make decisions within a well-defined package of resources and hence will ensure budgetary discipline. A better quality liquidity and debt management should decrease unused funds on the Governmental accounts and help to improve the strategy for accepting Governmental loans and to decrease costs on these loans.*

Evaluation of the Experts’ Committee:

The Experts' Committee showed sympathy towards the proposed changes to the public finance management, being regarded as systemic and comprehensive. Strengthening the transparency and strategic planning, transitioning to a multiple-year budgeting, widening the Programme

Planning, and implementing hard budget constraints throughout the public administration may fundamentally change the system of the administration of public matters and may lead step by step to a more efficient state finance. The key factor will be the implementation phase and accountability if the accepted principles have not been met. For example, the Programme Budgeting project has been existing in Slovakia for at least six years, however, its application is very poor. If the Programme Budgeting is successfully applied to all Budgetary Chapters, it could help substantially increase the quality of public finance management. Multiple-year budgeting should introduce increased stability to public finance and to the macroeconomic environment as such, which will allow further inflow of investment. The experts also appreciated the intention to manage liquidity and debts on the Governmental accounts and the effort to better manage the Governmental loans. The Reform's strategy is, in their opinion, a positive attempt to create a management system that will stop chaos and that will assist (*ad-hoc*) the executives in managing finance. They hope that by completing the Public Finance Management Reform, the amount of state's interventions in the economy will drop. The experts also agreed that the Reform is very important and useful. In their opinion, the Strategy adopted reacted to notoriously-known imperfections. They added that the ministerial culture in Slovakia is such that regularly prepared green papers are, as a rule, much better than the follow-up, but much more important, measures for execution (if any). It is not the green paper that is the most important, but whether and when its intentions are implemented. Some experts therefore think that the Reform implementation will require the MF to expend maximum effort aimed at acquiring a sufficient support to the Reform from the political parties and other ministries and at adopting measures that would safeguard the Reform's long-term existence regardless of the composition of the Cabinet. The Reform's strategy should be closely linked to the system for the formulation of political aims. Otherwise, it will only be a good intention having no practical outcome. An important aspect will be to ensure quality and ethical experts in the State Treasury and the State Debt Management Agency, which will also depend on adequate financial support.

Critics pointed out the insufficient communication of the Strategy's impact analyses. The budgetary measures are far from being as hard as they should have been. The Strategy was reproached for its insufficient specification of the measures that should be adopted in order that the aims can be achieved (e.g. the further decentralisation and supervision of public finance at the regional level, it does not provide any guarantee in terms of how many measures will be implemented during the current Cabinet's mandate). The measures that would help decrease state expenditure in the mid-term framework are also missing and so the critics are concerned that the measures proposed by the Reform's Strategy may achieve marginal improvement, however, they will not effect any major change.

Amendment to the Act on Budgetary Rules (Hard Budget Constraints for Budgetary and Semi-Budgetary (Subsidised) Organisations, ESA 95 Methodology for Public Administration Sector, Dissolution of Certain Budgetary Chapters)

On 21 October 2003, the National Council adopted the Amendment to the Act on Budgetary Rules, which introduces hard budget constraints for budgetary and semi-budgetary (subsidised) organisations. The Amendment also adopts more stringent rules regarding the creation of liabilities by budgetary and semi-budgetary organisations in a current year. The aim is to eliminate the generation of new liabilities that are not provided for in a current budget. The Amendment also introduces a sanction mechanism in the event the budget constraints have not been met. This means that should a budgetary and semi-budgetary organisation undertake to make payments that have not been included in its current budget and will rollover this liability to the next year, it breaches the obligations stipulated by the Act on Budgetary Rules. This breach gives rise to a penalty of maximum Sk 1 million, which in fact would be classified as a damage to the organisation that, pursuant to respective legislation (Labour Code, Acts on Civil and Public Service) gives rise to personal accountability.

One of the reasons for the preparation of the Amendment was to establish a legislative framework for the European System of Accounts, ESA 95, in the Slovak public administration (for all entities whose budgets make up the public budget). The reason for the Amendment was the need to create a public budget and to quantify the deficit using the methodology applied by the EU. Within the EU accession process and pre-accession fiscal supervision, each candidate country was obliged to submit deficit and public administration debt statistics, prepared according to the ESA 95 methodology, to the European Commission up to 1 April. Contrary to the cash principle applied by the originally-used IMF methodology, the ESA 95 methodology uses the accrual principle of monitoring transactions. According to ESA 95, the revenue and expenditure balances of the current year's public finance eliminate, contrary to the IMF methodology, all financial transactions from the revenue and expenditure balances.

With the aim of decreasing the number of Budgetary Chapters, the Amendment also abolished the Chapters for the Supreme Court of the Slovak Republic (NS), Public Prosecution of the Slovak Republic (GP), News Agency of the SR (TASR), Slovak Radio (SRo), Slovak Television (STV) and, as a result of the new local state administration set-up (see HESO 4/2003), also for the Regional State Administration Offices. The budgets of the NS SR and GP were transferred to the Chapter of the Ministry of Justice, who thought separate Budgetary Chapters were unjustified. The funds allocated to the TASR, SRo and STV were insignificant and therefore the abolition of separate Budgetary Chapters for these institutions is also justified.

The Amendment to the Act on Budgetary Rules became affective as from 15 November 2003.

Evaluation of the Experts' Committee:

There have been many differences in the public institutions' financial management. The experts positively assessed the fact that the system will be simpler and the budget constraints harder. An encouraging fact is also the transition to the ESA 95 methodology. The experts perceived the Amendment as a step towards an increased transparency and effectiveness of public resources administration. The change to the Act was necessary, as without having it, it would be difficult to keep the budget within the given parameters. The Amendment will also enforce discipline in public organisations' financial management.

What will be important is the implementation of the Amendment, as well as of the pivotal Programme Budgeting. It will also be necessary to reform the public finance such that it allows more effective supervision over the public finance administration so that the public has a chance to see the purpose and effectiveness of the public funds expended.

One respondent thinks it is a smart way to technically and politically deal with the budgetary makeshift. Should the Parliament fail to adopt a State Budget Act, the budget that will be applied in the meantime will be the one proposed by the Cabinet and not that used in the previous year, as has been the case so far.

Several experts agreed with the abolition of some of the Budgetary Chapters, e.g. the Supreme Court or Public Prosecution. At the same time, one respondent suggested that a separate Judicial Chapter (all levels) be created in future so that Courts are not financed through the Chapter of the Ministry of Justice. The critics argued that the abolition of separate Budgetary Chapters of the Supreme Court and Public Prosecution, and their inclusion in the Chapter of the Ministry of Justice, is wrong and is economically unjustifiable. In their opinion, the aim of this measure was to weaken the independence, in terms of decision-making, of both the institutions.

Strategy of the Ministry of Finance of the SR and the National Bank of Slovakia for the Adoption of the Euro in the Slovak Republic (Euro Implementation in years 2008-2010)

On 16 July 2003, the Cabinet approved the document drafted by the National Bank of Slovakia (NBS) and the Ministry of Finance (MF) addressing Slovakia's accession to the Economic and Monetary Union (EMU), called the Strategy for the Adoption of the Euro in the Slovak Republic. In May 2004, the Slovak Republic became a member of the EU. An inherent part of the decision on the accession to the Union is the obligation to join the euro zone. Hence, the question is not whether, but when, to join the EMU. Although there are a few countries with a special position, namely Denmark, Great Britain and Sweden, which have yet not adopted the euro, the new Member States were not given this option and do not even need to have a referendum on this question. In July the public opinion poll Eurobarometer revealed that 70% of the Slovaks are for the euro, whereas only 16% are against.

The key conclusion of the document is that it would be most advantageous for Slovakia to adopt the euro as soon as possible if the country manages to sustain the compliance with the conditions associated therewith. These conditions concern the five so-called Maastricht (Convergence) Criteria that define the formal conditions of a country's readiness for the euro. In its Memorandum, the Slovak Government expressed its resolution to establish prerequisites for meeting the Criteria before 2006. The Convergence Criteria require that a country's inflation rate may not exceed the average inflation rate of three EU countries with the lowest inflation (1% in July 2003) by more than 1.5 percentage points; the ratio of the budgeted or real fiscal deficit to the GDP may not exceed 3% (Slovakia's plan for 2004 is 3.9% of the planned GDP with expected decrease in the following years), or it must show a trend leading to this value; the ratio of the general government debt to the GDP may not be higher than 60%, or it may not be rising (nearly 45% in Slovakia in 2002); the long-term interest rates may not be higher than the average interest rates in 3 EU countries with the lowest inflation rate by more than 2 percentage points (thanks to Slovakia's rising rating, the interest rates are steadily going down); and the fifth requirement is that over the two years preceding the accession to the EMU the exchange rate of *the local currency to the euro remains within the band of +/-15% (during last three years the exchange rate of the Slovak koruna to the euro fluctuated within +/-3%), albeit close to the central parity to the euro and without any devaluation against the other EU members' currencies. The Maastricht Criteria also require that countries join the exchange mechanism ERM II two years prior to implementing the euro. This mechanism specifies that the local currency may not fluctuate beyond the narrow band of +/-15%. The ERM II is a „bridge" to the monetary union.*

According to the aforementioned document drafted by the NBS and MF, an inevitable prerequisite for meeting the Criteria is the implementation of reforms that the Government undertook in its Memorandum. Slovakia will, however, have to carry out the reforms regardless of its entry in the EU as they are a prerequisite for decreasing financial and monetary risks, increasing foreign investment inflow and enhancing the business environment. Given the strategy of the NBS and MF, Slovakia could accede the EMU sometime between 2008-2010. If the Memorandum of the Slovak Government as well as the NBS's assumptions regarding nominal criteria are fulfilled and if all the necessary reforms are well under way, the nearest possible term would be the year 2008. As the whole process of joining the EMU takes approximately four years, the negotiations concerning the central parity should commence in line with Slovakia's accession to the EU. Hence, the country could join the ERM II mechanism in 2006 and the EMU two years later.

Should the forecasted revival of the European and world economy result and should no unexpected shocks occur, for instance, in the area of oil prices, the pre-accession economic programme forecasts the acceleration of the sustainable economic growth from the level of about 4% in 2003 to 5% in 2006. Additionally, it predicts the decrease of the fiscal deficit to 3% in 2006, of the inflation rate from 8.5% to less than 3%, of the current account deficit to under 5% and, at the same time, the retention of the government debt (at the level of 50% of the GDP). In other words, the pre-accession economic programme assumes that the key strategic intention of the Memorandum of the Slovak Government, which is compliance with the Maastricht Criteria for the accession to the EMU, will be achieved.

As specified in the Strategy, the main benefits from the early adoption of the euro is the decrease of the costs on the currency conversion for the citizens and businesses (of 0.25% to 1%, in the Governor's of the NBS opinion) and the elimination of exchange risks (against the euro) without the necessity to hedge. At present, the exchange risks increase the price of foreign capital by 2% per annum. Given the volume of business transactions with the euro zone and the associated countries of Sk 1,600bn a year, the savings will not be trivial. Other positive effects will include: the pressure on the local economic and political relations to continue reforms, pressure on the implementation of the budget policy in relation to the Stability and Growth Pact of the EMU (an agreement adopted by all euro zone members obliging them to adhere to the principles of prudent management of the public finances) and stable business conditions.

In the opinion of the authors of the Strategy, the quantification of the impacts arising from the accession to the EMU is difficult. In accordance with existing forecasts and analyses, the main benefit will be the accelerated economic growth, by 1% per annum (increment to the GDP growth), which will be a cumulative effect of the decreased transaction costs, eliminated exchange risks and decreased risk premium and interest rates. The Governor of the NBS believes many critics of the EMU accession do not duly appreciate this argument.

The MF and NBS argue that the positives far outweigh the negatives. The most difficult criterion to achieve will be, in the Minister's opinion, the fiscal deficit limit. Nevertheless, he thinks this requirement must be met regardless of whether Slovakia accedes into the EMU as it is an inevitable precondition of long-term sustainable growth generally. The ability to adhere to this convergence criterion will depend on necessary reforms of the whole social system, including pension reform. The opponents criticising the early adoption of the euro argue that the investment required for the fulfilment of the European standards (e.g. connected with the environment) will create tremendous pressure on national budgets. Other voices indicated that with the aim of meeting the deficit limit of 3%, the Government will curtail government expenditure, particularly capital investment (which is the easiest option), which would have an adverse effect on potential output growth in the long run.

With regard to actual convergence, Slovakia, based on the NBS's data, reaches 48% (46% in 1995) of the average EU GDP per capita. As regards the currency level, it is 41% (34% in 1995). Hence, despite favourable trends, the actual convergence indicators are low. After the country's accession to the EU, the economy will presumably begin growing faster, on average by 1% to 2% over the EU average. Assuming that the actual exchange rate will annually appreciate by 1% to 2%, the Slovak economy will grow by 2% to 4% faster in a comparable parity than the EU and thus the country will rise from the current level of approximately 50% of the EU to 75% within 10 to 15 years. Opponents, however, emphasised the fact that Slovakia is lagging behind the EU average in terms of its economy, price and wages and should not be downgraded. In their opinion, this is the first barrier to the country's early accession to the euro zone. A rapid convergence of price levels in Slovakia and the EU could boost prices and degrade the living standard. On the other hand, the Governor of the NBS thinks that it is hard to determine when exactly and at what *level of actual convergence it is appropriate to join the EMU. As the current GDP of 48% of the EU average, the future 70% may not necessarily be enough. He thinks it makes no sense to wait until we catch up with the price level and the GDP per capita (which may happen in 20 to 30 years). The Governor argues that we have to grasp the opportunity because our accession will accelerate the actual convergence. The proponents of the early accession to the EMU say that the low price level will be Slovakia's competitive advantage, attracting investors, which will accelerate the convergence.*

From the NBS's and MF's point of view, the major disadvantage of the accession to the EMU will be the loss of the independent monetary policy. The adoption of the common currency will render the exchange rate, an equilibrium tool, useless. There are also concerns arising from the stabilisation efforts leading to decreased inflation, expended by the European Central Bank, as they jeopardize economic growth. As it is still necessary to count on asymmetric reactions to external shocks, the stabilisation function will have to be performed by other policies and markets: fiscal policy, labour market, wage policy and capital market.

Opponents' argument against the early adoption of the euro is the notorious devaluation of inhabitants' savings. They expect that as a result of the drop of interest rates, together with high inflation after the accession to the euro zone, the actual interest rates will plummet. As stated in the Strategy adopted, these concerns often stem from an erroneous assumption of the exchange rate appreciation (of Sk to euro) if we do not join the EMU. In the case of inappropriate economic policy, the exchange rate could very well depreciate. Additionally, not only citizens' savings, but also prices of goods will be converted to the euro. Low interest rates on savings will thus be offset by several factors, one of which is, e.g., a faster economic growth.

An important requirement, in the proponents' opinion, for the euro adoption is that Slovakia should not join the EMU later than the neighbouring countries with whom it has significant trade and business links. A strong argument for the early accession is, in their opinion, the Slovak economy's exposure and orientation to the EU markets. Prior to Slovakia's accession to the EU, the country exported over 60% of its total exports to the EU (90% after the accession of ten new countries). Sluggishness in this area could be a negative signal to investors. Conversely, the opponents to the early accession think that Slovakia will have a better position, if it stayed out of the euro zone longer than its neighbours. The country could then consistently pursue its reforms and benefit from higher interest rates and a cushion of a flexible exchange rate. The critics therefore believe the risks outweigh the benefits. They make a point of Slovakia's sluggishness in economy, wages and prices and of its competitive handicaps, particularly a communist heritage of widespread corruption. They lack, e.g. the idea of fixing the exchange at the time of the accession to the ERM II. It should provide at least a rough idea (supported by relevant analyses) about the span of the actual exchange rate of the Slovak koruna to euro, advantages for the economy and the market prior to its fixation. This concerns an idea about various alternative scenarios, not a specific prognosis of the exchange rate level. Another disadvantage of the early accession is the fact that in the case of joining the ERM II as early as in 2005 or 2006, the koruna's exchange rate will not have enough time to appreciate and hence will be fixed at a disadvantageous level, i.e. worse than it could be a few years later. They also point out the threat of speculative attacks at the fixed currency, arguing that a single monetary policy of the European Central Bank cannot be effective for some many countries with so varied cycles and reform needs. The Ministry of Finance and the National Bank were advised to consider additional criteria necessary for the accession, as is the case of Great Britain, where, besides the Maastricht Criteria, economy's flexibility, price level, etc. are monitored.

The adoption of the euro may be hindered by the pension reform. The problematic area is the so-called transformation costs, i.e. costs incurred by the implementation of the capital pillar that are expected at 1% of the GDP. This will affect the fiscal deficit (see HESO 1/2004) and hence endanger the country's ability to comply with the respective convergence criterion - fiscal deficit of max 3%. The Government was advised to slow down the capital pillar implementation, or even put it off. Some economists think the question of priority between the pension reform and the euro is short-sighted, as both are necessary. At the time when the Strategy was being drafted, the pension reform was revamped with the aim to decrease the transformation costs incurred by the capital pillar implementation.

The Ministry of Interior (MV) labelled the document as "PR" and not well-founded. In their opinion, the document is missing profound analyses and hence cannot become an unbiased foundation for the Government to make decisions. Other critical voices emphasised that the document has not exploited all opportunities that could be addressed by a document of such significance (note: a similar document on the same topic drawn up by the Bank of England comprising 1,800 pages). It lacks the EMU early accession risk analysis as well as the alternative later-accession analysis. Critics reproach the document for the fact that it does not quantify costs and benefits in relation to the timing. Slovakia's ambitions to accede the EMU were also commented by the former EU Member States. In its monthly report, the Deutsche Bundesbank remarked that it would be reasonable if the new Member States do not rush into the ERM II. These countries first need to *prepare their economies for the onset of hard competition associated with the implementation of the euro. The transformation process would be simpler with a higher degree of exchange flexibility at hand. The EC spokesman advised the candidate countries to achieve a sufficient level of convergence prior to limiting their monetary instruments by joining the ERM II. The not-long-ago Candidate Countries should, in the opinion of other experts, take their time because their fiscal deficits are well above the limit of 3% and a policy primarily aimed at decreasing deficits could harm their economic growth. Others argued that by implementing the EU standards, since new EU members will encounter a number of cost-demanding challenges and simultaneously need to maintain the deficit under 3% of the GDP, Slovakia could find itself between the devil and the deep blue sea.*

There are three EU countries that have not adopted the euro yet: Denmark, Sweden and Great Britain. Their citizens have thus far rejected the accession to the euro zone. The arguments against varied - for instance, in Sweden, people were afraid that the membership in the euro zone would endanger their social state as the Government would be forced to re-assess the expenditure and make cuts. British euro sceptics argued that the euro zone countries suffer from sluggish economic growth and that the strongest EU economies do not adhere to the Stability and Growth Pact. There are also less rational, yet more convincing arguments: loss of national identity and of symbols.

Based on the Strategy for the Adoption of the Euro, Slovakia's accession to the euro zone seems to be realistic in 2008 to 2010. These are, however, only rough estimates. In mid 2004, the Minister of Finance and the Governor of the NBS are to submit an updated strategy that will be used as a basis for determining more specific data and probably the terms for Slovakia's accession to the ERM II.

Evaluation of the Experts' Committee:

The experts consider the Strategy for the Adoption of the Euro in the Slovak Republic to be an important document. As stipulated in the EU Accession Agreement, Slovakia is obliged to implement the common European currency. Hence, there is no question whether to join, but when to join the EMU. The Government's and NBS's intention to join the euro zone as soon as possible, i.e. in 2008 – 2010, received less consent.

On one hand, there were experts who regarded the strategy for the adoption of the euro as adequate to Slovakia's position, well-founded and sufficiently supported by public discussion. The MF and the NBS managed to communicate the fact that the benefits to be brought by the early accession to the euro zone prevail against the disadvantages. A positive is that the country, after becoming a EU member, has a new vision that could help formulate the Government's economic policy in the long run. The years 2008-2010 are a realistic term, yet the experts think the success of the fiscal reform is still pending, likewise the interest of the euro zone to enlarge. Several studies have revealed that the plusses of joining the euro zone should outweigh possible difficulties. There are analyses that claim that the implementation of euro would be advantageous for Slovakia's economy and the analyses with the opposite conclusions have, in the opinion of euro proponents, not been presented and arguments against joining the EMU are unconvincing. The main advantage of adopting the common currency is the decrease of transaction costs for citizens and businesses and the elimination of exchange risks associated with the euro. Several experts agreed that implementation of the Maastricht (Convergence) Criteria and particularly the decrease in the fiscal deficit (to the level of 3% of the GDP) will be beneficial regardless of the acceptation or rejection of the euro - and the sooner, the better. One respondent thinks it would be no problem if the accession is co-ordinated with the neighbouring countries. Since the accession to the EMU is rather a political decision depending to a certain extent also on the European Central Bank and the European Commission, it remains an open question whether the Middle European Countries would implement the euro separately. Another expert admitted that the discussion about whether to join the EMU at the earliest date possible or a few years later seems worthless as, in his opinion, a few years will not help Slovakia to increase its actual and structural convergence to such a radical extent that it would counterbalance the key disadvantage - the loss of an independent monetary policy. „If we are willing to sacrifice [the monetary policy], with all medium-term negatives associated therewith, why don't we then join [the euro zone] as soon as it is technically possible?", he asked.

Some proponents of the early adoption of the euro understand commercial banks and their criticism of the common currency, because after the euro implementation they will lose a significant part of their revenues, and banking analysts a part of their job.

On the other hand, there was a second group of the experts who thought the Strategy incomplete or superficial. In their opinion, the authors are too "euro-optimistic" and, actually, unaware of what the euro will bring. With regard to the importance of the issue, the experts expected a more extensive analytical document mapping the pluses and minuses of the membership. The existing analyses have not yet sufficiently clarified the risks arising from Slovakia's earlier and later accession to the euro-zone. The adoption of euro should be preceded by a clearly quantified analysis of risks and benefits and by a definition of exact conditions that must be fulfilled before a common European currency can be implemented in Slovakia. One expert highlighted Great Britain's ten specific criteria that must be met prior to the referendum on the country's accession to the euro-zone.

Critics think the early adoption of the euro is not in line with Slovakia's economic interests. Furthermore, the ECB warns that the euro currency should not be adopted hastily. Critics' main arguments include the loss of an important element of a macro-economic regulation - sovereign monetary policy of the NBS, which could flexibly react to various economic pressures that occur in a transition economy, where reform measures are taken, much more frequently. Opponents argue that such countries as, e.g., Germany, Ireland, Portugal, or Slovakia need different currency policies as a consequence of the differences in the status and performance of their economies (different optimal currency areas). The Slovak currency is steadily appreciating and its later conversion may bring the appreciation of savings in the Slovak korunas. One of the respondents presented an opinion that an early fixation of the koruna's exchange rate could even result in the so-called Argentine scenario. Some experts were concerned about the price rise of products and services due to the conversion from the koruna to euro. Hence, the inhabitants' real income would drop, having an adverse effect on people's living and social standard.

The respondents' negative standpoint was stringent in terms of possible postponement or reduction of reforms due to the implementation of the euro. If, for example, the Convergence Criteria were implemented, the fiscal deficit will have to be maintained at the maximum limit of 3% of the GDP, which may result in inhibiting the cost-demanding pension reform. Several arguments for a later implementation of the euro, uttered by banking analysts, are based on, as characterised by one respondent, a naïve assumption that the reform effort of the current or future Government will not lose its vigour.

There was also an opinion that the effort to adopt the euro as soon as possible is motivated politically and that the NBS's stance is rather affected by personal ambitions and perks - to become an employee of the ECB, with a higher income, less responsibilities and less workload, as soon as possible.

Tax Policy

Tax Reform Concept (Flat Income Tax - 19%, Unified VAT - 19%, Raising Excise Tax, Exemptions Abolished, Tax Legislature Simplified)

On 5 June 2003, the Slovak Cabinet approved the draft Tax Reform Concept for 2004 to 2006 that has been drawn up by the Ministry of Finance (MF) of the Slovak Republic. According to the accompanying report, the Concept reacted to the fact that due to frequent legislative changes the tax law has become too complicated and confusing, with many exemptions, tax reliefs and holidays (e.g. only the Income Tax Act contained 90 exemptions, 19 income items did not fall in the tax base, 66 were free of tax and there were 37 different tax rates). The aim of the Tax Reform is to eliminate imperfections and deformations of the tax system. Furthermore, it aims at taxing all types of income at all levels equally and hence achieve, as stated in the Concept, the maximum possible level of justice. The tax reform is being carried out in the context of other social changes, e.g., the reform of the social system, pension system, healthcare, and it is, according to the Ministry of Finance (MF) necessary to ensure that all these reforms are tuned. The underlying principles of the tax reform are: justice, proportionality, neutrality, eliminating double taxation, simplicity and effectiveness. The Concept says that the needs of the state budget will be reflected in the tax rates, but may not affect the functioning of tax principles. The Tax Reform Concept was based on the assumption that with regard to specific needs of the society, it is the most appropriate to tax profit, property and consumption, while as regards the tax mix, it aimed at transferring the tax burden from direct taxes to indirect ones (VAT and excise taxes), which are easier to collect. The outcome of the tax reform will be the decrease of the weight of direct taxes. The missing tax revenues arising as a consequence of a flat tax rate imposed on corporate and income tax will be offset by increased revenues from other taxes, particularly VAT and excise taxes.

***Direct taxes**. The Concept proposes the so-called **flat tax**, i.e. an equal rate applied to all types of corporate and personal income (profit) at **19%**. It also abolishes, as from 1 January 2004, the widest possible number of tax exemptions. As regards the individuals, the one-off deductible should have been set such that no taxpayer pays more than before. At the rate of 19%, the deductible would thus amount to Sk 81,300 per taxpayer a year (Sk 80,832 approved) as opposed to current Sk 38,760. The same deductible would also be applied to spouses who have no taxable income (subject to the fact that the deductible amount for children of Sk 16,800 would remain* *unchanged). If a spouse had a taxable income that did not reach Sk 81,300 (or, as approved, Sk 80,832), a taxpayer could deduct the difference between the deductible and the spouse's income. According to the average numbers of children and spouses for whom taxpayers apply the deductible items, after the reform the taxpayers would apply a deductible of Sk 101,147. This amount should be appreciated every year by a method established in an act. The negotiations with the Ministry of Labour, Social Affairs and Family explored alternative suitable support systems for families with children that would ensure a more just distribution favouring families with children with lower income (e.g. a tax bonus, the so-called negative tax). In fact, this system eventually succeeded (see page 73). It concerns families with children who would not benefit from the deductible for children as their income is too low and hence they cannot deduct it at full. In connection with the pension system reform under preparation, the Concept proposed that the contributions paid in the mandatory pay-as-you-go (PAYG) public pension scheme and contributions to the second mandatory fully-funded private pension scheme would also be tax deductible. The third pillar would be regulated similarly to any other type of saving, i.e. the contributions (premiums) in the voluntary private pension scheme will not be tax deductible and capital yields therefrom will be subject to taxation. The contribution in the third pillar that is paid by an employer on behalf of employees (e.g. the supplementary pension insurance) will be, according to the Concept, the employer's tax deductible item, however, it will be a taxable item for the employees.*

*The Concept also proposed the abolition of the lump-sum taxation of entrepreneurs as a non systemic element. The aim of simplified taxation and tax administration for small businesses is to be met by the application of flat expenses (proposed at 20%, approved at 25%). Although the **assignment of** 1% of the paid **income tax** is, according to the MF, a non systemic element, the Concept proposed to maintain the current system of assigning 1% of taxes for community purposes, NGOs, as they perform irreplaceable society-wide functions of the third sector, which has a lack of own funds for the development of its activities as well as of financially strong donors (the Parliament has raised the amount of tax that can be assigned to the third sector to 2%). The new system is expected to introduce a substantial simplification to the income and corporate taxes and should align them with the aforementioned principles.*

*As regards property taxes, the Concept proposed the **abolition of the Property Transfer Tax** (unsuccessful so far) and the Inheritance and Gift Tax (successful) (see page 38) as these imposed multiple taxation and revenues therefrom were incredibly small.*

*As regards the **Real Estate Tax**, in the future all real estate should be taxed on the value principle (according to a price map). The valuation of real estate at market prices should be implemented in the medium term (by 2005). The concept also proposed partial changes to the Real Estate Tax as from 1 January 2004 with the aim of securing tax revenues for major cities and of creating space for eliminating transfers to these municipalities from the state budget. It also proposes to examine the alternative of implementing taxation of freehold only (i.e. the tax on building and flats would be abolished), while maintaining the total tax revenue.*

*As regards the taxation of motor vehicles (**Road Tax**), the Concept proposed that only vans and trucks be taxed according to their weight and the volume of exhaust emissions. Hence, passenger cars and busses would not be taxed (unsuccessful so far). With the aim to implement the EU Directive, it is necessary to apply tax relief on the combined transport.*

***Indirect taxes**. The Concept implements **a single VAT rate of 19%** applicable to all goods and services. The Parliament adopted a respective Amendment to the VAT Act (see page 31) and the upper rate of 20% was decreased and the lower one of 14% raised. Previous tax rates were effective from the start of 2003.*

*The new tax system expected that **excise taxes** would be fully harmonised with the EU legislation as of the date of Slovakia's accession (of all excise taxes, the only one that was not in compliance after earlier (August) changes (see page 32) with the minimum EU rates was the excise tax on tobacco). The Concept forecasted the implementation of tax warehouses as from 1 January 2004 and originally this was also the planned date for adjusting the excise taxes on beer, mineral oils and tobacco. As a consequence of the harmonisation, the excise tax on tobacco, as required by the EU, must be raised to 57% of the retail price (including VAT) of the type of cigarettes with the highest sales volume (after the August adjustment, the excise tax on cigarettes currently amounts to 53.2% of the price. Slovakia has at the same time managed to negotiate a transition period regarding this tax until 2009.)*

***Municipal fees** (maximum levels set) should be kept in place, however, there should be a review of their justification. This relates particularly to fees for using public areas, collection, transport and liquidation of communal and small construction waste as well as fees for the sale of alcoholic beverages and tobacco products. The last mentioned had to be cancelled at the date of Slovakia's accession to the EU.*

Tax Reform Impact on Public Finances in 2004

(in Sk m)

Tax Revenues	***Budget Framework***	***After Reform***	***Difference***
Income Tax	89 500	63 400	-26 100
Value Added Tax	107 900	118 400	10 500
Excise Taxes	36 700	42 200	5 500
- on Mineral Oils	*23 000*	*25 800*	
- on Alcohol	*4 000*	*4 000*	
- on Beer	*1 700*	*2 400*	
- on Wine	*200*	*200*	
- on Tobacco	*7 800*	*9 800*	
Road Tax	2 700	2 000	-700
Real Estate Tax	4 400	5 500	1 100
Inheritance and Gift Tax, Property Transfer Tax	1 500	0	-1 500
Other Revenues	***Before Reform***	***After Reform***	***Difference***
Communal Fee for Sale of Alc. and Tobacco Products	430	0	-430
Compensation of Pensioners	-	-1 600	-1 600
Total			**-13 230**

The Concept estimated the overall impact of the tax reform on public finances at a decrease of Sk 13.2bn on the Framework for the 2004 State Budget. The Tax Reform Concept reflects the Government's obligation ensuing from its Memorandum - to achieve the total fiscal deficit of maximum 3% of the GDP. In 2004 the proposed tax reform should, in the opinion of the Financial Policies Institute of the MF, have a negative impact on the growth of household consumption, down by 0.7 to 1.1 percentage points. The decline of household consumption should be partially offset by the increase in investment, up 0.3 percentage points. The decrease of aggregate demand should be offset by the decrease of imports, hence, the net impact of the tax reform on the country's economic growth was estimated to be no change, while the trade balance at stable prices should slightly improve. The Concept also forecasts long-term positive effects on unemployment. From the macroeconomic point of view, the Concept proposed should bring positive effects to the business environment. The current tax policy based on selective advantages to some industries or types of businesses will be replaced by a uniform policy establishing conditions that are generally favourable for business and investment (e.g. depreciation policy, better policy with regard to the redemption of tax losses, the abolition of the requirement that expenses must be paid so that they are recognised as taxable expenses, etc.). In the opinion of the MF, these should stimulate the country's economic growth. From the static point of view (disregarding the positive effects on the economic growth resulting from lower direct taxes and simplified tax legislation), the reform will, according to the analysis of the TREND weekly, have a negative impact (higher tax burden) on taxpayers who will in 2004 earn between Sk 1,000 to 24,500 gross and will not apply a tax bonus on a child (if the bonus applied, it will have a negative impact of people earning between Sk 13,000 to 24,500, in the case of two children, between Sk 15,500 to 24,500). In absolute figures, the reform will have the worst impact on people with gross monthly income around Sk 20,000 as their tax will rise by approximately Sk 260 a month. Relatively, after paying the flat tax, social insurance premiums and the VAT, the tax reform will most significantly have a negative effect on employees with an income of Sk 13,000 (average nominal monthly wage of employees in the economy of the SR in 2003 was Sk 14,365). The TREND's analysis did not reflect the increase of child support (under preparation at that time), from Sk 270 to Sk 500) (see page 73), nor the increases in excise taxes (see page 32). The tax reform was also expected to create a fiscal prerequisite for the compensation of social effects on some groups of the population that will be impacted by the increase in VAT and excise taxes and at the same time will not benefit from the cuts of direct taxes, as they have non taxable income (e.g., pensioners, the unemployed, etc.) (see HESO 1/2004).

Critics of the tax reform primarily focused on the tax rates (the flat income tax rate originally proposed was at 20% as well as the single VAT rate, excise taxes), on the level of the tax burden laid on the middle class who will, in their opinion, carry the heaviest burden of the reform, on the abolition of lump-sum income tax, on the original proposal to cancel the tax assignment, and on the proposed abolition of tax benefits on the supplementary private pension insurance companies/supplementary private pension funds.

The draft Tax Reform Concept for 2004 – 2006 was first discussed in the Tripartite. The representatives of the Confederation of Trade Unions of the SR disagreed with the draft Concept *and the representatives of the Federation of Employers' Associations of the SR recommended the document with comments.*

The Concept also refers to examples of brave tax reforms in other countries: New Zealand, Ireland and Estonia. Ireland and New Zealand radically decreased their income taxes, Estonia implemented a single tax rate and profits retained in the country are completely free of tax. The economic development in Ireland and New Zealand after the reforms' implementation is regarded as an economic miracle, characteristic for a significant inflow of foreign investment and a high economic growth.

The tax reform proposed required specific changes to the tax legislation (see below). Some of these changes became effective as of 1 January 2004, others are expected to become effective as of 1 May 2005, or in the middle term.

Evaluation of the Experts' Committee:

All in all, the Tax Reform Concept received a positive evaluation. Compared to the current situation, it is expected to bring substantial benefits. The Experts' Committee members posed a great number of contradictory arguments for and against:

Positives (as defined by the members of the Experts' Committee)**:**

- after several years in practise the majority of the changes will have positive dynamic effects upon the Slovak economy - it will motivate participants in the economic processes, consistent with the creed that it is worth working and it is not worth avoiding taxes;
- it will simplify and clarify the tax legislation, tax collection and administration (it is also necessary to simplify communication and contacts with Tax Offices and to consider electronic tax administration);
- more just flat tax - eliminating progressive tax rates will limit the discrimination of some income groups against others;
- unification of income and corporate taxes;
- restrictions to exemptions;
- a more just and better conceivable tax system - positive impacts on businesses and investors; higher inflow of investment including FDI as some grave barriers to enterprise will be eliminated; through implementing flat tax rate, the total tax levied on businesses will be lower than in the neighbouring countries, which will provide Slovakia with a competitive advantage in attracting FDI and a follow-up fight against unemployment;
- shift of weight from direct to indirect taxes;
- single VAT rate - restrictions to lobbyism arising from attempts to categorise goods at the lower VAT rate; removing advantages to some manufacturers and importers;
- proposed abolition of the Road Tax, Inheritance Tax, Gift Tax and Property Transfer Tax - avoidance of double taxation (e.g. of dividends);
- the rate will help stabilise public finances.

Negatives (as defined by the members of the Experts' Committee)**:**

- increased tax burden of the majority of the population;
- the heaviest burden will be placed on the shoulders of the middle class, of whom a portion may drop below the poverty margin after the implementation of other reforms (the social system, healthcare, education, etc.) and after price deregulation;
- negative impact on pensioners (increased prices as a result of higher indirect taxes, no direct advantages of decreased direct taxes) from a both static and dynamic point of view in the middle term; this will have to be compensated by increased pensions and other payments;
- insufficient analysis of the tax reform impacts on inhabitants; lack of qualified impact studies that would replace the currently used method of trial and error;
- elimination of exemptions that decreased tax burden;
- single VAT rate - no lower VAT rate (at least for a transition period) for certain types of goods and services (e.g., basic groceries, medicine, books, building works);
- increased excise taxes, particularly on mineral oils;
- high income tax rates (the opportunity to create a European tax paradise wasted), as well as VAT rates;
- misleading term "flat tax", as there still exist tax deductible items;
- inconsistency of the tax reform (removal of tax benefits provided to the supplementary private pension insurance companies/private pension funds) with the pension reform regarding its third pillar (voluntary private pension pillar/scheme) that is to be, in the opinion of the Ministry of Labour, Social Affairs and Family, the dominant one;
- the tax reform does not create any pressure on the state to make an more efficient use of state funds.

Even prior to the reform's approval, the Cabinet has adopted compromises to the original idea - it retained the tax assignment system (2% of the taxes may be channel to non profit organisations).

Later, as a result of unfavourable development of the state budget revenues, the Government decided to increase excise taxes *(see page 32)*, while there were exemptions to these implemented for wine and small breweries. Additionally, the Ministry of Finance agreed to not abolish the Property Transfer Tax and Road Tax because of the subsidies to municipal public transport. The aforementioned compromises could trigger an avalanche of demands raised by other interest groups (struggle for maintaining the lump-sum tax). If the Ministry accepted more compromises, what would remain of the tax reform, abandoning its key principles, would be a bare torso - reform effort stripped of its meaning.

Uniform VAT Rate at 19% Introduced (Amendment to the Act on Value Added Tax)

On 27 June 2003, the National Council (NR) passed the Amendment to the Act on Value Added Tax submitted by the Ministry of Finance of the Slovak Republic (MF). As from 1 January 2004 the Amendment abolishes two distinct VAT rates: the basic rate at 20% and the reduced one at 14%. It also introduced a single VAT rate applicable to all goods and services at 19%. This change ensues from the Government's Memorandum. The introduction of the single VAT rate is a pivotal element of the tax reform, the core of which became effective at the beginning of 2004. The reform transfers a part of the tax burden from direct onto indirect taxes. The approval of the single VAT rate, bringing increased tax revenues to the state coffers, was a key prerequisite for the following step - decrease of income and corporate taxes.

The MF expects that the single VAT rate will simplify the mechanism of the tax application, decrease administration for both taxpayers as well as tax administrators and eliminate speculation stemming from two different rates. The Minister of Finance, Ivan Mikloš said that the single VAT rate, within the comprehensive tax reform, would help improve the business environment and will become a stimulus for further investment. The changed VAT rate, together with increased excise taxes (see page 32), will at the same time offset lower state revenues as a consequence of the planned decrease in income and corporate taxes to be implemented in early 2004. The MF forecasts that in 2004 the change to the VAT rates will supply the state budget with additional Sk 14.1bn. The MF intends a neutral effect of the tax reform, i.e. the tax collected after the reform should be equal to the one before the reform. The MF further argues that the abolition of the lower tax rate was rendered necessary because through it, the state inappropriately subsidised all layers of the population and not only those that really needed the subsidy (pensioners, weaker social groups). All in all, the rise of the lower VAT rate will mostly affect the people who do not pay the income tax, as these will not be able to benefit from its decrease. For them, the Minister of Finance plans to implement direct compensation of approximately Sk 5bn. The introduction of the single VAT rate of 19% will trigger price increases of all types of goods and services that are currently taxed at the lower rate. These primarily include groceries, medicines, energies, construction, building works, books, newspapers, magazines, hotel and catering services.

The original idea of the tax reform assumed a single VAT rate at 20%. When discussing the Amendment, the Cabinet, however, decided to decrease the initial rate to 19%. It also changed the proposal made by the MF regarding the rate applied to the income and corporate tax and decreased it from 20% to 19%. A part of the ruling coalition, as well as some business circles, created pressure for more radical cuts of both types of taxes, or at least one of them. For instance, the Association of the Slovak Economists promoted flat income and corporate tax at the level of 16% and VAT tax at 19%. The negative tax impact, resulting from the lower income and corporate tax, could be offset by the abolition of the active unemployment policy, which aimed at creating new jobs and annually consumed Sk 4.5bn. The Association believes that this policy is inefficient and thinks that better conditions for fighting unemployment would rather be created by a healthy business environment. The Ministry rejected these proposals arguing that the 2004 state budget cannot afford this change, especially with regard to the intention of maintaining the fiscal deficit at 5% of the GDP. Another high-profile reproach referred to the inefficient use of state resources. Critics argued that should the state be better able to control its expenditure, there would be more space for implementing lower income and corporate tax or VAT rate.

The abolition of the lower VAT rate was much criticised by construction companies, book and press publishers, travel agencies, pharmacists, and also by the TU. In the opinion of the Association of Construction Entrepreneurs of Slovakia, the increased VAT rate for construction works will worsen the already poor situation in the construction industry in Slovakia. The current industry's share in the GDP is only 4% to 4.5%, while in more developed countries it generates from 10% to 12% of the GDP. Likewise, the Slovak Association of Travel Agents expressed its fundamental disagreement with the implementation of the VAT rate, which will, in its opinion, substantially affect the active tourism in Slovakia and will result in a price increase of 20% to 25%. Publishers and booksellers think that the single VAT rate of 19% will have an adverse impact of the sales of books and printed periodicals. Booksellers recognised a decrease in sales when the lower VAT rate *had been increased from 10% to 14%. Critics argue that should the sales of periodicals drop, the regional printed media may cease to exist. Protests against the increase of the VAT rate on books were also expressed by the Science Council of the Institute of Slovak Literature of the Slovak Academy of Sciences. In their opinion, the measure, if implemented, would liquidate the Slovak literature, literary science, literary studies and, all in all, the national culture history learning. The representatives of the publishing community, as well as some of the opposition Members of Parliament, proposed to retain the lower VAT rate for books, periodicals, or implement a zero rate, as is the case of some EU countries. They supported their proposal by saying that books are irreplaceable in the nation's cultural development and pointed at the right for information that is ensured by periodicals. The Minister of Finance rejected these arguments by emphasising the necessity of consistency, which would be loosened if a special VAT rate on books or medicines was introduced.*

EU Directives make it possible to use a single VAT rate at minimum 15% and one or two lower rates at minimum 5%. They however recommend a single rate. The majority of the EU countries use two. As regards the transition countries, a single VAT rate has been implemented in Russia and Ukraine.

The governmental draft act was passed in the Parliament with only technical and legislative adjustments. The most significant change - the proposition that all VAT payers should obligated to use double-entry accounting - was rejected.

The MF tried to increase state revenues during 2003 by imposing tax on advance invoices. Hence, the Amendment became effective on 1 August 2003 with the exception of a few provisions (e.g. VAT = 19%) that will come into effect as from 1 January 2004.

Evaluation of the Experts' Committee:

The majority of the evaluators welcomed the implementation of a single VAT rate, which is expected to simplify the tax collection system and limit the space for tax evasion. Some experts at the same time disagreed with the rate, which could, in their opinion, be lower, particularly if the state administration pursued the possibilities for reducing state expenditure. However, there were also opinions promoting the original rate of 20%, which would make it possible to further decrease the flat income and corporate tax (to the preferred level of 16%). Several experts would also support a lower VAT rate retained for certain types of goods and services (basic groceries, books, press, medicines, construction works). Others argued that the implementation of a single exception would encourage various lobbyist groups to negotiate lower tax rates for their particular product or service. Several experts also proposed to slow down the implementation of the reform and some suggested implementing a transition period while the lower rate would be retained. There was also an opinion that if the decrease of the VAT rate from 23% to 20% had not been implemented as from 1 January 2003 but within the current tax reform, the change would have received a much warmer welcome. Critics lacked arguments for the single VAT rate as well as better-founded impact studies analysing the effects of unified VAT rates upon the Slovak economy and inhabitants' social circumstances. The increase of the tax burden may cause problems to the Slovak farmers, tourism, healthcare system, publishing and construction industries, etc. The price rise, in the opinion of some experts, triggered by the increased VAT rate on certain goods and services will not be dramatic, however, several evaluators think it will adversely affect particularly lower and middle class individuals. As the Slovak economy is an open one, in future it may prove necessary to adjust our system to the ones used abroad by, e.g., implementing two VAT rates that are common in the EU.

Raising Excise Tax (on Mineral Oils, Beer and Tobacco)

On 27 June 2003 the National Council (NR) adopted the Amendment to the Act on Excise Taxes on Mineral Oils, the Amendment to the Act on Excise Taxes on Beer, and the Amendment to the Act on Excise Taxes on Tobacco, which imposed, as from 1 August 2003, higher rates of these taxes. The proposal for an early rise of the excise taxes was submitted by the MF with the aim of increasing tax revenues. These were to be applied so that the fiscal deficit at the planned level of 5% of the GDP could be retained. The threat of a higher deficit was mainly caused by the overestimated tax revenues of the VAT tax (the budget was missing over Sk 13bn) and corporate tax. The MF at the same time overestimated the revenues from the increased lower level of the VAT tax, from 10% to 14%, and exaggerated the growth of Slovakia's consumption. All in all, there was a threat that the deficit will be exceeded by Sk 3.8bn, i.e. by 0.3% of the GDP. In the attempt to confront the situation, the Ministry decided to raise excise taxes as early as in August, although this action had originally been planned for the beginning of 2004, when the re-vamped tax system was expected to be launched (see page 27). Originally, the increased excise taxes were to cover the gap of the state revenues in 2003 in full, however, since their adoption was delayed (the initial intention was to implement the rise as early as in July), the MF forecasted *lower revenues by Sk 600m to 640m.*

In the document submitted to the Cabinet, the MF proposed to increase the excise tax levied on mineral oils to Sk 13.90-Sk 17 per litre, up Sk 1 to Sk 2.50 per litre. As regards the excise tax on beer, the document proposed to use alcohol-volume-based system (e.g., 4.6%) instead of degrees Plato (e.g., 12°). The intended rate was at Sk 250 per hectolitre/alcohol volume. The excise tax imposed on cigarettes, cigars and cigarillos was to be adjusted regardless of the length at a single level of Sk 1.40 per piece. The rate on other tobacco products was to be Sk 1,350 per kilogram. Additionally, the MF planned to impose tax of Sk 25 per litre on still wine and raise the tax on sparkling wine, Sk 24 per litre to Sk 25 per litre. At stable consumption of these commodities, the Ministry predicted the increase of state revenues by approximately Sk 3.7bn. The Ministry also expected that due to higher demands on the tax administration, the number of staff at Tax Offices and Customs Duty Office will also have to increase.

During its meeting on 28 May 2003, the Cabinet substantially changed the original MF's proposal. It decided to suspend the excise tax on still wine, marginally increase the tax on beer and at the same time retain the degree-Plato system. On the other hand, the Ministers proposed to raise the excise tax on mineral oils by more than the proposed increases in the MF's document. Only the excise tax on tobacco was approved by the Cabinet at the amount as proposed. The Parliament passed the Cabinet's proposal with only one major change - a decreased tax rate for small breweries (they are currently four in Slovakia: Tatran, Popper, Horden, Steiger). The MF consented to the change. According to the EU legislation, smaller breweries are the ones with annual production under 200,000 hl. Distinctive taxation thereof is in compliance with the European standards and is applied in 9 EU countries. From the consumers' point of view, the price rise was to be as follows: petrol up Sk 3.80 per litre, diesel oil up Sk 3.20 per litre, a packet of cigarettes up Sk 9 and bottle of beer up about Sk 1.

	Current	**Rate proposed by the MF**	**Rate adopted by the NR SR**	**Min EU rate ***	**Excise tax increase (%)**
Beer – big breweries *(Sk/hl/degree Plato)*	30	Sk 250 *(per hl per %-age of alcohol)*	50	32,4	67
Beer - small breweries *(Sk/hl/degree Pato)*	23	Sk 250 *(per hl per %-age of alcohol)*	37	9	60
Still wine *(Sk/l)*	0	25	0	0	0
Sparkling wine *(Sk/l)*	24	25	24	0	0
Unleaded petrol *(Sk/l)*	12,4	13,9	15,5	11,81	25
Leaded petrol *(Sk/l)*	14,5	17	18	13,87	24
Kerosene *(Sk/l)*	11,8	13,9	14,5	10,08	23
Motor oil *(Sk/l)*	11,8	13,9	14,5	10,08	23
Heating oil *(Sk/kg)*	0,6	1,6	0,8	0,53	33
LPG *(Sk/kg)*	4,3	6,8	7,8	4,12	81
Alcohol *(Sk/l)*	250	250	250	226	0
Cigarettes - short *(Sk/pcs)*	0,95	1,4	1,4	1,5**	47
Cigarettes - long *(Sk/pcs)*	0,95	1,4	1,4	1,5**	47

** at the exchange rate of Euro 1 = Sk 41.16*
*** The SR has negotiated a transition period until 2009.*

All entities involved expressed their objection to the proposed increased tax on still wine, including The Union of Grapes and Wine Manufacturers in Slovakia, the Slovak Chamber of Agriculture and Food (SPPK), the Federation of Employers´ Associations (AZZZ), the Association of Towns and Communities of Slovakia (ZMOS). They all believed the planned rate would, at the given level, liquidate the Slovak winemaking because it would render the Slovak winemakers unable to compete with those in the neighbouring countries. The Cabinet satisfied these fears and did not levy excise taxes on still wines. The proposed tax on beer was strongly opposed by all brewing companies represented by the Slovak Association of Beer and Malt Manufacturers. Should the initially intended rate be imposed, resulting in an increase of price per a bottle of beer from Sk 2.25 to Sk 4.45, it would function as a prohibition on beer sales. The representatives of breweries also criticised the fact that the Cabinet had not included its intention to raise the excise tax on beer in its Memorandum and, hence, the manufacturers did not include it in their financial plans for 2003. The breweries have eventually managed to negotiate a lower increase, yet they did not regard it as a compromise, but an unfair measure against their sector. The breweries were concerned that the higher excise tax would decrease the production of beer and, hence, increase unemployment not only in the breweries, but also in associated sectors. The Cabinet's approach has therefore imposed uncertainty upon the business environment, as the breweries can never be sure now that the excise tax will not be increased again when there are gaps in the state budgets. The breweries further highlight the stagnating exports of beer since the beginning of the year, *when the increase of excise tax by 10% was followed by a decrease in sales by the same rate. With its excise tax on beer, Slovakia overtook the Czech Republic, where the tax rate is Sk 31 per hl (degree Plato used), as well as Germany with Sk 32 Sk per hl and degree Plato used. The AZZZ criticised the increase in excise taxes in general. Its representatives think that the change will affect the final consumption and, hence, tax revenues, which will not achieve the amount forecasted by the MF. In the AZZZ's opinion, the rise of excise taxes above the levels in the EU will prove worthless, while the increase of the prices of fuel will adversely affect the whole business sector. The SPPK thought the increase of excise taxes could endanger the whole farming sector, which would be, due to adverse conditions, facing the worst crisis of the decade, likely to produce annual losses of up to Sk 4bn. The critical comments also referred to the Ministry's decision to include the increase in excise taxes in the tax reform. They argued that the change to the rates was no different from similar measures adopted in the past and that the only purpose of the measure was to decrease the fiscal deficit. In the opinion of the opposition, the adoption of the Acts on the increase of excise taxes, together with the Act on VAT, meant the end of a social state in Slovakia. The opposition argued that the Cabinet did not try and deal with fiscal problems by restricting the state's overabundant consumption, but will only be rid of the burden by laying it on the citizens' shoulders. The measure would not boost the economy's performance, but will rather further its hindrance.*

The Amendment of the Excise Tax on Mineral Oils, the Amendment of the Excise Tax on Beer and the Amendment of the Excise Tax on Tobacco became effective on 1 August 2003.

Evaluation of the Experts' Committee:

The originally unintended increase in excise taxes and the change to the rules in the course of a fiscal year was regarded by the Committee as unacceptable, unprepared and non systemic. The experts think it is a risky precedent that may adversely affect the Slovak economy. Through higher taxes as from August than initially planned, all citizens paid for a bad estimate of the VAT revenues for 2003 by the MF's officials and for the follow-up gap in the state budget. The experts do not think a state budget deficit is a sufficient reason for taking such a measure and would prefer that the Cabinet looked for reserves and possibilities for decreasing fiscal expenditure. Tax rates should be sustainable in the long run, or, in other words, should be used as a medium-term instrument and not be responding to imminent problems in the state budget. Several experts were also surprised that the Cabinet that regards itself as rightist used, in the case of an increased deficit, a leftist response - increase in taxes. Some evaluators said that the MF would not manage to raise tax revenue anyway as the increased excise taxes will decrease consumption.

The experts also disagreed with excise tax rates exceeding minimum limits set out by the EU. Although they more or less agreed with the shift of emphasis from direct to indirect taxes, the experts did not agree with the tax mix between commodities. The fact that rates for alcoholic beverages rose only slightly (beer and small brewers were exempted by receiving a tax benefit) was regarded by many as a proof of the influence of strong interest groups. One opinion argued that in Slovakia not even a higher excise tax on alcohol than the one adopted would restrain its production. The experts think that at the same time it was necessary to launch an effort to stop illegal production and imports of alcohol, as well as tobacco products. A part of the experts would rather swallow a higher tax on alcohol, beer, tobacco and a tax on wine if the tax on mineral oils was kept down as the latter more affects the economic growth. As regards the consumption of mineral oils, the experts highlighted the fact that petrol prices can fluctuate, following crude oil price and exchange rate trends. The public perceived the increase in fuel prices particularly negatively, especially because it was adopted in the period when the exchange rate of the USD was lower than the long-term average. Should the exchange rate of the USD be adjusted to the long-term level or should the crude oil prices on international markets rise, there could be another fuel price increase that could have, in the opinion of several experts, much graver consequences. The increase in excise taxes, particularly the tax on mineral oils, could significantly push the inflation up.

Several experts were concerned about the fact that the year 2003 did not necessarily have to be the last one when non systemic measures would be used for offsetting deficits in the state budget, despite the recently adopted Strategy for Public Finance Management Reform (see page 17). The aim of this Strategy was to eliminate one-off measures resulting from a feeble emphasis on the need of appropriate quantification and sufficiently well-founded impact analyses in the process of the state budget compilation.

New Income Tax Act (Introduction of Flat Income Tax - 19%, Higher Tax Deductibles, Lump-Sum Tax Abolished, Introduction of 'Lump-Sum Expenses' for Tradesmen, Tax Assignment - 2%, Extra Tax Rate and Dividends Tax Abolished, Simplified Tax Legislature, Exemptions and Tax Reliefs Minimised)

On 28 October 2003, for the first time the Parliament passed the Income Tax Act, drafted by the Ministry of Finance (MF) as a part of the Tax Reform Concept for 2004 – 2006 (see page 27). The MF says it is the pivotal Act of the whole tax reform. Effective as of 1 January 2004, the new Act imposes a new flat tax rate on the income of individuals as well as corporations of 19%. Thus, the Act changes the progressive taxation of individuals and removes tax bands ranging from 10% to 38%. As regards enterprises, the Act decreased the currently used rate of 25%. Before, the income and corporate tax rates differed according to types of income, as a result of which there existed 21 different income tax rates and 443 different types of income.

Apart from the implementation of the flat tax, the Act also introduces a new system of tax deductible items. It increased the tax deductible per individual taxpayer to 19.2 times the life minimum (currently Sk 4,210), applicable as of January of a respective year, i.e. the tax deductible per a taxpayer for 2004 is Sk 80,832 (Sk 38,760 before). The same amount could by deducted by taxpayers whose spouses do not have their own income (Sk 12,000 before). Should a taxpayer's spouse earn an amount lower than the tax deductible, the taxpayer is eligible to deduct the difference between the deductible and the spouse's income. Third, after reaching the agreement with the Ministry of Labour, Social Affairs and Family of the SR, the tax deductible applicable to taxpayers' tax base in the case they have children (Sk 16,800) was replaced by the so-called tax bonus. An employed parent will be eligible to deduct Sk 4,800 a year directly from the amount of tax to be paid for each dependant child (see page 73).

The Act has also abolished the lump-sum tax (2% to 2.5% of gross income) as it was, in the MF's opinion, a non systemic element, the aim of which was to decrease the administrative workload of small businesses. In the new Tax Reform Concept, there was no room for it. Instead, tradesmen will be entitled to deduct lump-sum expenses of 25%, craftsmen 60%, of their gross income. Additionally, they will be allowed to deduct social security premiums paid as well as the tax deductible mentioned above. On the difference, they will then pay the income tax of 19%. The lump-sum expenses can however be used only by small businesses who are not VAT payers. Should a taxpayer opt for lump-sum expense method, he will not be obliged to maintain accounting records, nevertheless, no other taxpayers are given this option.

The income of basic activities of taxpayers who do not have to goal of producing profit (non profit organisations, incl. NGOs) will be exempt from tax. Their other incomes will be exempt to the amount of Sk 300,000, the amounts above this limit will be taxed at the above rate. The Act retains the Tax Assignment (although the MF initially proposed to cancel it as non systemic). Hence, individuals and legal entities will be allowed to assign 2% (1% before) of the amount of tax paid to a selected legal entity (non profit organisation) and community purposes. The new Act also abolished the mechanism of tax incentives that allowed taxpayers to decrease their tax liability in the value of a gift.

The Act also abolished the extra tax rate (varying from 5% to 25%) and introduced a withholding tax on selected types of income (yields from mutual funds, bonds, current accounts and cash vouchers) of 19%. The withholding tax system was also re-vamped - apart from some exceptional cases (e.g., non profit organisations, the National Property Fund of the SR, asset management companies, mutual funds, the National Bank of Slovakia) withholding tax paid during the year is treated as tax prepayment. This means that should the sum of prepayments be higher than the eventual amount of tax taxpayers will be entitled to receive the surplus back.

The new Act also abolishes withholding tax to dividends and profit shares (15%). This measure will save money for Slovak companies' shareholders, as the companies will now only pay the corporate tax of 19%. The Act excludes all incomes that have already been taxed and their further taxation would violate the principle of a single direct taxation. Hence, profit shares, paid from profits already taxed, will not be taxed when paid to beneficiaries, nor will they be taxed by these later. The provision only refers to income earned in 2004 but the EU Directive, which is superior to the Slovak legislation and valid as of May 2004, will provide this opportunity even earlier. The new Act also introduces changes to the supplementary pension insurance (DDP). Before, all benefits paid from this insurance were taxed at 10%. According to the new Act, only yields will be taxed at 19%, but not the insured persons' funds.

Apart from the aforementioned provisions, the new Act abolished a great number of tax exemptions and tax benefits (about 80%). The tax base calculation should also be simplified through a restricted scope of recognised tax deductible items. In 2004, employees' and tradesmen's premiums to the supplementary pension insurance (DDP) up to 10% (max up to Sk 24,000 a year) will not be taxed. After 2004, employees' premiums to the DDP will not be *recognised as tax deductible items. Additionally, employers' contributions to their employees' DDP also lost its status of non taxable items (for employees). Yet, they can still be deducted from the employers' tax base. This contribution will hence increase employees' tax base, however, it will not constitute a part of the base on which social security benefits are calculated. The Ministry of Finance and the Ministry of Labour are considering providing further incentives to voluntary pension schemes as of 2005 by implementing either tax benefits or state bonuses. The new Act also abolished all tax exemptions of revenues gained from the sale of securities and shares (with the exception of the securities acquired before the new Act became effective). Other exemptions abolished include: revenues of securities issued by the NBS, revenues denominated in foreign exchange, and revenues of mortgage bonds. The Act abolished the option of getting a tax loan as well as limit for the tax recognition of depreciation and leasing costs regarding passenger cars. The Act recognises provisions for bad debts as deductible items up to 100% of their value (debts overdue 12 months), however, it does not allow the businesses to write off these debts for good.*

The initially approved Act stipulated that the yields on pension savings would also be subject to flat taxation as from January 2004. These are savings that people will make within the so-called capital pillar of the pension scheme (fully-funded private pension scheme) in pension administration companies from 2005 onwards. The pensions from the first pay-as-you-go pillar of the Social Insurance Agency were not to be taxed. Later, the revenues (i.e. future pensions) were also exempt from taxation in the Act on Old-Age Pension Savings (see page 67). The proceeds from the sale of a flat or a house are also exempt from income tax subject to the fact that the seller owned the respective real estate and, simultaneously, this house or flat was registered as his permanent residence for at least two years preceding the sale (as before). The Members of Parliament decreased the period to two years from the originally proposed five years.

The new Act is much closer to the international tax law than ever before thanks to its definition and to precision. A marketing year (does not necessarily have to be a calendar year) could be used after the consent from the tax administrator. Besides, depreciation categories have been reduced to 4 (4, 6, 12, 20 years). The abolition of the fifth category should lead to increased investment in real estate. The Parliament also supported and prolonged the entitlement of beneficiaries to receive tax relief (Volkswagen, Bratislava, U.S. Steel, Košice) until the end of 2006, in compliance with the EÚ regulations.

The previous Income Tax Act produced 31.2% of the tax revenues. Several provisions in the new legislation will bring their fruits to the state budget only after 2004, however others will do so as early as in 2004. The overall impact on the state budget in 2004 was estimated by the MF at Sk 20.6bn (down by Sk 12.4bn in the case of income tax and by Sk 8.5bn in the case of corporate tax). This difference is to be offset by higher revenues from the flat VAT at 19% (see page 31) and by increased excise taxes.

A disagreement with the new Act was expressed by the opposition Members of Parliament who claimed that the Act will adversely affect the weakest social groups. The new Act was criticised by the representatives of the Confederation of Trade Unions of the SR who believe tax justice is embodied through progressive income tax, i.e., those who earn more pay more. They argue that the state will cease fulfilling its social role and will be replaced by a market state where there is no room for solidarity. Some opposition parties regarded the new Act as socially unjust, merely exacerbating social inequality. They also espoused the progressive taxation. Other critics argued that the new Act will back financially strong income groups, who do not need it, to the detriment of people with low earnings. Some critics proposed to return the Act to the Government for a revision and also to decrease taxes to handicapped people. The MF says that the aim is not to deform the Act and, hence, the problems of handicapped people should not be addressed in the tax, but in social security legislation. Other opponents claimed that the tax reform would increase the differences in the backward regions where the population is characteristic of low purchasing power. The major problem in these regions is expected to be the single VAT rate. Some members of the Parliamentary opposition agreed with the transfer of tax weight from direct to indirect taxes, but they argued that the change is proceeding very quickly. The representatives of the TU supported the changes to taxes but expressed a reserved stance towards the Government's tax policy, particularly to keeping tax exemptions and to sudden ad hoc *changes during the year (e.g., the increase of excise taxes in summer 2003 (see page 32)).*

The authors say that the primary aim of the Act was to simplify the tax system and tax legislation, permanently boost sustainable growth of the economy and inhabitants' life standard. The original tax system was, in their opinion, too complicated and the new system is to be more transparent and effective. The latter should also create room for fighting tax evasions as the motivation not to pay taxes will be much lower. The Minister of Finance, Ivan Mikloš, thinks the new Income Tax Act is a pivotal constituent of the tax reform and is convinced that it will bring a fundamental improvement of the business environment, as well as an increased motivation to work, save and invest. He also claims that the flat tax rate is fair: although it does not tax everyone equally, it is spread evenly across all types of income. The Act on the Flat Tax has removed double taxation of income, e.g. profits and shares on profits. Thanks to eliminating a number of exemptions, the Minister thinks, the Act is now going to perform its main, fiscal function.

A number of views agreed that the flat tax rate will bring the greatest benefits to taxpayers with above-average income and to inhabitants and families with children with below-average income. However, in contrast with the whole tax reform, the flat tax rate decreases the tax burden of all income groups. Conversely, the tax reform as a whole (including the single VAT flat rate, excise taxes) will tax more families without children and individuals with an average income between Sk 11,500 to Sk 21,000. This fact was hurled with criticism. Contrary to the unpopular parts of the reform, the Income Tax Act will raise the income of the working population and in the medium term eliminate the adverse effects caused by the higher VAT and excise taxes, which will thus not be so painful in the following years.

According to the MF, the lower tax should bring significant positives. The companies will retain more funds that could, e.g., be invested. It is also reasonable to expect a lower degree of tax evasions, increased investment (incl. foreign investment) and new jobs for the unemployed. In the Finance Minister's opinion, Slovakia will hence have an unrivalled tax system among all OECD and EU countries. Slovakia's competitiveness and attractiveness will rise. Even before the adoption of the core act of the whole reform, the country received recognition from reputed experts and institutions. The Slovak tax reform is, e.g., recommended by the IMF. Positive effects of the flat tax will bring fruits within this Cabinet's mandate, however, the forecasted significant betterment will not come immediately as the purpose of the reform is to bring benefits in the medium term. The Minister of Finance thinks that the success of the Slovak companies will also be reflected in the increased demand for workforce, which will raise wages and purchasing power. Many economists regard the flat income tax rate, together with the single VAT rate, to be the biggest change of the tax system since 1993. There were also voices calling for an even lower rate than 19%. The Finance Minister admitted that a decrease could be possible in the following years.

There are several countries in Europe with a flat income tax rate. Estonia implemented a flat tax of 26% in 1994 (additionally, as from 2000 the country does not levies any taxes on corporate profits reinvested in the country), followed by Latvia with 25% in 1995. In 2001 the flat tax of 13% was adopted in Russia. As of the beginning of 2004, it has also been introduced in Ukraine, also at the rate of 13%. The example of Estonia shows the positive impacts of flat tax on economic growth, purchasing power, corporate profits and the state budget balance (surplus).

The President did not sign the Income Tax Act and returned it to the Parliament recommending it not to pass the Act as a whole. In his mind, the implementation of the flat tax would be advantageous only for taxpayers with income over Sk 25,000 a month, which represents about 11% of all taxpayers. The increase of the tax deductible item will help only 13% of taxpayers with low income. The President further reasoned that the flat income tax hand in hand with the single VAT rate does not decrease the tax burden. The Parliament outvoted the President's veto on 4 December 2003.

The Income Tax Act became effective on 1 January 2004.

Evaluation of the Experts' Committee:

The new Income Tax Act introducing a flat tax rate of 19% received many positive attributes: one of the most important and most reformatory acts in recent years, a flagship of Slovakia's economic reforms, a fiscal revolution, a fundamental and brave act, the clearly most positive element of the tax reform, a unique and principal tax reform leading the right direction, etc.

The new Income Tax Act will have a positive influence on many areas. A relatively low tax and a simple tax system without complicated exemptions and provisions will provide the economy with new vigour, create prerequisites for a healthy economic growth, render stimuli for local business as well as domestic and foreign investment, help the labour market, and discourage taxpayers from tax evasions. The implementation of a simpler tax legislation and administration was necessary due to the work overload of Tax Authorities. The Act also increases the country's competitiveness. The tax reform, in particular, the flat tax has improved Slovakia's image abroad and generated many comments in renowned world media. The experts appreciated the shift of emphasis from direct to indirect taxes. Many also think the flat tax is fairer. A positive is the fact that after the implementation of the flat tax of 19% and increase of deductible items, no taxpayer will pay higher taxes than before.

Several experts deemed it possible that the tax rate was lower, which would provide Slovakia with an even larger competitive advantage in the region and will come close to the rates in some of the former USSR countries. The lower income tax rate should be implemented such that indirect taxes remain stable. At present, all taxpayers' savings from income taxes will be expended on higher VAT and excise taxes (Note: this does not apply to all social layers). Initially, it may be difficult to defend the flat tax if the revenues are lower than anticipated. A significant positive effect will however be manifested in the medium term, when it is expected that the purchasing power of the majority of the population will rise. The Income Tax Act dominates in its orientation *pro futura*.

There were contradictory views regarding the tax assignments, the abolition of the lump-sum tax and the implementation of lump-sum expenses for tradesmen.

New Act on Property Transfer Tax (Flat Rate Tax 3%, Inheritance and Gift Tax Abolished)

On 6 November 2003, the Members of Parliament passed the Act on Property Transfer Tax, which abolished the previous Act on Inheritance Tax, Gift Tax and Property Transfer Tax (the so-called tri-tax act).

Effective as of 1 January 2004, the new regulation retains the Property Transfer Tax that implements a single flat rate of 3% for both individuals and enterprises. When transferring the title to property, the tax base will be the agreed price, at minimum the price determined according to special regulations in force at the time when the freehold is entered in the Real Estate Register (the Decree of the Ministry of Justice of the Slovak Republic on Setting the General Value of Property). The new Act replaced the previous progressive rate (7 different levels), which depended on the price of a real estate, a family or other relation of the transferor and transferee. A prevailing part of the transfers fell in the third category (all enterprises and individuals except for relatives and persons who lived with the seller in the same household for at least a year). This category was taxed at 3% (the value of property transferred of maximum Sk 1m), 4% (Sk 1m to Sk 2m), 5% (Sk 2m to Sk 7m), and 6% (over Sk 7m). If property was transferred to close relatives, the rate was 0.5% (property value under Sk 1m) and 1% (over Sk 1m). Other family relatives were taxed at 2% regardless of the value of property.

The MF defended this measure by saying that there was absolutely no reason to divide the taxpayers into categories. The currently used system was, in the Ministry's opinion, unjust and very little effective, as the tax resulted in double taxation.

The new Act abolished the Inheritance Tax as well as the Gift Tax. The Tax Reform Concept, in its initial wording (see page 27), forecasted the abolition of all three taxes comprised in the tri-tax (Inheritance Tax, Gift Tax and Property Transfer Tax) as of 2004. The Minister of Finance, Ivan Mikloš, said that the abolition of the remaining taxes will depend on future state revenues after major tax changes have been implemented. The reason for postponing the abolition of all three taxes as initially proposed was the pressure of self-administration aimed at retaining the subsidies to regional cities for municipal public transport. It is the revenues from this tax that should be used in 2004 for financing the transport. The total volume of these subsidies is approximately Sk 1.7bn. According to the MF, the taxes retained should generate approximately Sk 900m. (The Framework for the 2004 State Budget, prepared by the MF, estimated the revenues from the tri-tax - if the tax reform was not implemented - of Sk 1.5bn).

The implementation of the flat Property Transfer Tax was opposed by the TU who promoted the idea of keeping the Inheritance Tax as well as the Gift Tax. According to the TU, the Inheritance Tax should be reintroduced with the closest relatives being exempt for the value of inheritance under Sk 4m. The critics also pointed out that the Slovaks would soon become "the most generous nation round the world", as instead of selling property, they will be giving it out as a gift. The Act, passed by the Parliament, was sent back to the Parliament by the President with the proposition to implement the rate of 0.5% for the closed family for property valued under Sk 1m. If the limit was exceeded, then the tax rate could be 3%. The President argued that the flat rate would adversely affect the first group of people, i.e. the closest relatives. The experts replied that property transfers within families represent only about 10% of all transactions and, hence, would not be that dramatic for the closest relatives. The Parliament outvoted the President's veto and passed the Act in its original wording.

The Act on the Property Transfer Tax became effective as from 14 January 2004 and should be in force until the end of 2004.

Evaluation of the Experts' Committee:

The experts think the new regulation stopped half way through. The abolition of the amoral Inheritance and Gift Taxes was the right thing to do, however, the Property Transfer Tax should have been abolished as well, according to the initial proposal to do so in the Tax Reform Concept. The Cabinet should not use self-government and municipal public transport as an excuse. Several respondents consider the action taken by the Minister of Finance to be too conservative. In regards to multiple taxation the experts do not see any reason why transfer of property should be taxed. The majority of the Experts' Committee voted for the abolition of the tri-tax that has no room in the new tax system. It has so far ensured only insignificant state revenue. Its net surplus (revenues minus administrative costs) is trivial, however, its negative impact on the real estate market huge - the prices for buildings and freehold are artificially pushed down and valuations are misrepresented so as to minimise tax. We can only hope that the politicians will keep their promises and abolish the Property Transfer Tax as of 1 January 2005. Meanwhile, people are likely to simply avoid it by "giving real estate to buyers for free".

The unification of the Property Transfer Tax rate is consistent with ideas already implemented in the income and corporate tax act. A single rate makes the whole system much clearer. One respondent considered the adoption of this Act to be an order from rich interest groups. Another asked why the previous system had to be changed - it would have been enough to adjust tax rates and the categories of taxpayers.

State Aid

State Subsidy of SKK 6.5 bn in Case of PSA Peugeot Citroën Investment in Trnava

In the first half of 2003, the Slovak Government approved the Proposal for Ensuring Tasks Ensuing from the Agreement on Investment Co-operation between the Slovak Republic, the City of Trnava and PSA Peugeot Citroën. The document lists key obligations arising from the Agreement and also recapitulates the measures taken in order to attract this investment, which was the largest in Slovakia at the time.

In the Agreement on Investment Co-operation (AIC), the Slovak Republic and the City of Trnava undertook to adhere to the project's time schedule, to form the company Trnavainvest, whose shareholder would be the City of Trnava, and to regularly inform the investor of the company's activities and the results. Besides other tasks, Trnavainvest shall ensure the acquisition of the freehold where the plant and its infrastructure are to be built (about 190 hectares for the car manufacturing plant and about 60 hectares for sub-suppliers). According to the AIC, the Investor is entitled to participate, in the form of technical supervision, in the performance of works and selection of sub-suppliers. After the acquisition of land is completed, Trnavainvest will be acquired by the Investor. However, it was not clear whether Trnavainvest would be sold or transferred free of charge. Additionally, the Government and the City of Trnava undertook to ensure equal conditions for future suppliers and to arrange a planning permission and building permit. The Government will also provide an investment grant for specific works and constructions, allowances for new jobs, and a tax relief. As tax reliefs are regulated by the European legislation to maximum 15% of a total investment, the entire state support must be approved by the European Commission. The AIC also binds the Slovak party to refrain from negotiating any other investment in the locality without the Investor's awareness thereof and his prior consent.

The Proposal has also set preliminary deadlines as to when specific infrastructure connections to the site should have been built. Temporary utility connections (drinking and service water, power and telecommunication networks) were to be built by late June 2003. The final utility networks were, according to the document, to be built two years later. The final gas connection should be in place by 31 May 2005. The end of 2005 is the deadline for completing a railway connection. The south and north road should be finished by 30 June 2005. One of the earliest required utility lines to be built is the sewerage system that was to be finished by 2 October 2003. Included among the works already performed were the assessment and selection of survey sites across Slovakia, as well as the elaboration of the project for the site Trnava-South, and its alternatives. The performed works also include connections between the utility lines and infrastructure, a proposal for removal obstacles on the site, and studies for connecting a road and railway system. The underlying documentation has been prepared for planning permission. Other works also include geological survey, geometric plans, and the identification of freehold owners. The costs of works performed have climbed up to Sk 10.5m. Preparatory works ensured that fundamental documents would be provided to Investors to enable a qualified decision and also created a foundation for the commencement of follow-up activities.

The tasks arising from the AIC will be fulfilled by several ministries. By the beginning of the school year 2003/2004, the Ministry of Education was required to ensure that the secondary vocational school in Trnava accommodates its equipment and curriculum to the foreign Investor's demands. By the end of 2003, the school, located not farther than 20 kilometres from the site, was expected to establish French sections. As early as 2003, the Ministry of Construction and Regional Development of the Slovak Republic was to fulfil a number of tasks associated with housing for citizens required to vacate their homes due to construction and also tasks related to future plant's employees. The co-operation of individual ministries and the supervision of the fulfilment of the tasks ensuing from the AIC will be co-ordinated by a Special Committee presided by the Minister of Economy. The Committee members will be: the Minister of Finance, the Minister of Transport, Posts and Telecommunications, the Minister of Labour, Social Affairs and Family, the Minister of Environment, the Minister of Construction and Regional Development, the Minister of Interior, the Minister of Agriculture and the Heads of the Office for State Aid, Office for Public Procurement, Geodesy, Cartography and Cadastre Authority of the Slovak Republic as well as the Mayor of Trnava.

The total of Slovakia's costs for meeting the obligation ensuing from the AIC are estimated at Sk 6.5bn. The return is expected within six months after the launch of the production, i.e. by June 2006. In 2003, the construction of the PSA Peugeot Citroën plant was to be financed from the state funds of nearly Sk 2.217bn (these funds were to be used for the acquisition of land and preparation of the site). In the first six months, the project required Sk 2.054bn, which the Ministry planned to set aside in the budget.

The Cabinet refuses to publicise the AIC in full, which was vehemently criticised by some NGOs. The Cabinet argued that the AIC is a business secret, the critics disagreed, saying that the fulfilment of the terms and conditions affect state property and hence the Agreement must be, pursuant to law, released to the public.

The City of Trnava won the PSA investment ahead of Žatec in the Czech Republic and Radomsko in Poland. The likely reasons in favour of Trnava were: location in the middle of Europe, a construction site with the area of 190 hectares easily accessible via a railway, motorway and navigable river, the opportunity to develop an industrial park for sub-suppliers in the vicinity of the plant, industrial background in the region, an available and educated workforce, as well as links to important markets where PSA is quickly expanding. PSA Peugeot Citroën commenced the construction of a new plant, with planned production of 300,000 cars a year, in September 2003. The French car manufacturer's basic investment will amount to EURO 710m (about Sk 29bn). The plant will directly offer 3,500 jobs and at minimum the same number of people will find jobs in associated suppliers' plants and in services. According to calculations, the annual production of the new plant will total approximately Sk 90bn to 100bn, with added value of 10bn. This means an addition to Slovakia's GDP of about 1% a year.

Evaluation of the Experts' Committee:

Despite more-or-less critical remarks, one group of experts approved the state support, whereas another one completely condemned it.

The state support to the investment by PSA Peugeot Citroën in Trnava convinced a relatively large part of the experts' committee of its importance. Its proponents believe that the PSA's investment will be extremely beneficial for the Slovak economy and will create new jobs. The experts emphasised that the state will recover the means invested within a very short period of time after the launch of the production. They also espoused the state support by the existence of the competitive environment in Central Europe, where all countries offer their prospective investors very similar incentives. Some experts criticised the volume of the state support. They mainly disagreed with the allowance for newly created jobs, tax relieves, as well as the planned measures in education. They agreed, however, with the state's support with regard to the infrastructure. There were also concerns that the state will not be able to fulfil all its promises or that the state support will be accompanied by corruption and siphoning of public resources. At the same time, there were voices calling for the change of the economic environment such that similar measures are rendered unnecessary in the future.

Critics pointed out the market deformation caused by similar measures. They think this is an inappropriate use of taxpayers' money. Every Slovak citizen will contribute to the construction of the PSA Peugeot Citroën's plan with Sk 1,300. Critics also doubt the recovery of the means as it is not possible to measure this quantity without bias and compare it interpersonally. They also condemned selective support for foreign investors. Therefore they believe it would be more just to adopt equal conditions, including the tax ones, for all enterprises. Critics argue the Government should prioritize improving the business environment in Slovakia in general. They believe a small portion of the aforementioned means should be used to eliminate Slovakia's greatest business barriers, such that investment would flow in the country without any further major incentives. Subsidising a "rich investor" is, in their opinion, a dangerous precedent, likewise freehold dispossession. „If the state had to be so generous to attract an investor to a well-developed region near Trnava, what will it have to offer to bring other investors to less developed regions?" asked the experts. Subsidies should be limited such that maximum amounts compensate the less developed infrastructure. If the Government's involvement is so extensive in the case of a site close to Bratislava, it encourages these expectations of weaker regions. The government officers probably disregard the demoralising effect of such decisions on other enterprises as well as on inhabitants in other regions. The experts expressed their disagreement with the fact that the state refused to release the exact terms and conditions of the AIC. They are also concerned about Slovakia's one-track orientation and dependence on the car manufacturing industry. If Slovakia's exports rely on a few major producers who additionally operate in a single industry, it may prove to be a risk factor in the days of recession.

In September 2003 the Slovak Government approved the Annex no. 1 to the AIC between the Slovak Republic, the City of Trnava and PSA Peugeot Citroën, which provided additional support of Sk 408.5m (see HESO 3/2003). The aim of the Annex was to help the French investor to accelerate the construction of the car manufacturing plant. Likewise, the AIC concluded in January that the Annex from September is confidential since it must protect business secrets. This was strongly criticised. In the opinion of the Centre for Environmental Public Advocacy (CEPA), the public is entitled to know where public funds go and how effectively they are used. The organisation has therefore submitted a petition to the Supreme Court of the SR against the Ministry of Economy. The petition objected to the violation of the free access to information as the Ministry refused to inform the public about the AIC.

A similar problem also occurred in the case of the agreement between the Government of the Slovak Republic, the City of Žilina and the car manufacturer Hyundai/Kia Motors (see the measure below). The Minister of Justice Mr Daniel Lipšic had an analysis elaborated which concluded that confidentially of the agreements on the provision of investment incentives is contradictory to the act on free access to information since these agreements deal with public finances. The analysis further concludes that if an investor demands confidentiality of an agreement or its part, a ministry (in this case the Ministry of Economy) is not authorised to undertake such an obligation, but must search counsel regarding what may and what may not be made confidential according to the law. Nevertheless, the analysis concludes that an agreement as a whole may not be rendered confidential, but some information that is to be kept confidential according to the law may be deleted from it prior to its publication.

Governmental Support to Hyundai/Kia Motors for the Construction of a Car Plant near the City of Žilina Amounting to SK 8.83bn (Contract between Hyundai and the Slovak Government)

On 4 March 2004, the Government of the Slovak Republic approved the Draft Investment Contract regarding the proposed construction of a car assembly plant near Žilina between KIA Motors Corporation, the Slovak Republic and the City of Žilina as well as the Investment Contract on the proposed construction of a car spare-parts and modules manufacturing plant near Žilina between Hyundai Mobis, the Slovak Republic and the City of Žilina. Following the conclusion of the investment contracts on 5 March 2004, in mid March the Government approved the Memorandum of Understanding between the Government and Hyundai/Kia Automotive Group, signed by the Prime Minister and the President of Hyundai Kia Automotive Group. The document expresses both parties' desires to implement and fulfil the provisions of both investment contracts.

The Investment Contracts has set legal obligations and duties, according to which both Korean companies, Kia and Mobis, will build a car manufacturing plant and a plant for spare parts for Kia. Furthermore, the Slovak Republic and the City of Žilina have undertaken to render necessary assistance and support to both companies, exert adequate effort so that all required permissions are granted, and endeavour to ensure generally favourable development of the business environment with a positive impact on the whole area of car and spare-parts manufacturing.

The new car manufacturing plant will be built approximately 10km from Žilina on the area of 166 hectares. The structures should be finished in late 2005 and in 2006. When the plant launches production, Kia is expected to directly employ 2811 people. The annual production of three different models is forecasted at 300,000 cars a year. The total investment of Kia is set at Euro 1.15bn (Sk 46.5bn). Of this amount, the car manufacturer, Kia Motors, will expend Euro 900m (instead of initially intended Euro 700m) and the supplier of spare parts, Hyundai Mobis, Euro 250m (instead of initially intended 190m). The concern plans to finance a half of the investment from its own resources, the remainder will probably be obtained from a European loan. Within the state support, Kia will not be granted any tax holidays as the support will rather be directed to the construction of the plant itself. Total public expenditures associated with this investment project will reach Sk 8.83bn. Of this amount, direct financial assistance should reach Sk 6.93bn. These funds will be used for the acquisition of freehold, procurement of fixed assets and allowance for the education of future plant employees. The proposed amount of the subsidy is consistent with the EU rules that stipulate that a state may offer an investor assistance totalling to maximum 15% of the total volume of investment (in this case Sk 6.975bn). The remaining tranche of the state support of Sk 1.9bn will be spent for the roads and infrastructure in the region.

Of the total state subsidy, Sk 2bn will be necessary as early as in 2004. After deducting tax effects, in the opinion of Ivan Mikloš, the Minister of Finance, this year it will be necessary to allocate Sk 1.5bn to 1.6bn to the project from the state budget. The Minister of Finance planned to get the money from the budgets of other ministries as the Members of Parliament, when voting on the budget, reduced the 2004 state reserve to Sk 260m. The exact state subsidy financing plan was to be approved by the Ministers in April. However, some members of the Cabinet disagreed with financing the subsidy from individual ministries' budgets, which was the most likely solution, because some anticipated projects will have to be cancelled and some ministries' budgets will be cut down. The Deputy Prime Minister of the Slovak Republic for the European Integration, Pál Csáky, expressed a contrary opinion to the cuts in the ministries' budget, particularly raising the issue that money allocated to healthcare, education and labour that had already been quite tight. The Minister of Finance acknowledged that during the year some of the funds from the ministries' budget will possibly be returned and if the state revenues show favourable development, the ministries will be allowed to expend the full funds budgeted. The Minister of Economy admitted that one of the possible solutions to financing Slovakia's obligations associated with the project would also be the increase of the fiscal deficit by 0.1% of the GDP (Sk 1.3bn).

Besides the investment incentives associated with the construction of the industrial complex, the Government has undertaken to build a motorway to Žilina. The car manufacturer's representatives were given a promise that the motorway will be completed by November 2006 (The Korean party initially requested October 2006 and the Government the end of the year). The finalisation of the 42-kilometre-long motorway section from Ladce to Žilina will, in the opinion of the Ministry of Transport, Post and Telecommunications, consume approximately Sk 22bn. There are three alternatives of financing: first, from the state budget; second, a bank loan with a state guarantee that will be taken by the construction company Doprastav; and finally, it could be financed from private funds, pursued by the Minister of Transport, Pavol Prokopovič. The most likely alternative however is a combination of all three options. The major hindrance to finishing the motorway on time is the terrain with a large number of bridges and difficult parts as well as buying freehold. According to the projects of the Slovak Road Administration, the motorway was originally planned to be put into operation no sooner than 2009 and it is presently not certain that it will be possible to meet the earlier deadline. As a part of the "indirect support" to the car manufacturer, Slovakia will also complete a railway terminal and modernise an airport in Dolný Hričov. Support was also offered by the City of Žilina, which decided, in order to respond to the needs of the car manufacturer, to build 1,000 to 2,000 flats, provide a policlinic, provide premises for training, support educational opportunities in the English language and ensure public transport.

As regards the land where the plant is to be built, it is necessary to buy 7,000 plots owned by 12,000 people, of whom all have been identified. To get the land ready for Kia Motors and Hyundai Mobis, the Ministry of Economy (MH) has established the companies Gov Invest I and Gov Invest II. Based on a Mandate, the purchase of freehold is also carried out by Žilina Invest. The freehold acquired and ready will then be purchased by the Korean company for a symbolic Sk 1. The price per square meter, initially estimated at Sk 95, has been much criticised by freehold owners, who thought it was much too low and requested minimum Sk 350. The freehold owners have therefore decided to submit a petition claiming that the land price in Teplička nad Váhom is at least Sk 360 per square meter (an estimate of an official appraiser). The dissatisfied citizens argue that the price of the best land may even be at Sk 500 to Sk 700 per square meter. The Minister of Finance has pointed out that the more money is used for purchasing freehold, the less there will remain for other purposes (fixed assets, allowance for future employees' education, etc.). The company buying the land, finding itself in the situation where there was too much information about various prices of freehold, approached the Authorised Institute of Engineering in Žilina and asked for assistance in dealing with the situation by approaching official appraisers who will later elaborate final opinions, by informing them of the rough price span from Sk 103 to Sk 126 per square meter of freehold in the given area. The Minister of Economy, Pavol Rusko, as well as the Mayor of Žilina, Ján Slota, threatened that the land will be dispossessed should the owners do not agree with the proposed prices.

The car manufacturer in Žilina is expected to decrease the unemployment in the regions, currently reaching 27,480 people. In three years, the plant plans to directly create 2,811 jobs, while other jobs will depend on suppliers' plants and their location across Slovakia. Slovakia's rivals in this respect are Poland and the Czech Republic. The experience of Volkswagen (VW) in Bratislava shows that suppliers in the vicinity of the plant will create up to twice as many jobs than the plant itself. It is likely that along with the car manufacturer, seven to ten direct suppliers will build their plants in a park located 60 to 100 kilometres far from Žilina. The volume of this additional investment has been estimated by the SARIO agency at roughly Sk 2bn to Sk 3bn. The President of the car manufacturer said that eight other firms that will supply the car-making plant will invest about Sk 10bn (USD 300m).

Based on the experience with VW, the economists think another indirect effect associated with the car manufacturer will be the rise of wages, which are likely to achieve the average level in the region and hence to increase the inhabitants' purchasing power. On the other hand, the economists point out that one of the main reasons why the Korean car manufacturer chose Slovakia was cheap workforce. Contrary to Bratislava with a relatively high price of labour, it is, in their opinion, unrealistic to expect a similar rise in average wages in Žilina.

The Minister of Finance has also highlighted the effect of higher growth of the economy and the living standard. After the launch of the production, the country's economic growth should increase by 1% of the GDP. Economic benefits of the plant for the Slovak economy were assessed by the MH using the so-called effect number method. By 2010 the benefits will amount to Sk 9.224bn and hence the state support will be returned within four years after the commencement of the production.

Attracting another major investor in Slovakia did not receive only a warm welcome (see also the investment made by PSA Peugeot Citroën in Trnava – page 40 and HESO 3/2003). Some experts point at high costs that will be covered from public resources. They do not regard a state support to investment as the best approach to boosting the economy. As the critics argue, savings of up to billions of korunas, if there were no subsidies to large investors, could help decrease corporation tax rates and hence, in the future, investors would be lured by a quality business environment *rather then by selective advantages. It is also necessary to take into consideration the alternative development of the regions affected, where similar investment will suppress other entrepreneurial activities. A large investment changes the economic structures of regions affected, which become cyclically dependant on a particular industry. Immediately after the approval of the arrival of a new strategic investor in Slovakia, the questions regarding stimuli to and transparency of such an investment were posed. They mainly concern the maximum limit, beyond which supporting investors is no longer worthwhile. Critics also pointed at the unwillingness to publicise agreements with investors, which they deem inappropriate as state subsidies are paid from a public pocket. The Minister of Economy said that the use of public money for the state support to this investment will be released so that it can be under public scrutiny. Business secrets however will remain protected as their publication could help competitors.*

The Korean manufacturer will build its first plant in Europe in Slovakia. Its whole production will be aimed at the European market, where last year, with 150,000 cars sold, Kia's sales rose by 40%. One of the drivers to move the assembly plant to Europe was the attempt to avoid a 10% customs duty on exports to the EU. The initial impulse however was the rising sales and market share on the Continent. The company is the fastest growing brand in Europe and one of the fastest growing brands around the globe.

Initially, apart from Slovakia there were two other countries competing to attract the investor, of which, after the Czech Republic lost the game, remained only Poland and Slovakia. The decision to invest in Slovakia was taken in early March after the Korean company analysed the terms and conditions offered by each of the countries. The Prime Minister, Mikuláš Dzurinda, said that Kia's decision for Slovakia was primarily affected by the reforms in taxes, social policy, healthcare and the quality of the workforce. The car manufacturers' top representative said that the decisive factor was the cheap and qualified workforce. Additionally, an important role in the decision-making process was also played by the fact that the Slovaks are less prone to strikes.

Rough estimates show that after both car manufacturers - PSA Peugeot Citroën in Trnava and Hyundai/Kia in Žilina - commence production, Slovakia will produce about 1.2 million passenger cars a year. In absolute figures, Slovakia will become the tenth largest producer in the world and the leading car manufacturer per capita.

Evaluation of the Experts' Committee:

The investment incentives provided by the Slovak Government were, without any doubts, one of the main reasons why Slovakia won another major foreign investment in the automotive industry. The arrival of Kia to Slovakia was regarded by the Experts' Committee to be a great success. It is good PR and an excellent signal to abroad communicating the attractiveness of the Slovak investment environment. The extensive investment will be beneficial for the whole Slovak economy and create new jobs in the region with quite a high unemployment rate. After the commencement of production, the positive effects arising from the bigger economy's output will multiply. In the opinion of one respondent, by attracting this extensive investment, the Slovak economy's position changes in that it will no longer be necessary to attract major foreign investment at any cost, as was the case of Hyundai/Kia Motors.

Several experts emphasised that the state will recover the money invested in a relatively short period of time after the plant commences production in the form of increased tax revenues, lower expenditure on the unemployed and overall development of the region. The state support was also partly defended by the fact that all Central European Countries offer similar incentives to attract foreign investors. Some experts criticised the amount of the state support that seemed exaggerated to them. They commented on this fact by saying that "we are more catholic than the Pope". As was the case of all other selective incentives, it would be appropriate to provide a better-founded reasoning and the cost/benefits analysis of means expended compared to its alternative use. The provision of the state support will, in the short term, narrow the space for decreasing taxes. One respondent however believes that the argument that the taxes could have been cut by the amount of the support, which would create space for spontaneous inflow of investment, is naïve. Arguments can also arise regarding the costs for the accelerated construction of the motorway as well as its financing.

The main problem, as critics see it, is rooted in selective support to large foreign investors, which is unsustainable in the long run. This gives rise to a negative precedent that Slovakia will support some private businesses more than the others and, furthermore, it will be paid by taxpayers. A more systemic support would be to create generally favourable conditions for investment and making business, which would improve the whole business environment, e.g., the elimination of corruption and barriers hindering business development, the decrease of taxes and other contributions, ensuring law enforceability, etc. It is always risky when a state, acting from a position of strength, gets to the forefront of entrepreneurial activities, as it deforms the market. For example, we may point at the dispossession of the freehold for the plant.

An important aspect regarding investment incentives is the transparency of the use of public finances. It is therefore necessary to publicise the whole agreement.

Some respondents think it is doubtful which resources should be used as the harvest will mostly be reaped in one region. They said that this kind of a state support should not be to the detriment of the Central and East Slovakia's regions which struggle with a high unemployment rate.

Buying out the Slovak Railway Companies' Debt by the Government Amounting to Sk 21bn

On 2 July 2003, the Cabinet approved two bills drafted by the Ministry of Transport, Posts and Telecommunications (MDPT): Draft Settlement of Financial Relations between the Railway Company (ZSSK) and the State and Draft Plan for Consolidating the Railways of the Slovak Republic (ŽSR), including buying out the ŽSR's debt by the state. Hence, as from 1 January 2004, the debts of the ZSSK and ŽSR should have been decreased by a total of Sk 21bn. The debt restructuring was carried out by transferring, at the beginning of 2004, a part of both companies' liabilities to the state debt.

*According to the documents as approved by the Cabinet, the state took over the responsibility for the **ZSSK**'s debts that were guaranteed by the state in the amount equal to the company's receivables from the state for the so-called public-interest services (Sk 7.32bn). Of this amount, Sk 3.17bn were generated in the period 1997 and 2000, and Sk 4.15bn was produced in 2002.*

*From the **ŽSR**, the state assumed a similar debt of Sk 13.6bn, comprising a receivable from the state for the public-interest services of Sk 13.11bn for 1994-2001 (of which Sk 6.9bn is interest on overdue payments; in January 2003 the receivable was additionally decreased by a payment from the National Property Fund (FNM) of Sk 1bn) and a receivable of Sk 1.52bn for 2002. Besides taking over the debt of the ŽSR, the Cabinet also agreed to write off the returnable financial aid of Sk 528bn dating back to 1998.*

The companies' receivables originated from the fact that the state did not meet its obligations arising from the companies' performance of public-interest services, which the state used to offset by providing state guarantees. According to the Minister of Transport, Pavol Prokopovič, the state will also help the railway companies in 2004, when apart from paying up the guaranteed debts, it will also contribute to investment of Sk 2.5bn. Without making this investment, the Slovak railways could be excluded from international railways. The debt restructuring of the ZSSK could end in 2007 and of the ŽSR in 2009 or 2010. The Minister of Transport said that after the debt has been restructured, both companies will become credible partners for banks.

The documents approved also contain a scenario of the ZSSK's financial development and additions to the ŽSR's Financial Model until 2007, which has been prepared together with the Ministry of Finance. The latter has also become the ŽSR's Financial Plan until 2007. Its underlying parameters include the constant length of tracks, forecasted inflation based on the NBS's analysis, the scope of public-interest services according to the contract effective from 2003 and fees at the level of the Price Decree of the Ministry of Finance of March 2003. Maintaining the level of transfers from the state budget at the 2003 level, it will be necessary, according to the documents, to decrease the volume of services. The Ministry of Transport initially requested that the funds for public-interest services are raised by nearly Sk 1.4bn (from Sk 6.6bn to Sk 7.9bn). The ministry of Finance rejected this request. The Ministry's officials said that once the debts from the past were restructured, both companies must prove that they can run their business efficiently.

In order to avoid a further generation of debts, both companies' investment was suspended, including the one that have already been started. The only investment they can continue using is the one channelled to railway safety systems and to obtaining funds from the EU.

Opponents to this measure criticised the Cabinet for restructuring both companies' debts without the Minister preparing a project for austerity measures and company restructuring. Critics further argued that certain elements are missing: a change to the companies' internal finance as well as changes on specific posts, including control mechanisms that would ensure effectiveness of the Cabinet's action after the debt restructuring.

As regards the ŽSR, the new CEO announced a ŽSR restructuring and consolidation plan that will be met by means of austerity measures aimed at stabilising debts and decreasing costs. As a consequence of on-going organisational changes, about 100 to 200 employees were expected to be laid off in the following months from the ŽSR Headquarters and nearly 300 employees were to be made redundant as a consequence of merging 25 Regional Offices (Railway Administration) into 4 Regional Managing Offices in Trnava, Žilina, Zvolen and Košice. In the future, through transferring non-core activities to new owners, about 4,700 people will change their employer. Hence, the number of ŽSR employees will fall again (in 2003 the ŽSR employed 22,106 people).

By earmarking the so-called non-core activities, the CEO plans to save Sk 500m a year. There are also plans to reduce the fees for using the railway network, the aim of which is to improve the company's ability to compete. Following this, as from 1 January 2005 the administration activities should be set aside from the track maintenance, the purpose of which is to create a business relation between these two activities. The new CEO's ambition is to ensure that the ŽSR's debts stop rising and that its railway network is administered efficiently. He hopes that the company will achieve a break-even point within three to four years.

Evaluation of the Experts' Committee:

The proposed and approved method of the railway companies' (ŽSR and ZSSK) debt restructuring has been received with much dissent by the experts. Each state aid and state ownership pose the so-called moral hazard ("Am I producing losses? It does not matter! The state will pay for it.") and give rise to similar demands from other entities. Any debt transfer onto the state, and thus onto taxpayers (and, generally, any state aid), should be limited in duration and tied to the achievement of measurable results and decreasing in scope. Hence, also in this case, the debt restructuring should include a long-term strategy comprising a reform of both companies, the outcome of which should be results in black figures. The reform should also ultimately deal with the relationship between the state and the railways companies such that both parties will honour their obligations. Any further guarantees for the companies' debts or transfers of companies' debts onto the state should be forbidden. Taking over the debt of the railway companies by the state before a fundamental restructuring of both companies that would stop the companies from generating further losses was regarded by the experts as pouring money down the drain. Several experts also presented the opinion that dividing the railway routes (ŽSR) from the transport company (ZSSK) has not brought any fundamental change and further transformation of the railway companies is lagging behind the original intentions. A solution could be rapid privatisation of both companies.

On the other hand, several experts considered the debt restructuring of the ŽSR and ZSSK to be justified as the state owed the railway companies, and also to be inevitable and expected as it was clear long ago that the railway companies were unable to pay back the loans guaranteed by the state from their own resources. It is deplorable that the state-owned railway companies borrow money at higher interest rates than the state could and then receive state guarantees. The approved restructuring was a type of heritage that had to be paid for, as in the past there were approved generous compensations for public-interest services that were supposed to disguise costs for "railway graft", to which the state responded by not paying for the debts and postponing the whole matter.

There was also an opinion that the politicians were simply not courageous enough to admit that many highly unprofitable tracks should be terminated, including significant reductions to local passenger transport in the places where there are alternative coach lines. Until the state stops providing aid to two parallel means of transport at the local level (railways and road), the Slovak taxpayers will have to carry on subsidising, by billions of *korunas*, half-empty coaches and half-full trains. Restrictions to state subsidies to long-haul railway and local coach transport could save several billion *korunas* a year.

In 2003 the ŽSR produced a loss of Sk 956.5m, which is an improvement by Sk 2.11bn as from 2002. The original restructuring plan for 2003 had forecasted the loss of Sk 70m, however, after initial austerity measures, the ŽSR business plan was adjusted last summer and the loss was upgraded to Sk 3.5bn. As of 31 December 2003, the ŽSR's liabilities amounted to Sk 49.868bn, whereas receivables to nearly Sk 15.467bn. As of 1 January 2004, the ŽSR's receivables from the state of Sk 13.6bn for public-interest services were offset with the state guarantees for ŽSR loans of the same amount. Hence, the ŽSR's total liabilities as of 1 January 2004 dropped to Sk 36.2bn.

In 2003, ZSSK generated a loss of nearly Sk 4.7bn although the plan forecasted a profit of Sk 267m. In 2002, the loss of ZSSK was Sk 298.6m (original plan: the profit of Sk 72.4m). As of 1 January 2004, the ZSSK employed 18,979 employees. According to the ZSSK's statistical data, in 2003, the company reduced the number of its employees by 1,800. In 2004, the ZSSK's business plan forecasts further layoffs of 290 people.

Direct Payments to Slovak Farmers Amounting to 52.5 Percent of EU Level

When discussing the 2004 State Budget Act (see HESO 4/2003), the Members of Parliament also approved the final amount of direct payments to farmers at the level of 52.5% of the EU Member States (25% of the amount is paid by the EU, 27.5% by the Slovak Republic). At face value, this will represent an additional Sk 340m on the amount proposed by the Cabinet (50%). The additional increase by 2.5 percentage point will drain Sk 70m from the Cabinet's reserve, Sk 170m *from the Defence Ministry, Sk 30m from the funds initially aimed at providing state premiums to building society savers and Sk 70m from the Ministry's of Agriculture reserves. The level of direct payments in 2004 is 52.5%, which is lower than the one permitted by the EU (55%) (see Conclusion of Accession negotiations with the EU – HESO 4/2002) and than the one requested by Slovak farmers. According to the Cabinet's calculation, an increase by each percentage point requires an additional Sk 136m. Hence, in 2004, the Slovak farmers will receive direct payments of approximately Sk 3.74bn as well as Sk 3.4bn from the EU coffers.*

For the Slovak agriculture, the 2004 state budget allocates a total of Sk 18.577bn. The national resources will channel Sk 11.817bn to the farming sector, whereas Sk 6.761 will be obtained from the EU. The largest sum of the EU budget is determined for direct payments to farmers so that these amount to a total of 52.5% of the payments to the current EU Members.

Farmers were also unsatisfied with the compromise outcome. They appealed to Members of Parliament that these approve maximum direct payments, i.e. 55%. They did not accept the arguments of the Minister of Finance, Ivan Mikloš, that each increment to direct payments above 50% would mean less funds to other areas. The farmers' representatives are not concerned about competition in the EU market. Rather, they are concerned about unequal conditions in the competition between the Slovak farmers and farmers in other Member States, including the new members. The Chair of the Slovak Chamber of Agriculture and Food (SPPK) expressed his regret over the outcome of the voting, but he understood it was a compromise that will not be changed. He argued that in the current situation the Slovak agriculture needs every million. It is in the interest of Slovakia, as the critics say, to ensure an equal position of its farmers relative to farmers in neighbouring countries. The farmers were also supported by one of the ruling parties. Prior to voting on the state budget, the Minister of Agriculture, Zsolt Simon, proposed to increase the direct payments using the funds saved from the unemployment support. Nevertheless, the Minister of Finance thought the subsidy of 50% of the level in the EU Member States was exorbitant. He underlined the reserved stance of the MMF, whose Slovak staff concluded that the rise of subsidies in the 2004 budget was regrettable and that it was not likely that it will accelerate the growth of the sector.

The draft budget for 2004, compiled in July 2003, counted on direct payments to farmers at the level of 40%. In September the Government promised to farmers direct payments of up to 45% of the EU average. When the 2004 budget was discussed by the Cabinet, the level of direct payments was again raised, to 50%.

Of the other new EU Members, Hungary and Poland decided to make direct payments to their farmers at the maximum possible level, 55%, and the Czech Republic adopted the level of 48%. The observers say that when comparing the volume of the resources granted to farmers in individual countries, the most important aspect is the relative amount of the incremental increase as from the previous year. In Hungary, in 2004, the farmers will receive approximately 26% more funds than the year before, whereas the Slovak farmers, with direct payments at the level of 52.5%, will receive 45% more than in 2003.

Regardless of the approved amount of payments, the funds will be provided to farmers only if the Integrated Administrative and Control System (IACS) is fully functioning. The system relates to the interconnection of databases monitoring activities in agriculture. The EU is very strict regarding the supervision of the land subsidised. However, Slovakia is lagging behind in the system development, which was also reproached by the European Commission in its monitoring report. Based on the system, the Agricultural Paying Agency will make payments of the subsidies from the local as well as the international sources.

Historically, direct payments, as a constituent part of the Common Agricultural Policy, are a compensation for the decrease of guaranteed prices. The EU Summit in Copenhagen in December 2002 (see – HESO 4/2002) decided that the basic level of direct subsidies to farmers was the same for acceding countries, amounting to 25% of the level of the support received by the original Member States' farmers. In the following years, direct payments to new Members will rise. In the first year after the accession, the initial level will be 25% and will rise by 5 percentage points in each following year until 2006. The full level of direct payments will be granted to new members after a ten-year transition period. As the Common Agricultural Policy is expected to be reformed in the future, the avenue that the European subsidies will take is not clear today. Likewise, 5 percentage points will be added each year to the maximum limit, to which the farmers of the new Member States will be entitled, including the domestic direct payments.

Evaluation of the Experts' Committee:

The lingering inefficiency of the system of subsidies to agriculture in Slovakia and the EU makes high subsidies to farmers doubtful. The logic of subsidies that allow farmers to sell their expensive produce for a cheaper, more competitive, price, is incorrect and, at least, unsustainable. Disregarding the fact that direct payments are also made by other, more developed, European countries, the experts admit that it is a non systemic and difficult-to-conceive measure, subsidising a private sector.

The experts believe the EU Common Agricultural Policy is built on feeble foundations and it regularly yields to the agricultural lobby. Taxpayers then finance an entity that brings them no benefit whatsoever. The new Member States has only adjusted. Critics say that it is difficult to believe how such a relatively small group of people producing only a fractional added value, with growth potential at nought, can acquire selective advantages.

Experts say that there is no guarantee that a soaring rise of subsidies to Slovak farmers (year-on-year increase by 45%) will lead to a fundamentally positive turnaround in their business and to a renewal of their equipment. Conversely, the threat posed is that inefficient farms will obtain further resources that will only prolong their agony. Paradoxically, instead of increasing the farmers' ability to compete in the subsidised EU market, the subsidies may eventually weaken the farmers' efforts and motivation to increase their production efficiency and their ability to compete. Should an efficiency analysis of the funds channelled to agriculture be conducted, it would be possible to see, as critics say, the nonsensical character of this decision much more clearly. Furthermore, compared to the parity of purchasing power, the level of direct payments to Slovak farmers correspond to 120% of the EU average and is higher than that of other Visegrad countries.

Some experts suggested that it would be better if the funds used for direct payments to farmers were rather used in the education system, infrastructure or more sophisticated production, which would, in their opinion, be more advantageous for Slovakia from the strategic point of view. They think that the decision to increase the direct payments to 52.5% of the EU level was a political, compromising and populist one. It is only a small remedy that the Slovak Government and Parliament did not take the opportunity to approve to levelling off the direct payments at the maximum level of 55%. The new Member State's farmers will not have the same starting line as their older EU peers, but they will have an opportunity to benefit from a better efficiency (economies of scale) and incomparably lower input costs.

One respondent said that in the case of more vigorous control of the claim to the direct payments, the subsidies could have even been raised above the maximum limit.

In its Framework for the 2005 State Budget, the Ministry of Finance forecasts that the direct payments to farmers will amount to 40% of the EU level (original proposal of the MF was 45%). The Minister of Finance, Ivan Mikloš, argues, however, that agriculture is the sector that contributes to the country's economic growth the least. Slovakia should, in his opinion, invest public finances more sensibly. According to the MF SR, although the country's part of the subsidy is lower than in 2004, the total amount of the subsidy to farmers will rise by Sk 1.6bn on 2004. The Framework further says that due to high contributions from the common EU budget, the Ministry on Agriculture can count on total resources of Sk 20.3bn in 2005, Sk 21.7bn in 2006 and Sk 23.2bn in 2007.

The Ministry of Agriculture disagrees with the MF's proposal and requests maximum level of direct payments for 2005, which is 60% of the EU average (EU 30% + SR 30%). The Minister of Agriculture, Zsolt Simon, assumes that the situation will develop similarly to the situation in 2003, when the direct payments were gaining percentages little by little before they were finally approved by the National Council.

Business and Investment Environment

New Act on Companies Register (Certificate of Incorporation within 5 Days, Implementation of Standard Forms, Policy Moved from Judges towards Higher Judicial Officials)

Adopted by the National Council of the Slovak Republic (NR SR) on 28 October 2003, the new Act on the Companies Register is based on the Proposal for Measures to Improve The Efficiency of the Companies Register approved by the Cabinet in April 2003 (see HESO 2/2003). The purpose of the new Act, drawn up by the Ministry of Justice of the Slovak Republic (MS SR), was to create prerequisites for making the operations of the Companies Register more efficient, including its legislative framework and technical background, and to implement a part of comprehensive institutional and organisational changes to judiciary aimed at accelerating judicial proceedings. Additionally, the need for the act also arose from the harmonisation of the Slovak legal code with that of the EU.

Evaluation of the previous legal situation:

The Companies Register and its administration were primarily regulated by the Commercial Code (OZ) and by Civil Proceedings Rules (OSP). In the opinion of the MS SR, the previous legal framework regarding the Companies Register proceedings caused severe problems that are summarised as follows:

- *it did not set terms for taking a resolution on an Application for an Entry in the Companies Register (hereinafter only "the Application for an Entry"), which resulted in several-month delays in registering companies without applicants having the right to appeal or to directly communicate with a respective judge;*
- *ambiguity with regard to requirements for the Application for an Entry, as well as the type and form of documents that applicants were obliged to enclose with the Application;*
- *twofold interpretation of the law in the case of declarative entries – inconsistency between an entry and a company's decision;*
- *ambiguous specification of the date of performing the entry;*
- *inconsistency between the Slovak Government's Regulation on the Commercial Bulletin and the amended Commercial Code, wherefore the former required less information to be disclosed than the latter, while the former completely omitted any provisions regarding the disclosure of information on the safe custody of documents in the Collection of Instruments;*
- *ambiguity of the provisions of the Companies Register especially in terms of the legal effect of the entry of some documents (constitutive and declarative effects);*
- *a significant time span between a Register Court's resolution on the entry contents and its publication.*

The Background Report on the new Act stated that a sluggish, and in some cases highly non-transparent, process of approval and formal checks of the entries in the Companies Register laid a tremendous workload on Register Courts and their judges, which to a substantial degree prolonged proceedings. In the Ministry's opinion, the Companies Register in its original form was a major hindrance to economic development and adversely affected the willingness of foreign entities to invest in Slovakia. The only possible way to remove some of the aforementioned negatives was, in the Ministry's opinion, to transition to a new Companies Register administration system, which should, by means of its inherent principles and mechanisms, ensure prompt and quality administration of the Applications for the Entry and guarantee a transparent and predictable action of all parties involved. This aim should have been achieved by the Act on Commercial Registrar by incorporating the following principles.

Basic principles of the new act

The new Act on the Companies Register leaves jurisdiction regarding the Companies Register administration with the courts, which (1) significantly reflects the historical context and legal tradition of the Slovak Republic, (2) ensures, in the Ministry's opinion, a smooth transition to the new system of the Companies Register administration, (3) corresponds to the requirement for an efficient solution (as the solution does not include transferring the Companies Register administration to any other body or institution) and (4) concurrently reflects an important legal coherence and necessity for informational links with other judicial proceedings.

The most important change effected by the new Act impacts the character of the registration process. The Act on the Companies Register introduced the new term, "registration", which encompasses the procedures of entering documents in the Companies Register, entering changes to these documents and deleting documents from the Companies Register. Contrary to the *previous regulations regarding the Companies Register, this procedure does not have a character of civil proceedings, but is included in other judicial actions, as defined by the Civil Proceedings Rules. The fact that the registration of documents is no longer regulated by the Civil Proceedings Rules allowed its transfer from judges' jurisdiction to higher judicial officers' discretion. Hence, according to the new Act, judges will only get involved in the registration process in the case of a dispute, i.e., where an applicant would seek a remedy when registration of, changes to, or deletion of documents would be declined. According to the Civil Proceedings Rules, making decisions on objections falls within the courts' jurisdiction. Another remedy (there has been none so far) for an applicant submitting an Application for an Entry is an appeal against a resolution by which a judge, having examined them, declined objections.*

According to the new Act, Applications for an Entry in, Change in or Deletion from the Companies Register will only be checked for their formal consistency, i.e., a court will only examine the completeness of the Application for an Entry, including its Annexes, to confirm the consistency of the information in the Application with that in the Annexes, as well as compliance with other prerequisites explicitly stipulated by law (e.g., whether an applicant has paid a judicial fee), rather than examining the Application's contents, as before (the so-called factual check). The responsibility for documents entered in the Companies Register will be borne by a respective applicant and a person who authorised or prepared a document. In the case of documents of special significance, e.g. initial entry of a company or entry on a company take-over, merger or division, factual checks to a certain extent will remain (i.e., the contents of the Application for an Entry and that of documents will be scrutinised), as a court must verify that other prerequisites strictly defined in the act and required by EU Directives have been met.

As opposed to the previous procedure, the outcome of a registration proceeding is either a negative resolution (if one or more prerequisites for the entry have not been met), or a company is directly entered in the Companies Register (if all prerequisites have been fulfilled), having the effect of a positive resolution on the entry. Cancelling the latter resolution (i.e. the positive resolution) has removed a time lag between the passing of the resolution, its issuance and factual entry in the Companies Register, whereby the time that elapsed between the entry in the Companies Register, effective from a legal point of view, and the publication of the information entered in the Companies Register in the Commercial Bulletin has shortened.

Another innovation introduced by the new Act is a standardised form of the Applications for an Entry and a stipulation of an exact list of supporting Annexes. In this respect, the Act will have to be followed by an execution regulation (a decree prepared by the Ministry of Justice). This modification is expected to remove the existing legal uncertainty of applicants submitting an Application for an Entry regarding essential elements of the Application and Annexes thereto, as well as the ambiguity of requirements imposed by different Register Courts in terms of the type and form of Annexes to be submitted. The use of prescribed forms and setting an exact list of Annexes will also ease the Courts' role in terms of checking whether or not an applicant has met prerequisites for the entry in the Companies Register, as stipulated by law. The MS SR believes that after properly filling in the forms by applicants, the whole registration process will promptly be accomplished. The Ministry's aim is to make it possible for applicants to carry out all changes in the Companies Register via internet.

The Act on the Companies Register also sets a fixed term of 5 working days for making an entry, which aims at creating conditions for a prompt administration of the applications (subject to submitting a complete and correct Application for an Entry as well as Annexes thereto) and at the same time removing the legal uncertainty experienced by applicants and third parties, which used to arise from lengthy Companies Register proceedings.

In the opinion of the MS SR, the Act on Companies Register will significantly improve the prerequisites for better relations between the business community and the Companies Register and will help create suitable conditions for business development in terms of desirable economic growth. The Ministry also believes that the new Companies Register administration system will also contribute to making the Companies Register's activities more transparent, and, especially from its users' point of view, to accelerating and simplifying the whole procedure. Hence, it should make it easier to start a business. Simpler procedures should help increase interest of foreign investors in Slovakia. The new Act will therefore make Slovakia's business environment more competitive, as it will create better conditions for developing entrepreneurial activities of foreign entities. The changes to the Companies Register will, in the opinion of a part of an expert community, help achieve its primary aim - to become a publicly available list furnishing information on companies in real time. The introduction of the standardised forms for reporting changes in the Companies Register, transfer of authority from judges to higher judicial officers and the obligation to make an entry within 5 days will, in experts' opinion, have a significantly positive effect upon the registration, as well as other, procedures (simpler and shorter) and on the whole business environment.

The amendment of the Act on Court Fees also affected some fees related to Companies Register proceedings. The fees for the application for the initial entry remained unchanged, for instance, Sk

20 thousand for the entry of a joint-stock company, Sk 10 thousand for other legal entities and Sk 5 thousand for natural persons - entrepreneurs. Different fees have, however, been introduced with regard to changes to documents in the Companies Register. So far, it used to be Sk 500 for each change, in some strictly stipulated cases courts required a 200-crown stamp. The new Act introduces a single fee of Sk 3000 regardless of the number of changes a person wishes to make at one time. If applicants ask for more changes within a single form, they will charge one fee only. Contrary to the past, there will be no fee on publishing information entered in the Companies Register in the Commercial Bulletin.

The Act on Companies Register became affective on 1 February 2004.

Evaluation of the Experts' Committee:

The new Act on the Companies Register has long been expected. Insufficiently defined rules in the past led to intentional obstructions and gave rise to widespread corruption. The experts think this is the way an effective support to business and investment should look. If the state wants to assist the business sector, it should do so by limiting bureaucracy and increasing effectiveness, including promptness of civil servants. The more regulations like this that Slovakia drafts, approves, and implements, the fewer tax incentives and other benefits will it need to lure prospective investors. Systemic changes are cheaper, more just and, in terms of long-term business stimulation, more effective. The Act will, in the experts' opinion, better the business environment, further the application of Corporate Governance principles, enhance flexibility, increase transparency, decrease corruption, and facilitate and accelerate the entry of new businesses in the market. Prompter administrative proceedings are cheaper for both businesses and the state. Promptness and barriers to company formation are among the critical criteria that foreign investors use to closely monitor investment potential. The Act may also help remove unfair practises arising from insufficient functionality of the former Companies Register in Slovakia.

The Act has also introduced a correct principle - if there is no dispute, the matter should not be dealt with by a judge. The approach of using higher judicial officers for making entries in the Companies Register is a suitable alternative.

The experts' committee hopes that the term of 5 days for making entries will be adhered to. If Slovakia succeeds in putting the act into practise without making compromises, it will be a small miracle that could serve as an example to other countries as well. The functioning of the Companies Register in Slovakia could thus come closer to the way Companies Registers work in Canada, New Zealand, Denmark, Great Britain or USA - the countries were Companies Registers are the most effective.

One expert pointed out an unclear mechanism for checking the accuracy of the information entered. Another one highlighted the fact that the Collection of Documents, a key source of business information, is being neglected. Courts are, in his opinion, benevolent to those who do not adhere to their obligations to the Collection of Documents.

One expert also suggested that the privatisation of the Companies Register's services is worthy of consideration.

Following the first phase of making the Companies Register more effective, the so-called legislative and organisational stage, another stage, technical and organisational, should follow and include all necessary measures for ensuring links between individual Registration Offices and the Central Register and for developing a publicly accessible central online database of the Companies Register. Next, information in the Companies Register should be made available via internet in a legally binding form such that it could be guaranteed that the information on internet corresponds to that entered in the Companies Register, whereby publishing information in the Commercial Bulletin could be abolished. Following the change to the legislation framework of the Companies Register, the second phase should also include the establishment of Public Relations Companies Register Offices at Register Courts, where applicants could make an entry immediately, subject to having a complete Application for an Entry, including Annexes. The third stage of the change to the Companies Register, electronic communication, will be aimed at creating all prerequisites for developing the Collection of Documents in an electronic format and at developing a platform for electronic communication of all parties involved. The electronic communication will use electronic signatures as a means to verify the parties' identity. This stage is expected to be completed in 2006.

Real Estate Register on the Internet (Authorised Access, Paid Services)

On 1 February 2004 the Institute of Geodesy, Cartography and Real Estate Register of the Slovak Republic (ÚGKK) together with the Geodetic and Cartographic Institute (GKÚ) launched a web-site *with the Real Estate Register (**www.katasterportal.sk**). Prior to the official start-up, the site had been tested by about 60 individuals and legal entities since 1 December 2003. The internet register required about 2.300 PCs with adequate equipment in Cadastral Offices (the investment in IT equipment in 2001 consumed Sk 90m of PHARE funds). It was the Government's requirement to develop a Real Estate Register accessible via internet. The Cabinet has therefore allocated Sk 10m to achieve this goal. Annual operational costs are expected to total Sk 5.2m. The creators believe paid services offered by the internet real estate register could cover a part of the running costs. In the first week of its operation the portal was accessed by 1211 visitors.*

The Real Estate Portal allows access to real estate data only to authorised users. In order for individuals or companies to use its information, they must register (fill in a questionnaire) and pay an advance of minimum Sk 1,000 to the account of the provider (GKÚ) at the National Bank of Slovakia. As soon as the amount is credited to the provider's account, the administrator posts it into the system and informs the customer thereof via an e-mail. From that time onwards, the customer may start using the register information. In each transaction, customers are informed of the fee and may decide whether they will pay or decline the service of the online transaction. The fees are then deducted from the advance payment.

The fees for information received from the real estate portal vary between Sk 30 to Sk 100 and are based on the list of administration fees. The fees are therefore similar to those applied at customers' personal visits to a Cadastral Office, however, they are likely to rise as from 1 July.

The information provided by the online real estate register is not legally binding yet and serve informational purposes only. The same goes for the information provided by the online Companies Register (see HESO 3/2000). The online real estate register is at present the largest Slovak public administration's portal, being currently updated on a monthly basis. In the future, as soon as a LAN network connecting 79 Cadastral Offices with the GKÚ is built, new data should be keyed in within 24 hours (in the Czech Republic, the register is updated every two hours). Within a year or two, the real estate portal could begin using electronic signature, which would allow authorised users to submit applications electronically. At present, the online register operates in a limited mode, with new services being added step by step. Cadastral proceeding system is expected to be integrated in the near future.

The system allows users to search for information using a digital map or identification data of a real estate (county, municipality, cadastral territory) or of an owner (for security reasons, there is a monitoring system allowing the provider to track retrospectively who searched what data on the system). The digital map's zoom function allows users to receive precise information even without knowing an exact location of a real estate property. The system makes available nearly all descriptive real estate information and if territories have vectorial land maps, it also offers graphical data. However, digital maps today cover only about a fifth of Slovakia. Director of the ÚGKK SR said the Institute would like to have maps of the whole territory of Slovakia in a digital format within 5 years, however, with the current budget of Sk 85m, it will not be possible before 2023.

Selected only in the second tender as the first one was not successful, the firm that implemented the system was NESS Czech, a daughter company of a multinational software firm, NESS Technologies, operating in 13 countries round the world, employing 4,400 people in total and forecasting this year's turnover of Sk 10bn. The same company also runs the online real estate register in the Czech Republic, where it has already been operating for 7 years (since last year in full version). The Czech online system, having about 400,000 visits a year, has so far cost about Sk 1.3bn. Last year the Czech register earned Czk 23m for services, being mostly used by legal entities (banks, official receivers, real estate agents).

The benefits of the online register primarily include saving time, limiting space for graft, and improving citizens' access to information. The online register is also expected to improve quality of information, enhance transparency in real estate relations and diminish the burden laid on the real estate register's and GKÚ's administration in terms of providing information. The GKÚ thinks the online register will also assist in developing information society in Slovakia and improving the country's international credibility. The electronic register will simplify the access to information to notaries dealing with patrimonies, as well as to official receivers, Tax Offices and local authorities. The online register will give less advantage to irregular register users who would have to register and to make the advance payment of Sk 1,000.

Critics have focused on the fees for online real estate register services. The opponents argue that through imposing fees on public real estate information on the internet, the ÚGKK violates the Free Information Access Act, which stipulates that compulsory persons that operate information systems containing data, where a special act does not forbid public access, are obliged to publish the information contained in these registers and lists on freely accessible internet web-sites. One of the reasons for imposing fees, as explained by the GKÚ, is to prevent access to the data and use of the portal to an uncontrolled number of users who could thus render the portal unusable. The Institute's representatives argued that Slovakia's paid online real estate register is not unique, although there are not many similar cases across Europe.

Evaluation of the Experts' Committee:

The online real estate register will finally put an end to a sluggish administrative procedure at Cadastral Offices and will provide its users with better access to information. It will also help in fighting corruption.

An important aspect will be that the register functions efficiently - both in terms of service quality as well as costs. It will be necessary to ensure efficiency of the establishment and of the running costs. That is why the experts also consented to service fees. They think the operation of an electronic register should be primarily financed by those who use its services. The experts assume the amount of particular fees will depend on clients' interest in using the online register and will make pressure on enhancing quality of the portal's services.

One respondent disagreed with fees for the online register services, arguing that the Cadastral Office is a public institution financed from citizens' taxes. It should therefore provide information free of charge. Besides, the whole project has probably been funded by the PHARE programme and has likely been of not-for-profit character. It would therefore be interesting to find out whether or not the agreement stipulates that the Cadastral Office may not earn profit on the project.

The significance and benefits of the online real estate register will further rise after dealing with some teething technical problems (e.g., problems when opening the web-site, making the application and payments for services faster).

The Real Estate Register is a positive example for all public institutions, which should follow it, whereby Slovakia's obsoleteness in this area could partly be removed. Developed economies allow their citizens to carry out a much larger number of transactions and the communication of citizens with public administration via internet, telephone, e-mail or fax. This has a positive effect on business environment and improves the quality of citizens' lives.

Competition Policy

Liberalisation of Prices in Compulsory Motor Third-Party Liability Insurance (Amendment to the Act on Compulsory Motor Third-Party Liability Insurance)

On 19 September 2003 the Members of Parliament passed the Amendment to the Act on the Compulsory Motor Third-Party Insurance prepared by the Government. Besides approximating the Slovak law with the EU legislation, the Act has also abolished the administrated third-party motor insurance premiums. Hence, the insurers providing motor insurance services may set premiums freely, applying their own criteria without having to obtain a prior consent from the Financial Market Authority. The original premium setting mechanism restricted pricing to certain limits, reflecting inflation and claim ratio, while the final amount of the premium could have been increased by maximum 30%. The calculation must also have reflected the cylinder volume as the only differentiating criterion. The new Act allows insurers to take into consideration other parameters as the age of a vehicle, driver's residence and age, and other risk factors. Nevertheless, it is not expected that these factors would extensively be used in the near future as insurers do not have sufficient data on previous years (some insurers have already started differentiating the rates according to drivers' age or residence though) (Note: the system of no-claims bonuses had already been introduced earlier). The full premium liberalisation has been proposed with the aim of increasing competition in the relevant market (at present, there are eight commercial insurance companies in the Slovak market offering third-party motor liability insurance; in 2002 and 2003 they were seven), while it had originally been intended to become effective only as from 2005.

The Amendment to the Act retains insurers' obligation to pay eight percent of total premiums collected to a fund financing medical emergency and a fire-fighting squad services. Although the Ministry of Finance made pressure on suspending this obligation, the Parliament supported the respective provision arguing that the abolition of the assistance would put the existence of these two services into jeopardy (there even appeared a proposal in the Parliament to raise the amount to 10 percent). In relation to this obligation, insurers had already approached the Constitutional Court of the of the Slovak Republic and ceased contributing to the funds (Sk 460m in 2002), wherefore they were penalised by the Financial Market Authority.

The opponents to the price liberalisation regarding third-party motor insurance argued that it would trigger tremendous price increase with a negative impact on drivers. The opponents also pointed out that insurers' outstanding liabilities from years before 2002 will hence be compensated through increased premiums. The Director of the Slovak Insurers' Bureau (the SKP) expected the rise in premiums as from the beginning of the year by roughly 30% (in 2002 it was by 50%). He *also predicted bigger differences between insurance providers in terms of prices. This has already proved to be true. He also said that substantial price increases could level off after the aforementioned liabilities from previous years have been paid out, i.e. within two to three years.*

The Amendment also approximated the third-party motor insurance in Slovakia to the EU legislation. Every Slovak insurer has thus an obligation to appoint a Claims Representative in each EU Member State (and vice versa*). Insurers will also have to indemnify claimants within three months after the claim has been reported. The SKP, which became the Information Centre as from 1 May 2004, will have to administer claims in two months. The Amendment also defines conditions for a claimant to be entitled to proceed his claim to the Insurance Guarantee Fund.*

The majority of the provision became effective as from 1 November 2003, or on the date of Slovakia's accession to the EU.

Evaluation of the Experts' Committee:

The liberalisation of the third-party motor insurance market was evaluated by the experts as a right and a necessary step to take as there is no need to regulate prices in a competitive environment. And the insurance market should be liberalised. Pricing according to the trends in inflation and claims ratio and according to a single differentiating factor - cylinder volume was a pure anachronism.

The experts were aware of the fact that the price increase, as an apparent outcome of the market liberalisation, will certainly not be a popular measure, albeit inevitable. Moreover, in the first years, the expected price rise will not be accompanied by an increased quality of service. Nevertheless, a well-functioning insurance market may help implement a healthy competitive environment. After a certain period of time the concerns of further rapid price increases will be diluted and later perhaps the premiums of the third-party motor insurance may even go down. The premiums will also be more dependant on a number of criteria as, e.g., drivers' residence or the age of a vehicle.

One expert also thinks the state will have to carry out a consistent supervision to prevent insurers' collapses as it had happened in the Czech Republic in the previous years. An important role will have to be played by the Financial Market Authority and the Antimonopoly Office of the Slovak Republic. These are the institution that should monitor the market and watch insurers so that no price agreements between them can arise. As another expert pointed out, another steep rise of premiums can be prevented by restricting judges' wanton rulings regarding multimillion indemnities for non property claims made by accident participants. These indemnities are sometimes many times higher than similar ones in the EU countries. Although these claims could not be addressed by the Amendment, it is desirable to set limits of "adequate compensation". The Slovak Insurers' Bureau could also become a participant in judicial procedding so that it could make objections to judges' rulings.

Some critics think that the full third-party motor insurance market liberalisation is unfair to disciplined drivers, who will, through increased premiums, pay for the deficits of insurance companies, which arose due to insufficient insurance coverage in the past, and who will hence pay for the drivers causing damages. Another ctitic said that the steep rise in the third-party motor insurance premiums reflects a crisis of the state regulatory bodies.

There also occurred a view that it should not be called liberalisation when a market strongly regulated by the state ensures to companies a certain market share since the third-party insurance is compulsory.

In 2003 the compulsory third-party motor insurance collected soared by 54%, to Sk 9.2bn. This tremendous increase was a result of increased premiums, while the number of vehicles covered dropped by nearly 2%. The latter was caused by the opportunity of a temporary suspension of the insurance (see HESO 1/2003) and also by many cases of terminated insurance cover due to outstanding premiums. Deficit in third-party motor insurance upsurged from Sk 2.2bn in 2002 to Sk 9.6bn in 2003. In the opinion of the SKP, the deficit was also partially caused by courts' rulings in previous years when the amount of indemnities swelled enormously. The new Act should ease the situation as it is expected to introduce new rules that will stop judges from ruling inadequate indemnities.

Year 2003

Insurer	No. of Vehicles Covered	Market Share by the No. of Vehicles Covered (in %-age)
Allianz - Slovenská poisťovňa, a.s.	1 066 163	66,09
KOOPERATIVA poisťovňa, a.s.	396 556	24,58
Česká poisťovňa - Slovensko, a.s.	62 245	3,86
Komunálna poisťovňa, a.s.	40 066	2,48
Generali Poisťovňa, a.s.	17 410	1,08

UNIQA poisťovňa, a.s.	17 143	1,06
ERGO poisťovňa, a.s.	13 632	0,85
Total	***1 613 215***	***100,00***

Source: the SKP

Act on Electronic Communications (Leading Operators' Compulsory Reference Offer for Network Interconnection with Competitors, Broader Powers of the Telecommunications Authority of the SR, Simplified Entrance into Telecommunications Market)

On 3 December 2003 the Members of the Parliament passed the Act on Electronic Communication. As from 1 January 2004 the new Act replaces the original one that regulated the performance of telecommunication activities. The draft act was prepared by the experts in the Research Institute of Posts and Telecommunications in Banská Bystrica together with the specialists from the Antimonopoly Office and the Telecommunications Authority, under the auspices of the Ministry of Transport, Post and Telecommunications (MDPT).

The main drivers for drawing up the new Act were: the need to change the regulation of the dynamically developing telecommunications market; insufficient legislative framework; powers and independence of the national telecommunications regulatory body (the Telecommunications Authority); the necessity of the approximation to the EU legislation; and a new single regulatory framework in the EU for all electronic communications networks and services. The previous act (see HESO 2/2000) contained numerous imperfections that were partly dealt with in a number of draft amendments (see HESO 2/2002, 2/2003). Being vetoed by the President, these have however never reached a sufficient support in the Parliament in order they could be adopted. The purpose of the Act on Electronic Communications is to liberalise the telecommunications market, allow a real competition between the operators and hence improve service quality, push down prices and increase transparency. Apart from other issues, the Act addresses voice telephony services, as well as the transfer of electronic mail. It also coins a new term of "Electronic communications", which originated from blending the sectors of telecommunications, media and information technologies and replaces the original term of telecommunications.

The new Act defines a wider scope of activities for the Telecommunications Authority of the Slovak Republic (TÚ), placing emphasis on its co-operation with other state agencies, in particular, with the Antimonopoly Office, the main protector of competition. It also requires that the TÚ carries out all its activities in compliance with the principles of efficiency, objectiveness, transparency, non discrimination, adequacy and legitimacy. The TÚ must publish the measures and decisions taken, as well as other information, on internet and in its Journal. It will continue being financed through the state budget, the Chapter of the MDPT (which is at the same time a shareholder of one of the major telecommunications providers, the Slovak Telecom, a dominant operator in the market). Financing of the TÚ was a target of the criticism from the EU. In the Czech Republic, for example, there has been operating an independent regulatory body with an independent budgetary chapter since 2000. In Slovakia, the problem is the legal form of the agency as its expenditure is linked to the state budget.

The regulatory framework is intended to be technologically neutral and stipulates the regulation in a single manner for all electronic communications networks and services. The new Act guarantees that electronic communications market players may only be regulated if this regulation would help ensure effective competition, while all players must be regulated in the same way. The new Act regulates the competition differently than the previous act as it clearly determines relevant markets (based on the list recommended by the European Commission), definines rules how the markets will be analysed and defines the companies with substantial influence on relevant markets. The provisions of the new Act bind the TÚ to analyse the relevant markets minimum once in two years, i.e. within this period the TÚ will be obliged to assess a particular product or service in terms of competition (the aim is that no company achieves a substantial influence in a relevant market). The TÚ's tasks also include the analysis whether there is a perspective in a market or whether an insufficiently effective competition persists. The Act has also set the criteria of substantial (dominant) influence, where the definition was taken over from the Directive of the European Parliament and the Council no. 97/33/ES. Substantial influence is a market share of 25%. The new Act continues using the term of the so-called administrative delict and has abolished the so-called transgressions, which were ineffective in practise. It explicitly defines the sanctions that are ranked according to the amount of a fine. The TÚ will be allowed to impose a fine on operators in the cases of competition violation and others amounting from Sk 500,000 20 million, which is more than before. The Act also binds the TÚ to consult and co-ordinate its activities (e.g. measures under preparation regarding the regulation of services to end users must be publicised and publicly discussed). The European Commission is, in the cases stipulated, authorised to request the national regulatory bodies that they suspend their decision.

Besides the conditions in the so-called general licence, the TÚ is obligated to specify respective regulatory duties to entities with a substantial influence on the market (e.g., to publicise specific information, adhere to the principle of non discrimination, maintain separate records, meet a justified requirement for an access to local networks (the so-called last mile), interconnect networks with competitors, determine a pricing method, impose regulatory duties on end users, lease circles and others as precisely specified in the Act). One of the regulatory obligations is the one of transparent access to and interconnection of networks, which requires that a major player publishes specific information in a reference offer, including particular accounting data, technical specifications, network attributes, conditions for using networks and prices. A reference offer is a sample agreement on the network interconnection (between a dominant operator and, e.g., an alternative one). The offer specifies key technical standards and contractual terms and conditions (agreements with individual operators may differ in details). The offer is elaborated by a dominant operator and submitted to the TÚ. After being approved by the latter, it is published. (Pursuant to the new Act, the TÚ published a draft offer of the dominant Slovak operator, the Slovak Telecom, for the interconnection of networks on its web site. The interconnection fees and their structure have however remained confidential. And they were these key issues that made the offer unacceptable for the alternative operators who have been negotiating about the interconnection since February last year.).

An important provision included in the Act is a dominant operator's duty to issue a reference offer for the access to local networks (own network) and the interconnection with competitors' networks within 60 days after being recognised as an operator with a substantial influence in the market by the TÚ, or after the new Act has become effective. The representatives of the Slovak Telecom (ST) criticised this provision, which is, in their opinion, unsustainable due to a too complex character of the document. They argued that the neighbouring countries' dominant operators were allowed 10 to 14 months to prepare their reference offers. The interconnection of networks will allow subscribers to various networks to make calls between one another. The access to local networks is pivotal for alternative operators, who will thus be given an opportunity to acquire clients and for whom it is not viable to build their own networks to end points. This provision could eventually put the real market liberalisation into practise.

The previous Telecommunications Act of 2000 has stipulated the obligation to interconnect networks, however, it did not make the follow-up steps clear. It remained blurred what would happen if networks were not interconnected. The indistinctly defined powers of the TÚ were put in doubt. The new Act on Electronic Communications has increased the powers of the TÚ in the negotiations between a dominant and other operators. Upon a request of interested parties or of its own initiative, the TÚ is entitled to enter negotiations about agreements on the access to and interconnection of networks, supervise the negotiation process and, if needed, set technical and general contractual terms and conditions, i.e. to effect an agreement ex ante. Hence, the Act changes the previous situation, where the TÚ could take action only when an agreement has been reached. This change and wider powers of the TÚ are a new promise to alternative operators who rejected the reference offer complaining that the terms and conditions therein were set by the dominant operator and were unacceptable. In twelve months since opening the telecommunications market to alternative providers (i.e. since abolishing the ST's monopoly regarding public voice services in fixed networks, effective as from 1 January 2003) an agreement on the networks interconnection was signed by one operator – ConnSpec Telekom, s.r.o., Bratislava. It was the first successful reference offer on the interconnection of fixed telecommunications networks between the dominant provider and alternative voice services providers (cf Orange Slovensko, one of two dominant mobile operators in Slovakia, made its network available to its rivals last year and has so far concluded agreements with three alternative players – Dial Telecom, GlobalTel Slovakia and eTel Slovensko, while the negotiating process took maximum 2 months). The TÚ granted 17 licences to new voice operators, who however are not using them as they have no connection to the ST's network. It is expected that agreements between the ST and major alternative players will be reached in the second half of 2004.

The new Act has also abolished the necessity of granting licences to new network providers. The entry of companies in relevant electronic communications markets has been made simpler and now it only requires that a company interested complies with the terms and conditions of a general permission. This general permission allows each entity that complies with the conditions stipulated by the law to provide equipment, networks and services, without any further need for an explicit permit or any other action to be taken by the regulatory body. The provider's only duty is to notify the regulatory body thereof. The underlying intention of the Act was to implement the simplest possible administrative procedure that would allow the commencement and continuation of the operation of networks and provision of the services associated with them. Apart from the general permission, the Act also introduces an individual permission where a regulatory body assigns particular frequencies or number to a specific entity.

The Act keeps in practise the provisions regarding the rights for the use of frequencies. These rights may not be restricted except in the cases where there is a lack of frequencies and such *restrictions are aimed at streamlining their use. Moreover, the new Act has further clarified the conditions regarding the individual licences to use frequencies and numbers.*

The Act has also changed the conditions for granting and financing universal services, which it defines in great detail. A company providing a universal service (currently, it is the fixed public telephone network of the ST) will be entitled to apply for the compensation for net costs arising therefrom. There will be a special account where all public services and networks providers will post their contributions according to their domestic market share, minimum 0.2% of their annual turnover. The amount of these contributions will be set separately for each entity.

The Act on Electronic Communications also contains the previous provisions regarding a subscriber's possibility to keep his or her phone number, which has become effective as from the day of Slovakia's accession to the EU. A company providing public telephone service must allow its users, wherever possible, to keep their telephone numbers independent of the operator providing the services. Last but not least, the new Act also regulates confidentiality, ensures the protection of business secrets and changes the provisions on the protection of information transferred.

During the preparation phase of the Act, the participants to the telecommunications market made 104 factual comments that were submitted through a special committee created for this specific purpose. The largest Slovak telecommunications providers united in the Association of Telecommunication Operators (ATO) welcomed the new Act despite the fact that it does not meet all their requirements. It was a success that the major market players were able to reach a consensus. The Act is expected to finally initiate a tougher competition in the Slovak market. On the other hand, the Slovak Telecom adopted a standpoint that alternative operators will take advantage of the networks interconnection for luring attractive corporate clients. Alternative operators expect the new Act to primarily effect a stronger position of the TÚ as a market regulator. The adoption of the Act was also warmly welcomed by the TÚ as it has clearly defined its powers and reinforced its regulatory position in the market. The regulator's representatives have however pointed out the TÚ's key weakness - financing. The Chair of the TÚ said that the organisation will have significant difficulties in putting its powers into practise. For 2004, the regulator applied for the budget of Sk 135m, however, it was allocated less than in 2003, by 6m. The development of alternative providers will strongly depend on the action and capabilities of the market regulator. The latter has however already anticipated possible difficulties - due to a low budget. The TÚ will not be able to hire quality experts and commission analyses from independent and esteemed legal counsellors. And it was because of procedural mistakes why several regulatory actions failed in the past.

Critics expressed their dissatisfaction with the provisions stipulating operators' duty to finance reconnaissance equipment, including its operation and calls deciphering upon a request from a state body or prosecuting authority. Despite a number of modifications to the Act, the Members of the Parliament have not removed these particular provisions. Several experts regarded this part of the Act as being unconstitutional. The Constitutional Court of the Slovak Republic has not expressed its opinion thereon yet. In the opinion of the ATO's Chair, this requirement may negatively affect the amount of operators' investment in their business.

The Act on Electronic Communications became effective on 1 January 2004.

Evaluation of the Experts' Committee:

The experts agreed to the fact that it was desirable to introduce a fiercer competition in the telecommunications market. The telecom market liberalisation is an important part of the information society development and Slovakia's further headway. The country has long been awaiting the new Act, which was, in the opinion of some of the experts, caused by strong clashes between interest groups. Delays in the actual market liberalisation, Slovak Telecom's dominance and unfair advantages of its monopolistic position were all a hindrance to the country's progress in terms modern technologies, keeping the prices of many services at a very high level (e.g. for fixed lines). More opportunities for new voice services operators to enter the market should lead to a gradual price decrease, bringing fruit to end users. The experts hope that the Act on Electronic Communications will facilitate a necessary pressure the Slovak Telecom (ST) will have to react to. Some of them assume the ST will fight back and will exert effort to retain its monopoly in the fixed networks market by offering unacceptable conditions for a networks interconnection to alternative operators. Therefore, the key aspect will be how consistently the new regulation will be applied and how the regulatory body, the Telecommunications Authority will act. Its main problem will probably be its insufficient capacity.

The majority of the experts think the dominant operator's obligation to give access to its competitors to local calls (the so-called last mile) is a key prerequisite for the emergence of a competitive environment in the telecom market. Several experts have however presented a view that the ST's reserved stance is conceivable as the new Act will allow alternative operators to approach the profitable corporate segment, whilst the ST will have to carry on providing less lucrative, or even loss, services – particularly the universal service of the fixed public telephone network). Some experts however called for even more radical changes with the eventual aim of fully liberalising the telecom market with no state involvement and complete deregulation of the telecom sector and with an absolutely free access to the market.

Act on Retail Chains (Stronger Regulation of Supermarkets)

Despite the Cabinet's disapproval, on 4 July 2003 the Members of the Parliament passed the Act on Retail Chains. The Act was drafted and submitted by the opposition and its aim was to set key rules for retail chains and their operation in the domestic market.

As from 1 September 2003, the Act forbids retailers to take unfair advantage of their economic strength to the detriment of their Slovak suppliers. The economic strength is defined based on a retailer's share in a relevant market, minimum 5%, or its total annual turnover, over Sk 1.5bn. The unfair advantages primarily include various fees and other payments in kind (for listing goods, for selling goods, for assigning goods a good location in a store, for promoting goods). Additionally, the Act does not allow groundless replacement of goods, unilateral changes to contractual terms and conditions by retailers, selling goods for a price lower than the sum of purchase price and transportation costs, checking goods quality on a supplier's premises, or a supplier's obligation to pay for the quality checks to be performed by a retailer. The Act has also stipulated retailers' duty to reflect 90% of the discount provided by suppliers in the final selling price and set the maximum invoicing credit period for 45 days, originally varying between 30 to 120 days, as revealed by the proponents of the Act. It also requires that private labels (products sold under a retailer's brand name) also indicate a respective manufacturer or his trademark. The adherence to the Act will be supervised by the Ministry of Economy (MH), whereas the retail sales and services will be monitored by the Slovak Commercial Inspection. The MH may impose a penalty for a breach of the Act raging from Sk 1m to Sk 10m. If repeated, the penalty may be double.

The July draft Act had been the third attempt since 2002 to regulate the legal relationships between suppliers and retail chains. The first draft (see HESO 3/2000) produced by the MH was discarded by the Economic Ministers' Meeting in November 2000, as they did not back the idea of dealing with potential misuse of the economic strength of retail chains through adopting a special act. Next, based on the analysis of retail chains' behaviour in the Slovak market prepared by the Antimonopoly Office, the Meeting recommended not to adopt any regulatory measures regarding the retail market. The second attempt (see HESO 2/2002) to pass such a measure came to nought two years ago when the then proposed Act was vetoed by the President and was not passed again due to the fact that the Parliament's mandate terminated. The author of the latest draft Act admitted to being inspired by the two previous draft acts. He has however omitted the provision on the compulsory minimum share of Slovak goods by product categories, the so-much criticised provision by the European Commission. When discussing the latest Act, the Members of Parliament crossed out many provisions, in particular the whole section regarding the establishment of new retail stores.

In its accompanying report, the drafters argue that retail chains build up hurdles between manufacturers and final users and are frequently a rival to producers rather than other retailers. Other arguments for adopting the Act included the fact that similar regulations were adopted by some of the EU Member Countries (Germany, France, Portugal and others). The report generated by the OECD, of which these countries are members, has however revealed that these measures were not very fruitful. The author of the Slovak Act is convinced that the Act is not in contradiction with European law as after some reservations expressed by the European Commission, the problematic sections were excluded. The Act was again verbally supported by the Slovak Chamber of Agriculture and Food (SPPK) and the Union of Entrepreneurs and Employers in Food Industry in Slovakia. The proponents also pointed out the poor economic position of the farming industry which was only deteriorating due fees imposed by retail chains and ever longer invoice credit period. They all regarded the adoption of the Act as a positive sign.

The Cabinet rejected the Act on the grounds of the comments made by the Minister of Economy, Robert Nemcsics, who considers the retail sector to be fully competitive. Slovakia, in the Cabinet's opinion, did not need any special piece of legislation protecting producers and wholesalers from retail chains as the existing legislative framework sufficiently covered all related aspects. Misuse of the economic strength is addressed in the Commercial Code and potential misuse of a monopolistic position in the market by the Act on the Protection of Competition. The Minister of Economy admitted that various listing fees could possibly cause problems, but these should be dealt with by rising competition between retail chains. Immediately after its adoption, the Act was fiercely criticised by local retailers (the Slovak Association of Commerce, the Slovak Chamber of Commerce and Industry, the Slovak Union of Consumer Cooperatives, the Business Alliance of Slovakia) as well as by the EU representatives. The critical opinions were united in saying that the new Act is an inadequate interference in business relationships between retailers and their *suppliers and is not in line with the Constitution, nor the Commercial Code and competition legislation. Opponents also doubted its enforceability. Although the Act entitles authorities to review agreements, it does not deal with the situation where a retailer refuses to show required documents. Other critics said that nobody would be able to force a retailer to sell products of a company that refuses to negotiate the terms and conditions, particularly in a situation where a retailer can choose from a number of suppliers. The credit period of invoices, set to 45 days, also seems problematic to apply. The Act on Agriculture binds processing firms to pay their suppliers, farmers, within 15 days after delivering produce, nevertheless, despite the fact that this provision is being violated, there is no single suitcase known. Opponents also noted that likewise strong customers, there are also strong suppliers who can make a pressure on their customers. There were however also retailers who were not concerned about the new Act. They did not try to conceal the fact that many vague provisions in the Act could be avoided. The Act was not supported by the Antimonopoly Office either. One of its representatives said that when a similar act was adopted in Ireland, the prices of food increased. The Act was also commented by the main negotiator of the European Commission's team for Slovakia who thinks it is not in line with the key principles of the Single European Market, with the right to settle and make business and to provide services, nor with the principle of free movement of goods and services. The EC has notified Slovakia of the unacceptability of the Act on Retail Chains as it believes it is discriminatory and restricts trade. The Commission requested that the Act is amended or abolished.*

Based on the then information of the Ministry of Economy, the Act was expected to have been amended or abolished prior to Slovakia's accession to the EU, which actually did not happen (the Parliament has recently received an amendment to the Act from the Cabinet; note: the Antimonopoly Office insists on completely abolishing the Act). The Act on Retail Chains became effective on 1 September 2003. Chain retailers were given a transition period of 3 months to adjust their existing agreements such that these are in compliance with the Act. In the case of the provisions regarding the private labels, the transition period was 6 months.

Evaluation of the Experts' Committee:

The experts think that the Act on Retail Chains is another example where interests of a small group of entities (producers, retailers, politicians) ruled over the interests of inhabitants. Measures of this kind mostly harm users as the increased regulation may push prices up. The new Act is, in the expert's opinion, a step backwards and is in conflict with free market principles, adversely affects a competitive environment and is not in compliance with the principles of the Single European Market, particularly with the right to settle and make business and with the principle of free movement of goods and services. Hence, the experts predicted only a short life of the Act. Furthermore, specific provisions can be avoided as state bodies are not very much enthusiastic about enforcing adherence thereto, since the Act did not win the support from the Cabinet.

Many respondents do not think the so much criticised fees and payments in kind (e.g. the so-called listing fees, fees for displaying goods on shelves, fees for retailers' promotion activities, etc.) pose any problem. They think the Act inadequately interferes with private business relationships between retailers and their suppliers, which stems from free will. The latter may, for instance, form associations that would be stronger in the negotiating process with chain retailers.

Some experts also said that supermarkets and hypermarkets are successful because consumers like them. Small local stores could become competitive if they changed their behaviour and looked for a gap in the market, as it is common in other countries. Through lower prices, hypermarkets raised the living standard of inhabitants more than all Slovak politicians altogether. The Parliament's decision to regulate retail chains was regarded to be a "medieval" attempt to fight everything strong and a misunderstanding of the modern principle of non-zero-sum games.

A smaller group of experts agreed with the regulation imposed on retail chains arguing that relationships between retailers and their suppliers are uneven and that terms and conditions for suppliers are not transparent and equal. These experts expected the new Act would make retailers refrain from "blackmailing" practises applied before (e.g. numerous fees collected from their suppliers.

Social Policy

Social Security

Concept of Pension Scheme Reform (1st Pay-As-You-Go Pillar, 2nd Fully-funded Pillar, 3rd Pillar of the Voluntary Forms of Pension Insurance)

The draft Concept of the Pension Scheme Reform in Slovakia was presented by the Minister of Labour, Social Affairs and Family, Mr. Ľudovít Kaník, in early February 2003. With some reservations regarding the deficit of the Social Insurance Agency and its impact upon public finances, the Cabinet approved the draft Concept on 2 April 2003 and hence terminated the previous Concept dating back to 2000 (see HESO 3/2000). The concept drafted includes also alternatives proposed by the Economic Ministers' Meeting and the Ministry of Labour, Social Affairs and Family of the Slovak Republic (MPSVR). According to the new Concept, the MPSVR was to draw up the relevant acts by 30 June so that the new system could be launched as at 1 January 2004. This task was partially fulfilled.

The following text is not updated and hence reflects the situation when the Pension Reform was adopted. There are therefore differences between the concept approved and the follow-up acts (see also the following measures in this Section).

*Likewise the previous one, the new Concept is also based on the three-pillar pension system. Apart from the current pay-as-you-go (PAYG) scheme administered by the Social Insurance Agency (SP), the concept also defines the **second fully-funded pillar**. Participation in the second pillar will be voluntary for all working people except for the citizens at the age of less than five years from retirement who at the time of the second pillar's implementation will not be affected thereby. Another exception to the voluntary principle of the fully-funded pillar will be people entering the labour market after the fully-funded pillar has been launched and higher-income groups (with income over Sk 110,000), who will all be obliged to take part in the pillar. There will also be employees, particularly police members and soldiers, who will not be involved in the new system although it was the original idea to include these groups in the universal system too and hence allow them to partake in the fully-funded pillar. Once a person has decided to join the second pillar, he or she will not be allowed to abandon it and will be obliged to make contributions to it. All the insured who will partake in the second pillar will contribute to it a part of their gross wages (the proposed amount is 10%), which will be administered on their personal pension accounts. Another ten percent of gross wages will be contributed to the PAYG scheme. Other contributions to the social scheme will include the following: and 5% to disability and partial disability funds and 3% to the widows' and widowers' funds. These will be administered by commercial life insurance companies.*

The compulsory contributions deducted from employees' wages by employers (at the maximum amount of three times average wage) will be collected by newly established financial institutions, the so-called pension administration companies (DSS) who will accumulate them in pension funds. Each of these companies will only be allowed to manage maximum three different types of funds, distinguished from one another by the rate of risk. Younger savers will have an opportunity to choose any of these three funds, whilst older people close to their retirement age will only be allowed to opt for the least risky one. The Concept's underlying assumption is that competition between the DSSs should improve the quality of their pension management services and increase yields. The competition will further be supported by inhabitants' free choice of a fund, a DSS as well as by their opportunity to change a DSS in the case of dissatisfaction. Pensions should then be paid by life insurance companies, where people after achieving the retirement age should transfer their savings from their personal accounts in DSSs. Hence, commercial life insurance companies will be the second key element of the second pillar. An alternative to the above method of paying pensions could be the so-called programmed payments from the personal pension account (i.e. a future pensioner would today pre-programme the amount of the future pension that could be changed over the years) in combination with the annuity. The total amount of pensions will hence eventually be the sum saved up in the fully-funded pillar and in the PAYG pillar, while the amount on the latter will also be dependant on the amount of PAYG contributions thereto. Apart from the money saved, the amount of pensions in the fully-funded pillar will also depend on the level of appreciation, or depreciation, of the investments of the pension funds. The appreciation of savings in the second pillar will primarily depend on the developments of capital markets, administrative charges for the account administration, regulation costs and investment decisions of fund managers. The level of fees will have a substantial effect on the final value of assets on the savers' personal pension accounts. There is an ongoing discussion among experts whether these charges should be regulated. The regulation could ensure higher pensions, nevertheless, if the competition is adequate, it would be useless. The document prepared by the Ministry does not deal with the charges. The draft act on the fully-funded pillar, presented by the

Head co-ordinator of the MPSVR team responsible for the pension reform, assumes that should a worker decide to save in the personal pension account in a DSS, he or she will pay two types of administration charges. The first charge will be deducted directly from his or her payroll on top of the compulsory contributions, and the second will be charged by a DSS on the total amount of the funds saved.

An important role in this area will be played by the intensity of regulation of the management companies and of their investment activities. The state is expected to assume full responsibility for transparency and safety of the system. Private entities involved in the pension system will be supervised by the Financial Market Authority(UFT). A new body, which was to be established according to the initial intentions in the Concept, would be, in the opinion of the Ministry of Finance and the UFT, useless as the scope of its activities would in fact be identical with that of the current UTF. The UTF has the experts needed, it is only necessary to adjust their scope of activities accordingly. The function of the Central Register of the Participants should be assumed by the Social Insurance Agency. A vigilant supervision should safeguard savings in personal pension accounts from devaluation and pension funds from going bust. Investing will however conform with the principle of higher yields with higher risks. Many financial companies argue that they can multiple the pension savings only if the state allows them to invest in risky assets around the globe. It is therefore the state's task to figure out how to create conditions for achieving the highest yields on one hand and how to eliminate investment risks, supervise funds and publish information on pension savings on the other.

The income of the fully-funded pillar will not be secured and the state is only expected to guarantee the minimum pensions of 40% of the average wage (at the level of average wage in January 2003, it would be about Sk 5,230 – the pension paid to the low-income group at the time was Sk 4,323). Guarantees necessary for the compulsory pension scheme (PAYG) to function will further be provided by the state. If a DSS goes bust or otherwise ceases existence, the funds accumulated will be transferred into another DSS or a depository (the so-called forced management). Each life insurance company offering annuity in the pension savings system will have to be reinsured or will have to have other sufficient capital funds. Damages to the DSS assets caused as a result of criminal acts of statutory representatives will be offset from the respective DSS's assets and from the statutory representative's personal assets. Should both a DSS and its reinsurer prove to be insolvent, the state will guarantee that savers will be paid 90% of the pensions, while the act should also stipulate the level of minimum pensions that should be guaranteed by the state to the full extent. The minimum level of yields will not be guaranteed, nevertheless, should there occur a major difference between yields offered by a several DSSs and this could not be explained satisfactorily, the DSSs will have to pay the differences from the equity.

Funds accumulated on personal pension accounts will be owned by savers. The reform proposed assumes the funds accumulated should fall in savers' inheritance until they are in the form of savings. Once an owner decides to retire and buy a life-long annuity (pension) using the money saved, the funds can be inherited no longer. The reform proponents argue that another reform's advantage is the opportunity of early retirement – i.e. prior to achieving the retirement age as set by the law. This would be allowed in the case a saver has saved up a minimum amount required, which would guarantee that this saver will receive at least the minimum pension as set by the law. The reform's critics pointed out that the portion of the population that would manage to accumulate enough funds for the early retirement has yet not been projected. The amount of the money saved in the fully-funded pillar will depend on such factors as the amount of salary, inflation rate, administrative fees for the accounts management and funds appreciation rate that often cannot be affected by savers.

The implementation of the fully-funded pillar poses a problem of the Social Insurance Agency's (SP) deficit financing. This concerns the so-called transformation costs. The deficit will arise due to the outflow of funds that people will pay to the first, PAYG, scheme. To cope with the problem, the state has so far put aside Sk 65bn (proceeds from the sales of the Slovak Gas Company (SPP), which should last, according to optimistic estimates, maximum until 2010. The Labour Minister believes that further privatisation of the state assets for about Sk 50bn would generate sufficient funds for the PAYG scheme until 2014 or 2015. The second problem is of an accounting nature, i.e. what to do with the SP's deficit in terms of public finances. If it were included in the country's fiscal deficit, it would threaten Slovakia's compliance with the convergence criteria and also the country's early accession to the Economic and Monetary Union (EMU). The Finance Minister Ivan Mikloš said that the negotiations with the representatives of the EU and Eurostat and particularly of the European Central Bank (see HESO 1/2004) do not develop favourably for Slovakia (April 2003). On the other hand, there have been heard voices calling for putting off the accession to the EMU and for implementing structural reforms instead, as these could be threatened by the country's accession in the EMU. There is also a question how many people will decide to switch to the new fully-funded pension scheme, as their number will affect the transformation costs. In the first years, the Minister expects that it will be about 30% to 50%. This flash estimate was disagreed by the Association of Asset Management Companies who think the figure will largely depend on the success of advertising campaigns of DSSs and it is likely to be higher.

***The first pillar** of the of the pension system, the **PAYG scheme**, will be financed continuously, i.e. today's working people will pay today's retirees pensions. The payments of contributions will continue to be collected by the Social Insurance Agency and will amount to 10% (those for will also join the fully-funded pillar) or 20% (those who will not join the fully-funded pillar) of gross wages. The first draft of the Concept defined the first pillar as a safety net for those who have not saved up enough money in the second pillar. The pensions of people who will only be insured by the first pillar will be derived from how much each person has been contributing to it and for how long. The pension will be calculated using the so-called wage points, where the new calculation methodology will reflect the income that was used for calculating the contributions to the pension system. Besides these two aspects, the eventual amount of pensions will also be determined by the real pension level reflecting the fiscal circumstances of the Social Insurance Agency. This will be regulated by a Social Insurance Act (see page 64). The Concept also assumes that the new Act will raise the retirement age to 60 years of age (by step by step increments by 9 months; in the long-term projections until 2085, it assumes the retirement age will rise to 65 years). The prolongation of the production age is, in the opinion of the reform's authors, necessary due to an adverse demographic trends. Decline in the productive population decreases the contributions to the SP, which hence has not sufficient funds for pensions. On the other hand, critics argue that that the outcome of this may cause that the life expectancy stops rising, or even shortens. In their opinion, the longer working age will lead to worsened health status which will result in an increased number of handicapped people.*

*The Pension Reform Concept also counts on the **third pillar**, i.e. a voluntary pension scheme. And it is the third pillar that should become, in the long-term horizon of several generations, the dominant part of the pension security system. Besides the supplementary private pension insurance companies (DDP), an important role in the third pillar should be played by life assurance products and investment products (in securities). The aim of the new act will be to allow all citizens to participate in the pension system under non discriminatory conditions, to set ownership relations in DPPs and to enhance the currently inappropriate protection of the insured (savers) in terms of their assets in and relations with the DDPs. In the Memorandum of the Government of the SR of November 2002, the Slovak Government has undertaken to reinforce the voluntary pillars of the pension system. Tax incentives should thus encourage people to invest money in financial products appropriate to this end. Currently, a DDP client may annually deduct up to Sk 24,000 from his or her tax base. The Ministry of Labour, Social Affairs and Family (MPSVR) intends to raise this limit, however, the Ministry of Finance disagrees. The aim of the MPSVR is to apply tax incentives also to some life assurance products and long-term bank deposits. Nevertheless, the new tax reform (see page 27) prepared by the Ministry of Finance did not include tax incentives to the third pillar. Many economists think tax incentives are unjust as they give an advantage to some products which results in market imbalances.*

*Since the presentation of the new Concept, there has occurred many **opinions** on **and comments** to it. The analysts from the Institute for Economic and Social Reforms (INEKO) supported the reform and recommended that both pillars (PAYG and the fully-funded) are implemented simultaneously. They also regarded important the emphasis laid on individual and voluntary pension schemes. They further advised to prepare a mechanism that would allow the first pillar to decrease contributions to it in future. INEKO experts were more reserved about the second pillar. They were primarily concerned about the circumstances that could postpone the launch of the reform. They think the state officials should first of all compare alternative analysis and pros and cons of both pillars in various time plans in line with impact studies on the public finances. The size of the fully-funded pillar should reflect the state's fiscal strength as well as the second pillar's role in minimising long-term risks associated with pensions. The second pillar relies on the fact that pensions will be paid from the yields on securities. If it is constrained with the limits of the country, it would equally be hit by the demographic trends like the first pillar, as the yields on securities will only be generated by people in productive age. It is therefore a right thing to do, as the INEKO representatives urge, to open the pillar to abroad. Moreover, in the long term, it will be necessary to support similar trends across the developed world. There should be no strong regulation in the second pillar that would force the companies to allocate their funds in the local market. The capital should primarily be invested abroad, however, it is necessary to define as early as today which securities the pension managers will be allowed to buy and what yields may hence be expected. In the INEKO experts' opinion, the society should also get ready for a longer working age, which should however be individual to the maximum possible extent. INEKO thinks the pension system reform is pivotal for the future economic development of Slovakia. Its analysts think the changes to the first pillar could be implemented as early as in the beginning of 2004. The changes to the second pillar will however need more analyses that should be compiled and then used for determining the date when the reform should be launched. The first as well as the second pillar imply a number of risks that can not be projected to such an extent that the most effective system can be chosen. It would therefore be an optimum solution to count on both pillars in the long term.*

The Pension Reform Concept was also criticised by its initial co-author Martin Thomay from the Institute for the Free Society. The future system of compulsory capitalisation will be, in his opinion, very costly (administrative and management costs, marketing costs, etc.) which is not *reflected in the Concept. As a result of these costs, the real yields from the fully-funded pillar may be lower by 20% to 40%. Another reason for low yields on the assets is the preference for low-risk investment (assuming the regulation of the DSSs will be implemented), as e.g. government bonds, treasury bills and time deposits to the detriment of stocks. Hence the proposed system will generate less income than an appropriately adjusted PAYG system. This is also implied in the analysis of the transformation costs (which cannot only be financed from the privatisation proceeds) and in the expected accelerated growth of wages (resulting from the accelerated approximation of Slovakia to the developed economies after the accession to the EU). M. Thomay also thinks that the Concept has not resolved the payments of pensions from the "obligatory capitalisation" yet. This relates to the "insurance" part where pensions should be paid by life assurance companies by means of annuities. The Slovak annuity market does not exist yet and will be small. Insurers have no experience with calculating the price of annuities and, moreover, there are no prerequisites to apply inflation index to annuities (there are no inflation-indexed bonds issued in Slovakia like in the UK or USA). The Concept also does not introduce sufficient changes to the PAYG system. In M. Thornay's opinion, it should more substantially rise the retirement age that is a pivotal measure to maintaining the PAYG system. Although the Concept strengthens the importance of the amount of funds accumulated by individual participants and limits the redistribution, it does not plan to introduce the so-called virtual accounts. The proposed distinction between the method of financing invalidity pensions and widow's, widower's and orphan's pensions and that of old-age pensions is insufficient. The transition to the compulsory commercial insurance will also pose a number of problems that are neglected in the Concept. One of them could be the position of pension administration companies (DSSs) that have no parallel in the Slovak legislation. M. Thomay thinks DSSs would not be able to become players on any European nor Slovak exchange. Another problematic and non systemic area is the restriction to only three funds. The new fully-funded pillar underestimates the forecasted problems associated with the proposed system of guarantees. In its proposed set-up, it would accumulate assets totalling to 60% to 70% of the GDP in forty years. Hence, the issue concerning pensions to be paid by the state, i.e. to be financed by taxpayers, arises, to the extent as set in the Concept rises concerns. Therefore, one of the priorities should be the impact analysis that the Concept lacks.*

Some of these conclusions have also been confirmed by the report produced by the International Monetary Fund (IMF). The second pillar is an excellent opportunity how to decrease the burden laid on the first pillar and may also enhance safety by diversifying resources of pension income and by stimulating development of the Slovak capital market. The decision regarding the second pillar must however be taken only after deeply assessing its related costs. A widespread exodus of funds from the first to the second pillar may make it difficult to meet Maastricht criteria setting the fiscal deficit at 3% of the GDP, said the IMF. The Government should therefore pursue its efforts in strengthening the Financial Market Authority institutionally to end of ensuring prudence and supervision. In the context of the small number of its population, Slovakia may face the problem that the administrative costs will surge, particularly when transposed per capita.

The TU pointed out the fact that the proposed pension system with a strong second pillar does not reflect the solidarity principle. They would rather prefer a strong PAYG system with a weaker supplementary fully-funded pillar. In their opinion, the contribution to the second pillar should hence not exceed 3% to 4%. The TU also expressed their concerns regarding the risks associated with the DSSs as these are not credible. The TU require that DSSs are bound by Mandates and that their statutory representatives are liable with their personal assets.

The Cabinet requested in the Concept that the Minister of Labour, Social Affairs and Family have submitted draft acts relating thereto by 30 June 2003. The new Social Insurance Act was approved by the Cabinet in June (see page 64). As regards the other draft acts, the Minister intended to have them prepared by the end of the year. They were the following: the Act on Old-Age Pension Savings, the Act on the Supplementary Private Pension Insurance and draft Amendments to some other related acts (the Act on Social Assistance, and legislation relating to the financial market). The acts that were to launch the reform were supposed to become effective as from January 2004, pension savings act about six months later when the DSSs were expected to have been granted the licences.

Evaluation of the Experts' Committee:

The reform of the pension system is inevitable as the current system is unsustainable. The Concept provided a firm fundament for further works and improvements that were needed to be done. The introduction of three pillars seems to be a reasonable approach to risks diversification. As the reform will be very demanding in terms of costs and time, it is important that its preparation is carried out with maximum attention. It would therefore be desirable that there are more detailed analyses aimed at its financial impacts and the fully-funded pillar effectiveness although there is no long-term experience with combined systems. Only then the second pillar should be implemented. At the same time, there should be held a nation-wide discussion about the reform as it will affect all citizens. If these do not agree with the reform's aims and trust them, the reform will fail in achieving them and the use of the public resources will not be effective.

The difficulties associated with the reform give rise to a number of contradictory views. Many experts think pension savings on savers' personal accounts is a much better option than the PAYG system, where the eventual pension does not reflect the total amount of the contributions made by an individual worker and hence is against the benefits-to-contribution principle. Others rather suggested that it would be better to focus on reforming the first (PAYG) pillar such that it would also have certain characteristics of the second pillar: less solidarity (i.e. it would more reflect contributions), inheritance of savings and variable retirement age. The second pillar would then reflect the capacity of the Slovak economy. The are also issues that need to be more discussed as e.g. immense transformation costs (hundreds of millions korunas, fiscal impact. Hence, alternatives should be analysed in more detail, as well as the likelihood of the outflow of capital and its possible impacts. Opponents criticised too stringent investment restrictions of licensed private pension administration companies in terms of risks and investment instruments arguing that it will push yields down. They think that too much regulation will result in low pensions. It is also uncertain whether taking over a model from a country were it works automatically means this model would also work in Central Europe. Some experts also think the Concept did not reflect certain aspects associated with Slovakia's accession to the EU. They were also concerned about inhabitants' high expectations from the reform and the readiness of the Slovak insurance and capital markets.

Some members of the Experts' Committee think that the lack of tax incentives for the third pillar would likely result in the stagnation and eventual end of the supplementary private pension insurance companies as well as of the voluntary pillar that could otherwise decrease the relative importance of the fully-funded pillar and hence also the fiscal costs necessary for the reform. The Concept also assumes that eventually the third pillar should become the determining element of the pension system. Experts also criticised that the Concept does not propose a fully universal system as some employees (e.g. soldiers, police) will have their own pension schemes.

Social Insurance Act (Reform of the Pay-As-You-Go Scheme, Raising the Retirement Age to 62 Years, Stronger Benefits-to-Contribution Tie, Automatic Pensions Adjustment)

On 30 October 2003 the Parliament overruled the Presidential veto on the new Social Insurance Act. The new Act was submitted by the Ministry of Labour, Social Affairs and Family (MPSVR) as the first Act of the Pension reform. The Social Insurance Act reforms the pay-as-you-go (PAYG) scheme. It changes the retirement age, which will be gradually rising, sets a new method of calculation of retirement pensions and modifies the social contributions administration by the Social Insurance Agency (SP). The Act has also introduces changes to the system of sickness insurance and unemployment benefits.

The previous PAYG ***pension insurance*** *was, according the the MPSVR, unsustainable and its accumulated deficit in 2040 would reach, if the the most pessimistic estimates come true, Sk 1,289bn. The reasons of the adverse situation, as defined by the MPSVR, are as follows: negative demographic trends, when the number of workers per a pensioner is set to fall; system dependance on political pressures, where the state could set lower social contributions for its employees than the employees in the private sector; weak benefits-to-contribution ties, where major differences in the amount of social contributions to the SP resulted only in minute differences in the eventual pensions, which motivated employers to pay just a small portion on wages officially and the rest unofficially. This behaviour of employers resulted in lower revenues of the SP. The main intention of the Social Insurance Act, as well as of the whole pension scheme reform is gradual implementation of a direct relation between social contributions paid and years worked on one hand and the amount of the old-age pension on the other. In the end, the MPSVR forecasts a self-dependant PAYG pension insurance system that would not be tied to any subsidies from other resources.*

The new wording of the Act brought a new division of social contributions to various funds within the SP. The contributions accumulated in the so called Pension Insurance Fund will be in the case of those who will remain in the PAYG scheme divided into three parts - 20% of gross wages will go to the old-age insurance, 6% to the disability pensions and 2.75% (the Governmental proposal - 2%) to the so-called Reserve Fund of the SP . In the case of those who will as from 2005 decide for the fully-funded pillar, the contributions of 20% will be in the case of old-age pension divided one more time: 9% will go to the PAYG system and 9% to the fully-funded fully-funded pillar. The remaining two percent will also go to the Reserve Fund of the SP (making up 4.75% in total).

Social contributions rates according to the new Social Insurance Act

(in %-age of the calculation base)

Payers / Type of Social Insurance	Employee	Employer	Self--employed[1]	Voluntary employed	State[2]
Old-Age Insurance[3]	4*	16	20	20	20**
Disability Insurance[3]	3	3	6	6	6
Reserve Fund of the SP[3]	-	2,75	2,75	2,75	-
Sickness Insurance	1,4	1,4	4,4	4,4	-
Unemployment Insurance	1	1	-	2	-
Guarantee Insurance[4]	-	0,25	-	-	-
Accident Insurance	-	0,3 - 2,1***	-	-	-
TOTAL	***9,4***	***24,7 - 26,5***	***33,15***	***35,15***	***26,0***

[1] *tradesmen*

[2] *contributions for mother (or fathers) on maternity leave, soldiers during their obligatory, substitute, specialised service and for citizens on military civil service*

[3] *pension insurance (the PAYG pillar)*

[4] *insurance of employers' insolvency so that employees' claims can be satisfied*

** old-age insurance rate is decreased by 0.5% for each dependant child*

*** the Social Insurance Agency pays the old-age insurance for people receiving disability pension until these reach their retirement age (from the Disability Fund to the Old-Age Insurance Fund)*

**** a specific rate depends on a job risk grade*

Note: minimum and maximum calculation bases for social contributions have been raised

Social contributions rates applicable until 31 December 2003

(in %-age of the calculation base)

Payers / Type of Social Insurance	Employee	Employer[4]	Self-employed	Voluntary employed	State[5]
Pension Insurance[1]	6,4	21,6	28	28	State Budget*
Sickness Insurance	1,4	3,4	4,8	-	State Budget*
Unemployment Insurance[2]	1	2,75	3	3	-
Guarantee Fund[2]	-	0,25	-	-	-
Third-party Liability Insurance[3]	-	0,2 - 1,2**	-	-	-
TOTAL	***8,8***	***28,2–29,2***	***35,8***	***31,0***	***State Budget****

[1] *includes old-age, disability insurance and contributions to the Reserve fund of the Social Insurance Agency*

[2] *administered by the National Labour Office (NUP); the Guarantee Fund- insurance of employers' insolvency*

[3] *accident insurance*

[4] *employers employing handicapped people used to pay lower rates*

[5] *the state paid sickness insurance for dependant pupils at secondary schools and students at universities and the unemployed who do not receive benefits; the state paid pension insurance for dependant students at universities, for mothers (or fathers) on maternity leave, handicapped people, soldiers during their obligatory, substitute, specialised service and for citizens on military civil service; the NUP paid compulsory sickness and pension insurance for the unemployed who receive unemployment benefits*

** the rate was set by the State Budget Act for each following year*

*** a specific rate depends on a job risk grade*

*According to the new Act, the **retirement age** increases to **62 years** for both men and women, regardless of the gender and number of children, the retirement age of all citizens in the PAYG pillar will rise by nine months each year, starting with 2004, until it reaches 62 years for all citizens. According to the original proposal, the retirement age was supposed to annually rise by only six months, the acceleration was forced by the the Framework for the 2004 State Budget. Citizens will also be allowed to retire even sooner, the amount of pension they will receive though will decrease by 0.5% for each month of earlier retirement. The early retirement will also be restricted by the amount of pension, which after being adjusted for deductions, may not fall under 1.2-times the life minimum and by the obligation to pay to the pension fund for minimum 10 years. If an unemployed person who is entitled to receiving the unemployment benefit asks for an early retirement, the period that will be deducted from his or her amount of pension will be adjusted for the period when he or she was receiving the unemployment benefit. The same mechanism will be applied to people who after reaching the retirement age will continue working. This person's pension will be raised by 0.5% for each month worked after reaching the retirement age. According to the information from the MPSVR, there are 90% of people who are willing to carry on working even after reaching the retirement age. Pensioners who decide to work will continue making contributions to the pension insurance on their income. After retiring, the contributions paid will be reflected in their pensions. The Act however distinguishes persons who after reaching retirement age work and receive pension and those who work but do not receive pension. If a person in retirement age continues working and at the same time receives old-age pension from the Social Insurance Agency (SP), the contributions to the pension insurance paid of his or her income will be reflected in his or her follow-up pension to only 50%. If an employed person does not receive the old-age pension, his or her contribution will be reflected in his or her* *follow-up pension to the full extent.*

Major changes also occurred in the pension calculation method. Each insured person will have his or her pension account with the SP and will be informed every year of the balance, the amount of future pension, his or her monthly and annual salary, the nominal monthly wage of employees in the economy, how many years he she has worked, or how many years he or she is yet to work.

Opposed to the previous system, the new system strengthens the benefit-to-contribution tie. The amount of pension will in the PAYG pillar depend on the number of years worked and on a person's average wage during the whole period of making payments to the pension insurance. The new calculation method will not be applicable to those who have retired after 1 January 2004, but reached the retirement age earlier.

The rate of annual old-age pension increase should not be decided by the Members of Parliament anymore (see however HESO 4/2003). The already ascribed pensions will be appreciated every year automatically, as of 1 July, in a percentage that will reflect the ratio of year-on-year growth of average wage in the Slovak economy to the year-on-year rise of consumer prices (life costs; inflation). According to the MPSVR, the old-age pension should not be used as a political weapon anymore. The previous act on social insurance, prepared by the previous ministry, also assumed automatic pension increases as of 1 July in the smaller of the following - the rate of rise of consumer prices or average wage in the economy.

The gap in the funds of the Social Insurance Agency that will be caused by channeling a part of the funds to the fully-funded pillar (the so-called transformation costs) will partly be offset by proceeds from the privatisation of the Slovak Gas Company (SPP), in the amount of roughly Sk 65bn. This amount will however not suffice to compensating the whole deficit. The Cabinet hence plans to privatise some more companies so that it can accumulate more funds. Some opinions though argue that these funds will not suffice either and additional resources will have to be exploited.

The success of the Pension Reform depends to a large extent on the fact how many of the currently economically active people will decide to join the second, fully-funded pillar. According to the MPSVR, it would be ideal if it were about 50% in the course of 2 years. A higher percentage could, according to the Ministry, cause problems in funding the PAYG scheme, as the money channeled to the fully-funded pillar would be missing in the first pillar.

With its retrograde effectivity, the Act will adversely affect those who during their productive age earned, for one reason or another, less than the average wage in the economy, as according to the new calculation methodology, these people will receive lower pensions as in the previous system. In 1998 this group of people comprised 62% of the working population. There was therefore an expectation of a huge repulsion to the reform. A major discussion was expected with regard to the accelerated increase of the retirement age, as some political representatives (including some in the ruling coalition) proclaimed they would not give their support to the Reform.

The MPSVR initially planned to implement a universal Pension System applicable to all economically active citizens. Nevertheless, this principle was abandoned due to the disagreement of the Ministry of Interior, Ministry of Defence, Ministry of Justice, The Slovak Information Service, Ministry of Transport, Telecommunications and the Post, The National Security Office and State Prosecution of the Slovak Republic. The employees of these agencies will still be receiving pensions according to special provisions.

***Sickness benefits** have split into a short-term and long-term part. A sickness benefit will in the first ten days of a sickness leave be paid by an employer (according to a special act, see page 71) – the benefit in the first three days will be 25% (initially proposed 18%) of daily gross wages; in the other days (4 through 7), it will be 55%. From the eleventh day onwards, sickness benefits will be paid, as before, by the SP, currently at the amount of 55% of gross wages. The total rate of sickness insurance has decreased by two percentage points, to 2.8%.*

*The claim to an unemployment benefit may be risen by a citizen who have paid unemployment contributions for three of four years prior to getting registered as an unemployed. The unemployment benefit is paid for maximum 6 months regardless of the number of years worked. The amount of this support represents 50% of gross wages throughout the period. The overall rate of **unemployment contribution** has been decreased from 3.75% to 2% (original proposal was 2.5%) of the calculation base.*

The new Act on the Social Insurance has also changed the organisational structure of the SP. The Governing Council, a Tripartite body elected by the Parliament, was replaced by a 5-member Board of Directors, nominated by the Cabinet. Three candidates are proposed by the Labour Minister, one candidate by the representatives of employees and representatives of employers each. The Tripartite principle of representation has also been applied to the Supervisory Board consisting of Government representatives (5), representatives of employers (5) and of employees (5). The Supervisory Board is elected by the Parliament.

The media also appreciated the fact that the social insurance reform endeavours to more effectively use the existing resources rather than increasing contributions to the system.

The Social Insurance Act became effective on 1 January 2004, some of its provisions as from the date of their publishing in the Collection of Laws, some as from Slovakia's accession to the EU.

Evaluation of the Experts' Committee:

The new Social Insurance Act was accepted positively. The experts appreciated systemic changes as the Ministry of Labour, Social Affairs and Family did not try and amend the previous Act, but drew up a new Act that brings substantial changes to the PAYG scheme. The experts positively evaluated the increased benefit-to-contribution tie, where contrary to the previous system, the rule „the higher contributions, the higher pensions" is applied. The new Act introduces the economically inevitable increase of the retirement age, implied from the demographic and economic trends and common in economically more developed countries, too. In the new system, people can determine their retirement age themselves, which will further be strengthened after the implementation of the second pillar. The perception of the pension will change – it will be more motivational and just, as there will be a clear link between work and remuneration. The experts also welcomed the new method of pension appreciation, as it will not be dependant on a political will and a consensus in the Cabinet, but will be automatic as of 1 July. The experts also mentioned the new system for the appointment of the five-member Board of Directors of the Social Insurance Agency, where the majority representation will be maintained by the Government, which expresses the state's responsibility for paying the pensions.

Negative attitudes were adopted concerning the universal character of the system, as there remained exceptions for some governmental agencies. The fact that a relatively high number of people may receive lower pensions in the new system than in the previous one may, in the opinion of some of the experts, slow down the reform. A part of the experts were also missing virtual personal accounts, or at least a plan to implement them, as these could determine the amount of the pension. The planned system of personal accounts exactly defines ratios between individual pensions. There also occurred an opinion that the state should more actively support young families, which would have a positive effect upon the demographic trends having a positive impact on the pension system, as the total amount of funds in the pension system will always be dependant on the number of economically active people. Critics also referred to the unresolved issue of financing the reform as such and to the fact that the first pillar was developed without an exact knowledge of the design of the second pillar. There also occurred criticism regarding the PAYG scheme and the new Social Insurance Act, which, as it argues, does not solve anything, but only prolongs the situation without any perspective.

Act on Old-Age Pension Savings (Fully-funded Pension Scheme Introduced)

On 16 December 2003 the Cabinet approved the Act on the Old-Age Savings. The President vetoed the Act and returned it to the Parliament, which overruled the Presidential veto and passed the Act on 20 January 2004. The Act was prepared by the Ministry of Labour, Social Affairs and Family (MPSVR) and it launched the second phase of the Pension Reform (see its concept on page 60). After the Social Insurance Act, which has reformed the first, pay-as-you-go pillar (see page 64), the Social Insurance Act implements the second fully-funded pillar. As from 1 January 2005 all citizens will hence have a chance to save up for their pension. The purpose of the reform is to bar the increasing debt of the PAYG scheme, caused by the adverse demographic trend, and to increase peoples' involvement in their lifestyle in retirement.

The new system will be based on contributions, i.e., it will be financed from contributions made to personal pension accounts. From January 2005 to June 2006 all citizens will have an opportunity to decide whether or not they want to participate in the second pillar. Savers will be paid money from this system if they have been contributing to it for minimum ten years (the Members of Parliament changed the original proposal of 17 years). Young people who will get employed for the first time in 2005 will participate in the second pillar obligatorily. People will choose one of the pension administration companies (DSS). If they are dissatisfied with it, they will be entitled to change it, but maximum once a year. The savers' pensions will comprise those paid from the fully-funded pillar and those paid from the PAYG pillar. According to the estimates, the second pillar should provide pensions at 30% to 35% of savers' wages, which means, together with the first pillar, it should ensure pension in the amount of 53% to 58% of people's wages. The real amount of pension will however depend on a number of factors, particularly securities markets where the DSS will invest. Likewise the Concept of Pension Reform, the Act on Old-Age Pension Savings also counts on early retirement. Savers will be allowed to retire earlier if they are entitled to a pension from the first and second pilar in the amount of 0.6-times subsistance minimum (from each of the pillars). The fully-funded pillar will also pay widow's, widower's and orphan's pensions.

Of the current rate of 21.75% that is contributed by employers to the system on behalf of their employees, employers will contribute 9% to peoples' personal pension accounts via the Social Insurance Agency (SP). Any outstanding payments of employers will be paid to the DSS from the Reserve Fund, which will be transformed, as from 2005, into the so-called Solidarity Reserve Fund. This will be stronger by 2 percentage points as the contributions thereto will be of 4.75% of the calculation base. The fund will also be used for compensating damages caused by the illicit action of a DSS, up to 50%. Another obligation of the SP will be to register pension savers, including keeping track of all transactions concerning pension funds. The SP will pay contributions to pensions of handicapped people, who have been saving before, until they reach the retirement age. The state will make contributions for soldiers and people who personally, full-time look after a child (the contributions are 9% of the calculation base). The means on the personal pension accounts will be personal property of savers, will not be taxed and will be inherited. The percentage of total social contributions for the pension insurance will increase from 28 to 28.75% of gross wages. The maximum calculation base has also been raised to up to Sk 32,000, three-times average wage – in 2003 the average nominal monthly wage of employees in the Slovak economy was Sk 14,365). The Act on Old-Age Pension Savings also increased pension benefits by 4% (see HESO 4/2003).

The key activities in the new system will be performed by the ***pension administration companies (DSS) and life insurance companies*** *– private joint-stock enterprises. The role of the DSS will be to create three pension funds which will administer pension assets. They will at the same time pay up pensions (or early pensions or pensions for the deceased). Savers will transfer from his or her private pension account to the insurance company only a part of the funds, which will ensure his pension at minimum 0.6-times subsistance minimum, while they will retain the remaining funds on their private pension accounts in the DSS, which will pay them back to the saver during a period specified by savers. The second option will be that a saver will, upon retirement, choose a life insurer, where he or she will transfer all the funds from the personal pension account. The insurer will then pay a life-long pension (annuity). The depositories of the second pillar will be banks or branch offices of foreign banks that have obtained a permission to provide investment services in Slovakia. Its role will be to provide investment services to the DSSs. Pension funds will only be administered by DSSs that have acquired a state licence to be granted by the Financial Market Authority after having complied with stringent requirements. The company will need share capital of minimum Sk 300m, a creditworthy origin, transparent relations between companies in a group, and shareholders who are able to cope with potential unfavourable financial situation. The criteria will also include the bank used as a depository for the pension funds, expertise, credibility or people nominated in the Board of Directors, Supervisory Board, statutory representatives and top management. To acquire a licence, the DSS must prove capacity of the people who participate in the establishment of the DSS (a suitable person will be a natural person or a legal entity that has been making business for at least three years without interruption prior to submitting an application for the licence). Over a 50% share of the share capital in a DSS may only be owned by a bank, insurance company, securities broker, asset management company and companies with registered seat outside of Slovakia with a similar scope of activities, or a foreign asset management company that is licenced to trade in the area of collective investing. The Act also sets other criteria as, e. g., no links between DSSs (in terms of assets, nor people). DSSs may not perform other activities than pension funds management.*

The remuneration of a DSS for the administration of a pension fund per month may not exceed 0.07% (0.08% in the first 3 months of the existence) of the average net value of the assets in the fund. The charge for the administration of a personal pension account will be 1% of the amount of a monthly contribution. The charge for the change of a DSS will only be applied if it is the second change within one year. The DSS may not apply a charge to a client who has decided to change a pension fund within one DSS.

Each DSS will administer ***3 pension funds*** *(a growth fund, a balanced fund and a conservative fund). The Act requires that each DSS acquires at least 50,000 clients in all funds within 18 months of its establishment, otherwise the Financial Market Authority will impose forced administration on it.*

- *The assets in the* ***conservative fund****, aimed at minimalising risks, may only be invested in bonds and money products, guaranteeing the full amount of assets. People who will reach their retirement age within seven years from joining the fully-funded pillar must use this fund.*
- *The second fund –* ***balanced fund*** *– may invest in stocks, however, to maximum 50% of its total assets and in bonds and money, which must sum up to minimum 50% of its assets; assets not hedged from FX risks may make maximum 50% of its total assets. The fund may only be used by people who will not reach their retirement age earlier than in 7 years.*
- *The* ***growth fund*** *may invest in stocks; its assets not hedged from FX risks may represent maximum 80% of its total assets. It may be only used by people minimum 15 years from their retirement age.*

In 18 months of its existence, the yields on the growth fund may not decrease under 70% (balanced fund - 80% and conservative fund 90%) of the average yields of the same type of fund *in the market. If a DSS is unable to cope with the requirement on a longer basis, it will be obliged to transfer assets of its share capital to the fund and hence offset the difference. DSSs will annually inform savers of balances on their accounts free of charge. Savers will also have an opportunity to check their balance via internet.*

The system will be supervised by the Financial Market Authority (UFT). DSSs will be obliged to report to savers and the UFT. It will also be obliged to provide all required documents to the UFT. The UFT will be allowed to stop every suspicious transaction. An intermediate level of supervision will be depositories. If a depository finds out that a DSS intends to invest funds not in line with the rules, it will be obliged to notify the UFT and the DSS thereof.

Impacts (Transformation Costs):

Long-term Development of the PAYG-Scheme Balance
(in % of the GDP)

Scenario	2005	2010	2015	2020	2030	2040	2050	2070
A	-0,08%	0,08%	-0,04%	-0,94%	-1,82%	-2,02%	-1,90%	-0,64%
B	-0,08%	0,63%	1,10%	0,23%	-0,76%	-0,94%	-0,91%	0,14%

Note: Scenario A: current retirement age at 62
Scenario B: retirement age at 65

Average Balance of the PAYG Scheme in Selected Periods		
Scenario	2003 - 2019	2020 - 2050
A	-0,17%	-1,79%
B	0,48%	-0,71%

Short-term Development of the PAYG-Scheme Balance

Year	2005	2006	2007	2008	2010	2012
Nominal GDP *(in Sk bn)*	1407	1521	1662	1811	2112	2467
Deficits *(in % of GDP)*						
Scenario A	-0,08%	-0,26%	-0,28%	-0,25%	0,08%	0,13%
Scenario B	-0,08%	-0,25%	-0,14%	-0,02%	0,63%	0,98%
Deficits *(in Sk bn)*						
Scenario A	-1,13	-3,95	-4,65	-4,53	1,69	3,21
Scenario B	-1,13	-3,80	-2,33	-0,36	13,31	24,18

In the first years (2005 to 2008), the fully-funded pillar will, according to the economic impacts analysis, cause a deficit of the PAYG system. In 2010 - 2012 the Social Insurance Agency should generate a slight surplus, while a deficit should again occur in 2015 and the following years. The initial deficits are supposed to cause no problems as the Government has a reserve in the National Bank of Slovakia of about Sk 66bn, as a result of privatisation proceeds (see HESO 2/2002). These funds should be used for financing the transformation costs. The later deficits could be offset by fiscal instruments (e.g., through decreasing overall fiscal expenditures), without using any further privatisation income, and/or by fiscal deficit increase, or extending working life until 65.

Total Contributions to the Fully-funded Pillar (Transformation Costs)
(in % of the GDP)
(Forecasted Contribution Rate 9%)

Transition age	2005	2006	2007	2008	2009	2010	2011	2012	2013
30	0,14	0,49	0,53	0,57	0,61	0,66	0,69	0,72	0,76
35	0,21	0,72	0,77	0,82	0,86	0,92	0,95	1,00	1,04
40	0,28	0,97	1,03	1,07	1,13	1,18	1,22	1,28	1,33
45	0,36	1,26	1,31	1,37	1,42	1,48	1,53	1,58	1,63

Note: transition age = most people younger than the transition age will use the new system, while most people over transition age will remain in the PAYG scheme

The accompanying report to the Act says that the Pension Reform should not cause any major fiscal deficits that could not be financed, including compliance with the Convergence Criteria (fiscal *deficit of maximum 3% of the GDP). The Finance Minister, Ivan Mikloš, and the Labour Minister, Ľudovít Kaník, said that the costs for the development of the fully-funded pillar will not deepen the fiscal deficit by more than 1% of the GDP a year. Both Ministers will carry on with their talks with the Eurostat that the future deficit of the SP is not included in Slovakia's fiscal deficit so that Slovakia can accede the euro area (see HESO 1/2004). Some analysts say that the total transformation costs of the Pension Reform should also include people's costs resulting from longer working life, until 62 (see HESO 2/2003). According to the MPSVR, the Pension Reform may have a positive effect upon the employment as a result of accelerated economic growth. In the long run, the implementation of pension savings, in line with decreased contributions, should have a positive impact on better business environment in Slovakia.*

Pros and cons of the fully-funded pillar (the MPSVR analysis):

„The yields in the fully-funded pillar will depend on the yields from investment of pension assets on the financial market. The yields of the PAYG scheme are determined by the rise of wages. If a demographic development is constant, the system with a higher yield rate is more advantageous. If in a certain time period the rise in wages is higher than the yields in the fully-funded pension system, the PAYG system is more advantageous, and vice versa. Through introducing a combined system, the risks of both the PAYG and fully-funded schemes are diversified between the labour and financial markets. An in-depth financial crisis, caused, e.g., by hyperinflation, war or a natural disaster, may significantly decrease the real level of accumulated assets in the fully-funded pillar. Inflation may in the PAYG scheme affect rise in wages and therefore this system is more resistant to inflation. On the other hand, the fully-funded pillar offers higher yields in the long run than the PAYG scheme and hence its implementation in a modern pension system is justified. Its design and scope will depend on the social, economic, political, cultural and historical circumstances of the country."

The Labour Minister, Ľudovít Kaník, believes that the system of pension savings will help significantly increase the life standard of pensioners. He thinks that the adoption of the Act is a break point. The aim of the MPSVR in the next period will be to enhance people's trust in the system, emphasising its transparency and removing doubts. People should be motivated to use the fully-funded pillar as it offers higher yields, as well as by personal ownership of the money saved – non existent in the first pillar (the original draft did not include the personal ownership of the money saved, it was added in by the Parliament). The Minister's priority is not the highest possible yields, but first and foremost the security of citizens' pension savings. The transition to personal accounts through an intermediate entity (the SP) was supported by the example of the Croatian system, where money is collected by the SP, which thanks to its technical equipment has no problems doing it. In Sweden, contributions are also collected by a state agency which transfers them, without incurring any additional costs, to individual management companies. The money of the Swedish citizens (compulsory insurance) who do not decide for a particular management company are forwarded to a fund that the state agency administers itself. According to the Association of Asset Management Companies, the Slovakia's approach is an optimum option. Some foreign experts also positively evaluated the Slovak system for the existence of three pension funds, which puts Slovakia in the club of four countries that offer this choice.

Critics expressed their reservations to the restrictions imposed on the activities of pension funds. Several opponents disagreed with their obligation to invest minimum 50% of the funds accumulated in Slovakia (this provision was pushed through by the Economy Minister, Pavol Rusko, reasoning that it will reinforce the local capital market). The critics argue that it will limit the yields of the funds (and hence pensions) as the Slovak financial market has not developed yet. Its size is too small to cope with such an inflow of investment. The funds will hence have to give up lucrative investment opportunities abroad. This restriction was also much criticised by the European Commission, which thinks it is a discriminatory provision violating one of the principal EU freedoms – free movement of capital. Several Members of Parliament suggested that the limit is decreased to 40%, saying that the funds are to be established for pensioners and not for supporting the economy. On the other hand, there also occurred suggestions to increase it to up to 80%, saying that this kind of a restriction can support Slovak companies. Several opposition Members warned from a high risk of losing money as private pension management companies pose a high risk. They do not trust this type of companies after prior bankruptcies of non banking financial institutions in Slovakia.

Opponents also criticised the central system of contributions collections via the SP which is, in their opinion, not capable of collecting its own contributions effectively. For instance, its outstanding contributions total to about Sk 30bn. The critics think it is highly unlikely that the SP would be effective in getting outstanding contributions from other state-owned companies. They say that the private sector is much more effective. Other critics also say that the second pillar significantly discourages creditworthy companies to enter the market. One of the obstacles is, in their opinion, the obligation to acquire 50,000 clients within the set period of time under the threat of forced administration from the Financial Market Authority. Critics also complained about the proposed, but rejected provision that stipulated that pension savings would be state's and not citizens' property. This provision would allow politicians to interfere with the system. If it were in *place, politicians could, in future, cancel the whole system without the possibility of calling it „the nationalisation". Some critics also called for a stronger fully-funded pillar as they thought it should accumulate funds for the old-age insurance (10%) and disability insurance (6%). The latter will however be a part of the PAYG pillar. The opponents to this view argue that in such situation the fully-funded pillar would incur too high transformation costs as well as a risk of a too high fiscal deficit.*

The President vetoed the Act on Old-Age Pension Savings as he was dissatisfied with the amount of pension appreciation (4%) for 2004 (see HESO 4/2003), which, in his opinion, did not compensate the increased living costs. He pointed out the increased VAT in January, from 14% to 19%, adjustments to excise taxes in August, as well as the price increases of energies in January (see HESO 4/2003). The increase by 4% is not enough to offset the year-on-year consumer prices rise. The Parliament overruled the Presidential veto on 20 January 2004 and adopted the Act on Old-Age Pension Savings.

The Act on Old-Age Pension Savings will become effective as from 1 January 2005, except for some provisions that become effective as from 1 February 2004.

Evaluation of the Experts' Committee:

The Act on Old-Age Pension Savings implements the second, fully-funded, pillar, one of two most important pillars of the Pension Reform. The prevailing part of the experts welcomed the fully-funded pillar that will allow people to save up money for their pensions in several years, which will allow them to live, when they retire, with dignity. Slovakia is one of few European countries that have opted for this progressive path, transferring the responsibility for their own lives over to the citizens. Without the Pension Reform, including also the Social Insurance Act (defining the PAYG pillar), the PAYG scheme would be unsustainable. A multiple-pillar system diversifies risks – both economic and political. The evaluators appreciated it that the ruling coalition found strength to adopt such a difficult reform. Despite the fact that some areas will have to be improved through amendments and secondary legislation, the core of the Act is right, correct and in place.

The Committee was critical about the fact that pension funds will have to invest minimum 50% of their assets in the local capital market. This restriction only supports ineffective investment as Slovak companies will issue securities without having an actual need for it. A lower flexibility will result in lower yields and, hence, lower pensions. One respondent thinks it would be interesting to discuss whether the second pillar is less sensitive to political pressures and whether it is more liberal than the first one. Other reservations referred to the increase of contributions, albeit small. These should have rather decreased. The collection of contributions through the SP may also cause problems. A threat to the second pillar may also be posed by an unfavourable development on capital markets worldwide and the Slovaks' distrust to asset management companies. Hence, it is pivotal that the state transparently grants licences only to companies with adequate capital and experience in the market. It is important to emphasise the transparency and openness of the system so that the weak trust of people is not wasted, as it concerns a huge amount of invested money, that will thoroughly change the Slovak capital market within a few years. It will be necessary to address the question of the PAYG pillar and its financing (including the transformation costs) such that it becomes sustainable in the long run. The Cabinet will also have to deal with the questions of inclusion/exclusion of the transformation costs in the fiscal deficit.

Several experts were dissatisfied saying that the fully-funded fully-funded pillar should have been the key one. Conversely, others regarded the fully-funded pillar as unnecessary. The latter thought that it would have been better to reform the PAYG pillar and make it more benefit-to-contribution tied. Then, it would suffice to introduce the voluntary private pension pillar, which actually already exists as the supplementary private pension insurance and life policies. The use of proceeds from privatisation for offsetting transformation costs is, in some opinions, a siphoning of public finances and a dangerous precedence of political irresponsibility. Politicians are making decisions about what will happen in 20 years although they cannot predict what will happen in 5 years. A minority views concluded that it is the inability of political elites to deal with the problem.

Introduction of Employers' Obligation to Pay Sickness Insurance Benefits in First 10 Days of Sickness Leave (Draft Act on Income Compensation in the Event of an Employee's Temporary Sickness Leave)

On 11 June 2003 the Slovak Government passed the Draft Act on Income Compensation in the Event of an Employee's Temporary Sickness Leave (following the President's veto, the Parliament adopted the act on 30 October 2003). Relating to the Social Insurance Act, it is a new piece of legislation, which determines the conditions for paying sickness benefits during the first ten days of an employee's sickness leave. The Draft Act was submitted by the Ministry of Labour, Social

Affairs and Family of the Slovak Republic (MPSVR). The main change brought by the new Act was the introduction of employers' obligation to pay a part of employees' benefits in the event of their sickness leave. According to the previous legislation, sickness insurance benefits were paid by the Social Insurance Agency (SP) during the whole period of employees' sickness. Upon the adoption of the new Act, employers are obliged to pay their employees' sickness leave during the first ten days, whereas the SP covers sickness insurance benefits therefrom. The maximum entitlement to sickness insurance benefits as stipulated by the Draft Act is 52 weeks. During the first three days of a temporary sickness leave employers are obliged to pay their employees benefits of 25% (the Draft initially proposed 18%) of their daily gross wages. From the fourth through the tenth day, employees are entitled to benefits of 55% of their daily gross wages. The Act also provides for higher daily benefits if there is a collective agreement thereabout, however, these may not exceed 80% of an employee's daily gross wages. Employees who are on temporary sickness leave resulting from the use of alcohol or other addictive substances will only be entitled to receiving half of their statutory income compensation. According to the new Social Insurance Act (see page 64), as from the eleventh day employees will be paid, by the Social Insurance Agency, 55% of their daily gross wages. The MPSVR has at the same time proposed to change the maximum limit of daily gross wages on which the benefits may be paid to 1.5 times the average wage in the national economy.

In order to compensate employers for the increase of their costs, the MPSVR has proposed to decrease employers' contributions to the health insurance fund from 3.4% to 1.4%, while the employees will carry on paying 1.4% of their gross wages. This reduction should, in the Ministry's opinion, save employers' funds, as current contributions totalled approximately Sk 10bn, whereas after the change costs should be reduced by Sk 6bn. Estimates forecast the corporate expenditures on sickness insurance at Sk 3.5bn, which represents a decrease in employers' total expenditures by approximately Sk 2.5bn. Income compensation paid by employers to employees is also tax deductible. The decrease of the burden on employers results from the fact that the SP has been generating surpluses in terms of health insurance, which in the past used to be transferred to the pension insurance fund. As from 1 January 2004, the new Social Insurance Act rendered such cross-subsidies impossible. Since 1999 SP's overall expenditures on health insurance has constantly, albeit slightly, been decreasing, reaching Sk 7bn in 2002. The MPSVR intends to cut down other social insurance premiums too. Within next three years the overall rate of social insurance premiums is expected to fall by 5 to 6 percentage points.

The reason for changing the legislation was, in the Ministry's opinion, the impracticality of the social insurance system, which was not suitable for higher-income employees and abused by employees with earnings much below the average wage. The argument is that in order to avoid a substantial loss of earnings during illness, the former used to take vacation (rather than going on sickness leave), whereas the latter benefited from pretending to be ill as their loss of income would not be as high. As regards the latter, the marginal income when it was still advantageous was about Sk 7.5 thousand. From this level insurance benefits remained stable regardless of employees' income and premiums paid. The former problem should be dealt with by raising the maximum gross wage on which the benefits may be paid to 1.5 times the average wage. The Ministry regards this limit as sufficient, because the purpose of the insurance is merely to help bridge a temporary sickness leave and higher-income people can compensate the income lost through savings or commercial insurance. The abuse of the system, on the other hand, should be hindered by transferring the obligation to pay a part of sickness insurance benefits to employers, who would hence be, as the Ministry argues, motivated to more widely control the work discipline of their employees (according to law, employers are entitled to contact sick employees at their homes to check whether they adhere to a therapy regimen) as well as to improve the work environment leading to a decrease in the morbidity rate. The obligation to pay the benefits is also expected to stop employers from recommending employees to take sickness leave when they have no work for them. The proponents of the reform also argued that the fact that the sickness rate precisely followed the social circumstances in Slovak regions also proved the abuse of the health insurance system. In the region with the lowest unemployment, Bratislava, in 2002, on average 2.3% of the insured fell ill each day; on the other hand, in Stará Ľubovňa District, with a much higher unemployment rate, the daily rate of sick people climbed up to 14.4%.

The business community's reaction to the Draft Act drafted by the MPSVR was contradictory. The Federation of Employers' Associations of the Slovak Republic (AZZZ) expressed dissatisfaction as that the Ministry did not provide sufficient evidence that the burden to be laid on enterprises, especially the small ones, would be offset. The AZZZ also doubted the Government's calculations indicating that the reform would be, for employers, financially beneficial. Based on the sources available, the AZZZ, however, did not bring up any alternative calculations regarding the Act's impacts. A different attitude was adopted, for example, by the President of the Wood Processors' Union who was convinced that with the new Act in place, firms would better control unjustified morbidity, which had so far been paid by the SP.

The Act on Income Compensation in the Event of an Employee's Temporary Sickness Leave came into effect on 1 January 2004.

Evaluation of the Experts' Committee:

The majority of the experts considers this measure to be correct and assumes that it will help hinder the abuse of the health insurance system. Some experts also think the change to the way the benefits will be paid will assist a purging of the labour market. Employees will have to realise that they themselves are responsible for their health, as there is no demand for frequent absentees on the market. Employers will be able to better control their employees' work attendance and will be motivated to verify whether or not an absence is justified. On the other hand, the experts think that the measure will increase employers' administrative expenditures, as they will probably have to create funds for sickness benefits, which may have an adverse, albeit small, effect upon future pay rises. The experts admit though that these administrative costs will be offset by lower costs resulting from a lower sickness rate of employees.

The measure adopted is, in the experts' opinion, the second best possible. From an overall system point of view, it would be better if the sickness leave insurance were transformed to commercial insurance and hence employees could choose whether or not to get insured. The amount of benefits would hence be stipulated by insurance policies. If an employee did not get insured, they would receive no sickness benefits and any attempted abuse would be treated as a criminal act -- fraud.

Critics argue that the measure will uselessly burden businesses and will make no pressure on state administration to make its performance more efficient. The abuse of the system could have been addressed by enhanced inspections of physicians and by scrutinising frequent absentees. A minority opinion claims that the measure may adversely affect the health of employees, who will, whether of their own decision or under pressure from their employers, be working when sick. A few experts identified themselves with the comment made by the AZZZ who were missing a more detailed quantification and analysis of the new system's benefits and its impact on SMEs.

A survey conducted by The Business Alliance of Slovakia in April 2004 implies that 60% of the selected businesses think that the new Act will bring benefits to the business environment in Slovakia. Conversely, 32% of the respondents said the new measure would instead be an obstacle. Thirty-six percent of the businesspeople enquired claimed that the new system had decreased costs, whereas 32% recorded an increase in costs due to paying sickness benefits to their employees in the first ten days of the employees' sickness leave. Other managers (32%) did not record any changes to the companies' costs that arose from the implementation of the new system. The survey also showed that compared to the same period last year, from 1 January to 31 March 2004 the average sickness rate per an employee dropped by 36%. While in the first three months of 2004 the companies participating in the survey recorded an average sickness leave per employee of 1.8 day, in the same period last year it was over 2.8 days.

State Social Support and Social Assistance

New Child Allowance Act (Flat Amount of Child Allowance SKK 500 per Child, Tax Bonus SKK 400 per Child)

Through the new Child Allowance Act adopted on 6 November 2003 and effective as from 1 January 2004, the Members of Parliament decided that the state will pay a flat child allowance of Sk 500 per child regardless of a child's age and family income. Hence, the flat child allowance has risen by Sk 230. At the same time the new Act has abolished the contribution to the child allowance, the amount of which was set based on a family income and a child's age. The Labour Minister, Mr. Ľudovít Kaník, argued that the contribution was not a motivating factor as it did not make people try and secure their family with income, while it was quite an administrative burden at the same time. The main concept of the new Act is to provide support to all families with dependant children equally, with no regard to a family income and the age of children. The child allowance is the state's broadest direct financial support to families with dependant children. It emphasises a meaningful use of financial means allocated for the due care of children who are under the compulsory school attendance.

According to the new Act, a dependant child is a child until ending up his or her compulsory school attendance, no longer, however, than until the twenty-fifth year of age (if the child is getting ready for university studies or cannot get employed due to an injury or an illness). A dependent child is also a child with a long-term adverse health status. A dependant child is not a child who is eligible for a disability or a social pension, whose university studies are longer than usual (pursuant to the University Act), nor a child who has achieved the university education of the second grade.

Although the new Act did not stipulate any other child allowance, it is linked to the Tax Reform (see pages 27, 35), which has, along with the child allowance, introduced the so-called tax bonus. Tax allowance hence comprises two parts. Besides a flat monthly allowance of Sk 500, an employed parent will also receive a tax bonus that can be deducted from the amount of tax to be paid of Sk 4,800 a year (or Sk 400 a month) per each dependant child. Each family with at least one working parent is eleigible to the bonus. The parent can deduct the bonus from his or her tax to be paid (or from his or her tax prepayments). Should a parent achieve a negative tax to be paid, he or she will be entitled to get the bonus refunded. Taxpayers will be entitled to get the bonus if their income in a respective tax period reached minimum six times the minimum wage (the Cabinet originally proposed 12-times the minimum wage).

According to the analysis prepared by the Government, the new Child Allowance Act will in 2004 consume additional Sk 8.1bn (later adjusted to Sk 8.4bn) (with 1,350,000 children and at the amount of allowance of Sk 500; in the first half of 2003 the average number of beneficiaries was 813,200), which is less than in 2003, by about Sk 1.5bn. Based on the Tax Reform and the agreement with the Ministry of Finance, the funds saved will be used for tax bonuses to child allowance for employed parents. As the new system does not reflect the parents' income, it will remove heavy administrative burden associated therewith and allow to transfer all administrative tasks to one agency without any major costs. From 1 January 2004 to 31 March 2004, the child allowances were, in the case of companies with over 20 employees, still to be paid by employers, from 1 April 2004 onwards all contributions were supposed to be paid by the Offices of Labour, Social Affairs and Family. The implementation of the new system required Sk 300m for technical support and Sk 550,000 for forms.

The new system was criticised by the oposition who argued that it will worsen the circumstances of families where none of the parents work (apart of the unemployed, it also concerns pensioners or handicapped people who look after children). The increase of the child allowance will not allow these people to cope with increased living costs of families with children, nor further cost increases forecasted for 2004. They further argued that the family policy should have been dealt with hand in hand with social policy, which has not happened. Opponents requested that the amount of the allowance be determined based on the price development and be not left at full state's dicreetion. The risks associated with the concept as presented is, according to some opinions, that parents living in regions with a high unemployement rate may find it difficult to get a job. Hence, they will not be able to find a job and will not be eligible for the tax bonus for dependant children.

As a general type of support, the child allowance paid on all children regardless of income is used in almost all EU countries. The only exception are Spain and Italy, where parents exceeding a certain income limit lose the entitlement thereto (in Spain, it is over Sk 321,000, in Italy, nearly Sk 2 million a year). The same amount of the allowance regardless of a child's age (until a limit) is applied in Sweden and Spain. The child allowance is a family support that is, according to the EU legislation, exported.

In the previous system, the flat child allowance was Sk 270 a month. Depending on the family income and the age of dependant children, the state also provided parents with lower income with a contribution to the allowance from Sk 210 to Sk 620. (see HESO 4/2002). The system distinguishes 2 income brackets and 3 child age brackets. Additionally to the contribution, one of the parents could deduct Sk 16,800 a year from his or her tax base per each dependent child. In January to April 2003 the average amount of the allowance and the contributions was Sk 567 and the average monthly benefit of the tax deductible item per child was Sk 195 – which totaled Sk 762 altogether. The new Act supports families with children with Sk 900 a month (Sk 400 + Sk 500).

The Child Allowance Act became effective on 1 January 2004.

Evaluation of the Experts' Committee:

The majority of the experts appreciated the support to families with children in the form of the tax bonus, which encourages people to work, albeit half time. Hence, it puts into practise the crede "it is worth working". The new Act simplified the system of child allowances like the Tax Reform simplified the taxes.

Different views were expressed in connection with the retention of the flat child allowance. One group presented an opinion that if we support families with children, we should do it at equal terms. Therefore, the flat allowance is just as it does not discriminate any children who are eligible for the allowance. The opponents argue that the flat allowance is not an ideal solution as there is no need that all taxpayers contribute to allowances of children of rich parents who do not need them. Flat allowances – it means also to well-off families – are a waste of public finnaces and are just the contrary of what it should be – addressed and effective use of state social support, which is one of the proclaimed Government's tasks. Some experts think the new Act will adversely affect financially weak inhabitants who are characteristic for their high uneployment rate.

Employment Policy

Amendment to the Labour Code (Partial Labour Market Liberalisation)

On 21 March 2003 the Members of Parliament adopted the Amendment to the Labour Code. It was submitted by the Ministry of Labour, Social Affairs and Family of (MPSVR) and it reacts to the requirements set out in the EU Directives, the International Labour Organization (ILO), as well as of the practise. The main purpose of the draft Amendment was to ensure higher flexibility in employment relations, to restrict the coercive character of the Labour Code and to establish prerequisites for a wider collective negotiation framework. The Labour Code only sets key aspects, basic frameworks and limits and it assumes that respective employment relations will further be specified at the corporate level, depending on specific circumstances of employers, regions and industries. One of the aims is also the equality of employees and employers in the case of a violation of employment relations and also in the case of disputes during collective negotiations.

Key changes:

- *The new Code stipulates the right of employees and employers for collective negotiation, the right of employees to go on strike and employees for a ban thereof.*
- *It proposed a longer probation period of 6 months, originally 3 months, which was not eventually approved.*
- *It defines anew the fixed-period employment and part-time work such that an employer can ensure the fulfilment of all his tasks, depending on whether they are long-term or iterim tasks. Employers can more freely conclude, prolong and renew employment contracts (renewals and prolongations with more people) in the case of fixed-term and part-time contracts (opportunity to use fixed-term contracts for upto three years (initially proposed 5 years)). This measure is supposed to allow firms dependent on the cycle to hire a necessary number of employees in the time of recovery and then to lay them off in the time of recession.*
- *It restricts the protection of employees in the case of termination of employement concluded for a shorter working time than 20 hours a week. This relation can be terminated by both employers and employees for any reason or without giving any reason. This type of a contract termination requires a fifteen-day notice.*
- *According to the new Code, an employer may terminate a fixed-term employment contract without giving any reason immediately; in that case, an employee is entitled to a compensation totaling to the amount he or she would receive during the whole period of the contract.*
- *It abolishes a type of temporary work contract (the initial draft also abolished the job work agreements for students). This type of contract should be replaced by an employment contract up to 20 hours a week.*
- *It abolishes a ban on employment relation between spouses.*
- *It provides a more detailed specification of the termination of an employment relation. To the end of strengthening the work discipline, it allows employers to terminate an employment contract with an employee in a simpler manner if the employee is not able to duly perform his or her duties. If an employee violates the terms and conditions in a less serious manner, the employer may terminate the contract as soon as this repeats and the employee had been notified of his or her misdemeanour within the previous six months (so far, it has only been in the case of serious breach, in the case of less serious violation, this violation whould have to be recurring on a permanent basis).*
- *It allows employers to temporarily suspend the performance of their duties and obligations arising from an employment contract if an employee is justifiably suspect of a serious misdemeanour of working discipline or of commiting a crime and his or her activities may threaten employers' interests. Having agreed on it with the employees' representatives, an employer may under these cicumstances suspend the relation with this employee for one month (initially proposed six months). The employee is entitled to wage compensation for this period amounting to the average income earned (initially proposal – half of the average wage and if proved innocent, the second half).*
- *According to the new Code, an employer may terminate an employment contract with immediate effect if an employee has been convicted of committing a criminal deed or has significantly breached working discipline. An employer may not end a contract with immediate effect with a pregnant employee, an employee on a maternity or parental leave, with an employee who is single and is looking after a child younger than three years of age, nor with an employee looking after a close relative who is handicapped. With all these categories except for an employee on a maternity leave, an employer may terminate an employment contract with a notice.*
- *If it does not concern a contract termination for unsatisfactory performance of an employee's duties, an employee may terminate a contract with an employee for a less substantial*

incapability to fulfil his or her tasks or for any other reason that gives grounds for the immediate termination of an employment contract only if the employer has no opportunity to further employ this employee, including for a shorter working hours, at a place that was agreed as a place of work, or the employee has rejected another, but suitable, work offered to him or her by the employer.

- *The Code unifies the notice period for two months for both employers and employees, if not agreed otherwise in a collective agreement (so far, it was 3 months in the case of the employment termination for organisational reasons, in other cases, it was 2 months). If an employer terminates a contract that has lasted over five years, the notice period is minimum 3 months.*
- *The new Labour Code also stipulates a compensation in the amount of a 2-month wage if an employment contract is terminated for organisational reason or due to an employee's health status if this employee agrees with the termination of the contract without any notice period. In the case of employees who have been working with their employer for over than 5 years, the compensation equals to three times their average monthly wage.*
- *The new Code also sets more precise rules of personal leasing (when an employee works for another natural person or legal entity). It has coined the term „using employer" and has introduced equal terms and conditions for termporary staff with those of permanent staff of the using employer (the HR agents and agencies that provide personal leasing services has later been dealt with in the Act on Employement Services (see page 78)).*
- *The Code provides a comprehensive definition of the obstacles at work and the provision of free time to employees as well as wage compensations (e.g. a birth of a child, blood donorship, compulsory health checks, convalescence leave, training). In the case of some of the obstacles, the Code restricts the number of days off that an employer is obliged to provide and pay (e.g., 7 days a year for medical checkups, accompaniment of family relatives to medical facilities, death of a relative). In other cases, employers must provide a day off - without providing a compensation for wage though (e.g. one day for an employee's wedding, for going to military authorities, to perform duties in trade unions (TUs) or an employee committee etc.) if social partners do not agree more favourable terms and coditions for employees in a collective agreement.*
- *It has abolished compensation for wages for TU representatives in the time of performing their TU duties.*
- *It deregulates working time: depending on the nature of a job and the type of work, the new Labour Code allows employers to design the working time accordingly, which means either evenly or unevenly accross weeks. The Code has also set maximum limits for required overtime (150 hours a year) and additional overtime agreed upon with employees (250 hours a year) (before, it was 150 hours a year + 150 hours a year based on an agreeement with a respective TU and after having received a permission from the National Labour Office). The agreement about overtime is in the sole dicreetion of employers and employees, i.e. the former do not have to ask for a permission from TUs nor the National Labour Office.*
- *The new Labour Code also makes it possible that a pregnant woman, a woman or a man permanently looking after a child under three years of age, a lone woman or a man permantly looking after a child under 15 may only work overtime if they agree to it (it was not possible before at all). They may also agree with their employers that they will be on standby duty if necessary.*
- *It stipulates maximum working time hours with one employer of 48 hours per week (including overtime) – before, it was 58 hours including overtime with all employers; however, exceptions are possible in the case of agricultural seasonal works.*
- *The proposed abolition of the entritlement to 8 hours off after a business trip if employees returned after midnight did not pass.*
- *The proposed 5-week vacation regadless of age did not pass; i.e. 4-week vacation (8 weeks for teachers), while after having worked 15 years, employees are entitled to one additional week.*
- *The new Labour Code has also abolished the so-called further vacation applicable to workers with uneven working time (seasonal jobs, jobs dependant on weather conditions).*
- *It also allows the co-existence of the Employees' Council and TU in one company, as is the case in other European countries. Contrary to the current situation, the Labour Code protects the employees' representatives from a dissmisal if these do not agree with the dissmisal and to have a fair and unbiased trial. Employees' Councils may be established in companies with over 50 employees (before they were compulsory in firms with over 20 employees).*
- *Employers are obliged to allow TUs, Employees' Councils or employees' councelors (smaller firms) to perform their activities at working place.*
- *The new Code also defines the right of employees for information about the company's financial position and on the forecasted future development. This must be provided in a conceivable manner and at an appropriate time. Employees' representatives check that employment rules and regulations are adhered to and may make proposals for the improvement of employees' working conditions.*

- *The Members of Parliament added new provisions regarding the ban on sexual discrimination at the workplace. Employers are not allowed to try to probe for employees' sexual orientation.*
- *An employee who feels being harmed by not adherance to the equal treatment principles may search the execution of his or her rights at a court, including an adequate pecuniary compensation of non property damage. If an employee provides an evidence that may imply direct or indirect discrimnination, it is an employer's duty to prove that the principle of equal treatment has not been violated.*
- *The Members of Parliament also banned any action against employees for lodging a complaint, charge or initiating prosecution against another employee or an employer.*

The draft Amendment arose an ebb of public criticism. The main opponents were the TUs represented by the Confederation of Trade Unions of the Slovak Republic. Trade unions (TUs) called for an alert and threatened with a general strike. Eventually, the Tripartite managed to reach a consensus.

TUs´ requirements approved:

- *The new Labour Code maintained minimum wage requirements and tariff classes. Tariff classes will reflect the difficulty of work and not its duration achieved as before (originally, the MPSVR intended to abolish tariff classes).*
- *The new act does not contain the provision regarding the job agencies.*
- *The weekly working hours in companies on a shift system (two or three shifts a day) remained shortenend.*
- *The TUs have given up the „further vacation", however they managed to secure the additional week of vacation of one week (for employees working in more difficult or unhealthy working conditions).*
- *In the case of a dissmisal, an employee will be allowed to choose between the compensation or a notice period.*
- *The new Code also keeps an employer's obligation to find a more suitable job for employees who cannot carry out their current job due to health reasons. In this case, the notice period lapses only when the employer has fulfilled this obligation, if not agreed with the employee otherwise.*
- *Uneven working time is set based on the agreement with employee representatives or on the agreement with the employer.*
- *TUs have the right to check the health and safety measures, nevetheless, they will not be entitled to stop production.*

The Labour Code Amendment brought up over 200 amended provisions. It represents a large change to the original Labour Code produced in the workshop of the then Labour Minister, Peter Magvaši. In the opinion of many experts as well as of the current MPSVR, the original Labour Code, as a result of many bans, was a major hindrance to people's opportunities to get employed and increase their life standard. It was also often avoided which resulted in the lower protection of employees. In the opinion of the MPSVR, the amended Labour Code should encourage the creation of new jobs. The new Labour Code should also positively affect the state budget. It was also warmly welcomed by the business community as it gives wider freedom in hiring and laying off employees. The business community expressed their satisfaction with decreased powers of TUs in companies. The new Labour Code was also supported by the representatives of major foreign investors. The Amendment will bring new drivers for competition, will encourage investment and will allow to launch production with higher added value, the fruit of which will be secure jobs. The Amendment was strongly protested by the TUs. They argued that the new Labour Code is unconstitutional, providing employers with a big chance to use the new changes to the detriment of employees. As an example, they mentioned the prolonged probation period of six months (not adopted in the end), which could be abused by, e.g., hypermarkets who could thus hire staff for a minimum wage and then replace it after six months. The TUs also believe the new Labour Code less protects employees with a specific social and health background. It concerns, e.g., mothers with children under three years of age. TUs have also pointed out that the Amendment abolishes the principle of an even spread of working time accross five working days. Paradoxically, both the TUs and the MPSVR claimed having support of the International Labour Organization in this issue. Disputes led to January protests of the TUs outside the MPSVR premises. The TUs requested the change of the new Labour Code's philosophy, which was rejected by the MPSVR. In the end, both parties launched negotiation at a Tripartite table. After difficult talks, to the satisfaction of all parties involved, they achieved a compromise.

The Amendment of the Labour Code became effective as from 1 July 2003 with the exception of those provisions that became effective as from 1 January 2004 or as from Slovakia's accession to the EU.

Evaluation of the Experts' Committee:

The Experts´ Committe regarded the Amendment to the Labour Code as a very important and welcomed measure. There however occurred differences in experts´ perception of the effects of the new piece of legislation. A part of the Committee expects a positive outcome within a very short term, whereas others think the amended labour Code is only the beginning of the path leading a free and flexible labour market, and hence to a significant drop in unemployment. A frequently uttered opinion was that the new Amendment just eliminated deformations implemented by the previous Labour Code. The majority of the experts were satisfied that the new legislation is a shift towards market priciples in the employment relations, giving employers the right to more flexibly hire and dismiss workforce. Labour code must, in their opinion, be flexible so that contracting parties can react to the labour market circumstamces and behave rationally and economically. The experts also welcome the fact that although the role of the TUs in companies is still significant, it was partially subdued. Some experts were missing stronger motivating drivers aimed at, e.g., employees who have difficulties to find a job (e.g. handicapped people). There also occurred concerns regading the abolition of short-time work contracts and whether it was justified. A certain group of the experts presented a view that Slovakia is yet not ready for a full labour market liberalisation as the culture and level of employment relations has yet not reached the sufficient level. However, in the same breath they said that the culture will rise (as it has risen in business relations), because employers will realise the setbacks of high HR fluctuations. Thus, the current stringent protection of employees will be rendered unnecessary. Employment relations should stem from mutual benefits. The experts appreciated it that the individual parties, when negotiating the new Labour Code, did not try and abuse the arguments like the necessity of approximating the Slovak legislation with that one of the EU. This type of arguments is today often used for pushing through partial interests of various lobbyist groups. Some experts also agreed with the criticism of the proposed six-month probation period (eventually not approved) as such a probation period would be too long and would give employers, in particular in the retailing and wholesaling sectors, a weapon against employees. The probation period could actually be replaced by fixed-term contracts. The compromising wording of the Labour Code, a result of the talks between the MPSVR and the TUs, proves of the both parties' ability to come to terms.

Another group of the experts think that a number of consessions to the TUs (for instance, maintaining the minimum wage determined according to the level of job difficulty) is a step in a wrong direction as it decreases the market flexibility. There also occurred an opinion that through adopting a compromising proposal the Government has likely wasted an opportunity to shift the labour legislation towards greater freedom and protection of ownership. The new Labour Code hence kept in place a great number of hurdles to private businesses. The changes adopted that should implement greater flexibility are, in this opinion, not sufficient although a certain progress has definitely been made. A group of the experts wondered why the state has decided to regulated certain businesses (HR leasing) that successfully operate. The experts also think the Labour Code goes too far in defining certain very specific terms and conditions of employment relations, including, for example, compensation in the case of an employment contract termination without a notice period, maximum number of days off for funerals of relatives, medical check-ups or an annual limit for accompaniment of relatives to a health facility. These issues should be solely dealt with in employment contracts. There also occurred a rare view that the new Labour Code rather protects employers than employees.

As revealed in January polls conducted by the Business Alliance of Slovakia with selected businesses operating in Slovakia, the amended Labour Code will clearly be beneficial to Slovakia's business environment. Businesses already enjoy greater flexibility in employment relations. The respondents said that the new Labour Code slightly stimulates the creation of new jobs. However, its contribution to the elimination of illicit work (black work) is only minute. After the new Labour Code became effective, 32% of the respondents said their personal expenses had risen. Conversely, 14% said their personal expenses had declined. Other respondent businesses had not detected any changes in terms of their personal expenses.

Act on Employment Services (New Instruments of Active Policy on the Labour Market - Motivational and Activation Contributions, Employment Services Provided by Private Agencies, Higher Frequency Attendance at Labour Offices for Inactive Unemployed)

On 4 December 2003 the Members of Parliament adopted the new Act on Employment services prepared and submitted by the Ministry of Labour, Social Affairs and Family (MPSVR). In line with the proposed Act on State Administration Bodies in the Fields of Social Affairs, Family and Employment Services (see HESO 3/2003) and the Social Insurance Act (see page 64), the purpose of the new Act was to specify the rights and obligations of the participants in relation to the use of employment services. A year after the last amendment to the Employment Act (see HESO 4/2002), active employment policy encountered new changes.

The new Act defines the framework for the provision of employement services by state administration bodies at two organisational levels - the Head Office of Labour, Social Affairs and Family (ÚPSVR) and the territorial offices of labour, social affairs and family. After the reform of the local state administration (see HESO 4/2003), the latter render the services originally provided by the abolished labour offices and social departments of district offices. The new Act has at the same time created a framework for the provision of employment services by other entities than state administration bodies. Hence, ***Agencies for Supported Employment*** *may be established to the end of providing specialised training, specifying capabilities and skills of the handicapped and the long-term unemployed (registeted as unemployed for over a year) and of searching for a suitable employment. In order to mediate temporary employement, Agencies for Temporary Employment may arise. These will first employ a person and then assign this person to a company that will need additional workforce. The aim of this provision is to develop conditions for the enhancement of flexibility in providing employers with additional temporary workforce in the peak periods. The agencies will be business entities who will have to acquire a permission from the ÚPSVR and who will provide their services on a business basis.*

The so far existing instruments of the active employment policy have remained in place, however some new ones were edded. Contributions within the framework of active market measures will be given to each unemployed who complies with specific terms. These contributions will be granted and, hence, will not depend on an official's decision. New contributions include a ***reimbursement of a part of travel costs*** *of a job applicant associated with a selection process or a job interview that takes place outside of the unemployed person's County or residence. The amount of contribution will be determined by the MPSVR in a generally binding regulation. Job applicants who receive training preparing them for the labour market from a Labour Office will also be reimbursed food, accommodation and travel expenses from their permanent residence to the venue of the training and back.*

Another support is ***contribution for services for a family with children****. This will be provided by the Office to those job applicants who are looking after a child that does not go to school yet and who are trained for the labour market. This contribution is supposed to reimburse a part of the expenditures for a nursery school or a kindergarten or for a babysitter. The maximum amount of this support is Sk 1,200 a month for the first child and Sk 900 for the following children.*

Another type of support to job applicants is a ***relocation contribution****. Its maximum amount is Sk 10,000 and may only be paid if a job applicant furnishes documents proving his or her move from his or her original residence to the place of work, minimum 30 kilometres away. A job applicant must also furnish a proof of the change of permanent residence, which was criticised. It is a one-off constribution that job applicants may receive once in two years.*

*The unemployed who are registered with a territorial office for at least three month and set up their own business which lasts for minimum two years are entitled to the next type of support (****contribution for self-employment****; a similar contribution is available for handicapped people who set up their own business). Citizens may claim this support if they provide evidence of their business's expenses. The amount of support is dependant on the average unemployment rate in the region (County) and whether a job applicant falls in the group of disadvantaged unemployed. The maximum support is twenty-four times the minimum price of work (sum of the minimum wage and social security contributions) (with price of work at Sk 8,200, the maximum support could be Sk 197,000).*

According to the law, a disadvantaged job aplicant is a person under 25 or over 50 who has not been employed for a long term, a person fully involved in family life, a lone person looking after a child under 10, a person who could not get employed due to his or her health status (note: not a handicapped person), a person migrating within the EU or a handicapped person. These people will be entitled to the ***contribution for disadvantaged job applicants*** *that is rendered to employers who employ such a person, however for maximum 24 months only. This contribution is payable monthly and amounts to maximum 100% of the total price of work of this employee.*

Another new type of support is ***a contribution for an assistant.*** *An assistant is a person helping a handicapped person during his or her working time. Depending on the length of the employment contract, the amount of the contribution may climb up to 90% of the price of work. A handicappped person who is unemployed who sets up his or her own business in the so-called sheltered workshop (minimum 50% of the staff are handicapped people) will receive a contribution of maximum 24-times the total price of work.*

A motivation to find a job for the unemployed who receive unemployment benefits is supposed to be ***a one-off bonus of 50% of undrawn amount of the unemployment benefit*** *due to the person until the end of the supported period (maximum 3 months). The entitlement to this bonus arises to people unemployed for longer than three months. This measure came to existence as a result of the amendment to the Social Insurance Act.*

Apart from municipalities, also NGOs, schools, social and medical facilities, and churches will be able to employ the unemployed for petty and volunteering works. For the creation of a job, the *organisation will receive an **activating allowance** of Sk 900 (max 10% of the total price of work). Besides the social assitance, a job applicant, or the unemployed, will also receive the so-called activating allowance of Sk 1,000 (see HESO 4/2003). According to the Act, an activating activity is an activity maintaining job a applicant's working habits, while it must include minimum 10 hours a week.*

*A territorial office will also provide graduates as well as employers with a **contribution to traineeships**, of Sk 1,000 a month, that are perfomed by these graduates for maximum 6 months, 20 hours a week. The office will also reimburse trainees' accident insurance costs should these buy accident insurance policy for the traineeship.*

*Other contributions defined in the Act are: **a contribution for the establishment of a sheltered workshop or a sheltered workplace** and **a contribution for operational costs of a sheltered workshop or a sheltered workplace and for employees' travel expenses**.*

*There are also changes to the definition of a **job applicant's duty to actively and verifiably look for a job**. Job applicants are obliged to attend a territorial office within three days after receiving a written request so that they can be offered a job or participate in active labour market measures. With effectivity as from 2004, the frequency of visits in territorial offices varies. The long-term unemployed who do not participate in any active unemployment policy activity must report to the office once in every seven days. The unemployed who participate in an office's programmes and activities must do so once in a month. Other job applicants are required to come to their respective office once in two weeks (as before). Employers, on the other hand, are not obliged to report free positions to territorial offices any more. This obligation was perceived as ineffecicient and to be „a bureaucratic bothering". The new Act has also made changes to the services rendered by territorial offices to the unemployed.*

*The Office of Labour, Social Affairs and Family will ensure that an unemployed will have the so-called **individual action plan**, which will have a form of a written document and which will based on the assessment of personal capacities, abilities, skills determine the type and scope of assistance, as well as the approach necessary for enabling his or her employment. The State Secretary of the MPSVR deems every job applicant should have the individual action plan ready by the end of 2004.*

The Act defines anew the active labour market policy financing. The new financing was transferred from unemployment contributions paid by working population to the state budget. The 2004 state budget hence allocated Sk 2.18bn for the active labour market policy. The financing of the active labour market policy will be moved from the former National Labour Office (NÚP) to the European Social Fund, which is expected to contribute with minimum Sk 1bn. The new motivational employment scheme is compatible with the EU legislation.

The State Secretary of the MPSVR, Mr. Miroslav Beblavý, thinks that the Act on Employment Services is only one in the series of standards to be prepared by the Ministry to subdue unemployment. The European funds should help finance all instruments aimed at supporting employment, with the estimated rise of funds to Sk 3bn to Sk 4bn. It was also expected that in January 2004 5,000 clerks will leave the former NÚP offices and will join the new territorial offices, which would be a cut by 573 people on the previous year. The intention of the authors of the Act was to put job applicants to the labour market as soon as possible, particularly people who have long been unemployed. The proponents of the Act positively regarded the results of the last year's change to the Employment Act, where more frequent visits of the unemployed to Labour Offices helped fight black work, particularly the one performed by people receiving various kind of support and working abroad at the same time.

Concerns regarding the new Act referred mainly to the increased administrative workload of the newly created territorial offices of labour, social affairs and family and so-called „trade" with employer confírmations proving that a person is looking for job, so much discussed in the media. Criticism was also aimed at the provision regarding the relocation contribution, which indirectly assumed a purchase of a new flat, which is impossible for most of the unemployed. Some critics argued that it is not the unwillingness to work that is the main reason of high unemployment, but lack of jobs, particularly in less developed regions (combined with unwillingness to travel or move after work).

The Statistical Office of the Slovak Republic (ŠÚ SR) has revealed that the unemployment rate has risen in first three quarters of 2003 by about 2% on the previous year. The 2003 registered unemployment rate (according to the number of disposable job applicants) plummeted from 17.7% in January to 13.8% in October. The downward trend stopped in November, reaching 14.2% (according to the Labour Force Sample Survey of the ŠÚ SR, the unemployement rate fluctuated between 18.4% in 1Q and 17% in 3Q 2003).

The Act on Employment Services abolished the Employment Act. The new Act became effective on 1 February 2004 with the exception of some provisions that became effective as from Slovakia's accession to the EU.

Evaluation of the Experts' Committee:

Experts appreciated the new active labour market policy instruments that are supposed to help Slovakia fulfil the so-called new European employment strategy. They should assist Slovakia to subdue the number of the unemployed and to shake still waters of the Slovak labour market. The Act on Employment Services lays emphasis on the activity and motivation of the unemployed people aimed at finding and keeping a job, which is right. The reform of the welfare system aimed at the support of work activity (crede: „It is worth working!") is attractive and economically justified. A positive aspect is also fighting black work and hence also fictitious unemployment. It is necessary to help people who are in need and who abuse the welfare system. These people must be identified, e.g., by stringent checks.

A key factor is the implementation of new standards. Time will show how the new Act is put into practise (or avoided). It is very important to assess the effectiveness of individual measures so that public resources are not wasted on support that is ineffective.

One respondent was critical about the conditions set for the allocation of the relocation contribution, which requires a permanent residence in a new town. This provision is, in the expert's opinion, inflexible and for the majority of the unemployed unattainable. How many unemployed could afford to buy a flat/house in another town? Experts also criticised the measure that stipulates that the relocation contribution is not linked to the length of employment with a new employer, i.e., theoretically, an applicant may ask for the contribution after having been working with a new employer for a week. Instead of the relocation contribution, a tax deduction of a part of the relocation costs would be more effective (it exists in, e.g., USA, Canada), which decreases the income redistribution.

Registered Unemployment Rate [1] *(in %)*

Year	2003											
Month	1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.
	17,7	17,1	16,5	15,4	14,8	14,6	14,5	14,3	13,9	13,8	14,2	15,6
Year	2004											
Month	1.	2.	3.	4.	5.	6.						
	16,6	16,5	16,0	15,3	14,5	13,9						

[1] *Registered Unemployment Rate (as of the last day of month) is calculated from the number of disposable job applicants; data from the Head-Office of Labour, Social Affairs and Family*

Unemployment Rate according to the Labour Force Sample Survey of the ŠÚ SR *(in %)*

Quarter/Year	1/01	2/01	3/01	4/01	2001	1/02	2/02	3/02	4/02	2002
	19,7	19,2	19,0	18,7	**19,2**	19,4	18,6	18,2	17,9	**18,5**
Quarter/Year	1/03	2/03	3/03	4/03	2003	1/04				
	18,4	17,0	17,0	17,4	**17,4**	19,3				

Source: ŠÚ SR

The ING Bank data show that the so-called core unemployment rate (the unemployment rate of the disposable unemployment adjusted for seasonality and impact of public works) dropped in May 2004 to 15%, by four percentage points.

Education Policy

Act on the Financing of Primary Schools, Secondary Schools and School Facilities (Pupil-Based Budget, Educational Vouchers to Finance Spare-Time Educational Activity)

On 6 November 2003 the National Council of the Slovak Republic adopted the Act on the Financing of Primary Schools, Secondary Schools and School Facilities, the aim of which is to implement a transparent, standardised and motivational system of financing regional schools, applying multiple sources. The need for the act was driven by the legislative requirement for aligning the financing of regional schools with the public administration decentralisation project (see HESO 2/2003) and with changes to the structure of the Local State Administration effective 1 January 2004 (see HESO 4/2003).

The Ministry of the Education (MŠ), who drew up the Act, recognised that the financing of primary and secondary schools, as well as of school facilities, had been administratively very demanding and the use of the funds allocated from the state budget had been inefficient. State schools administered by municipalities and Self-Governing Regions had been receiving funds for their operation from their founders, who in turn received financing via a decentralisation subsidy, from the Ministry of Finance. On the other hand, municipalities and Self-Governing Regions, as founders of all state schools, received funds for wages and salaries, including social security packages, from County Offices' budgets via District and Regional State Administration Offices. Financial means were allocated to non-state schools and school facilities based on average expenditures per pupil in corresponding types of state schools or school facilities, via the budget of a municipality, Self-Governing Region, Regional Office and District Office.

In the MŠ's opinion, the system that was used in determining the volume of funds to be provided to individual founders for schools and facilities caused low efficiency in using financial means provided by the state budget. This allocation system did not motivate the founders to restructure and rationalise the school network, nor to implement a more effective use of the existing school capacities, which would have reflected demographic trends in regions. The new Act has therefore brought about a number of major changes to school financing.

The new Act distinguishes financing delegated powers from financing original powers of municipalities and Self-Governing Regions (VÚC). Funds aimed at ***financing delegated powers*** *will be allocated to school founders such that they may be used for a specified purpose only. At the first level, the funds provided by the MŠ will be allocated to school founders via newly-established Regional School Offices (although the Minister of Finance and some Members of Parliament proposed to dispense the funds directly to the Self-Governing Regions). The amount of the funds will be derived from financial standards for individual schools. It will also be affected by the number of pupils and by the standardised amount per pupil in each particular type of school. During the 3-year transition period, the schools will receive at minimum 95% of today's funds even if the number of pupils has dropped. The standards imposed will reflect various school types' different needs in terms of human resources and finance. The standards will also reflect different weather conditions (there will be 3 climatic zones differing in the length of a heating period: 6, 7 and 8 months), types of studies (daily, evening, etc.), languages taught (the schools teaching in a different language than Slovak will have a financial standard higher by 8%; in the case of bilingual schools, the standard will be higher by 25%), numbers of handicapped pupils (integrated pupils), and the sizes of schools (primary village schools with low numbers of pupils will receive more money per pupil).*

Determined annually by the MŠ and valid always until 31 January, the ***financial standard*** *sets annual financial means per pupil and comprises a wage standard and an operations standard. Therefore, these financial means provided to municipalities and Self-Governing Regions, as school founders, for exercising the new powers imposed upon them are regulated as restricted-use funds. The second level of financing comprises the funds to schools and school facilities provided by school founders. Consistent with local circumstances and needs, founders may, to the extent required, adjust the volume of financial means for individual schools and school facilities (the founder may retain 20% and 25% from the wage standard and the operations standard, respectively, and allocate this amount per the founder's discretion according to development priorities, or keep it as reserves). The Government, however, will also set a minimum wage and operations standards that schools must receive from their founders. The standardised contribution will be the dominant part of the school funding allocated from the state budget and should suffice to ensure a standard schools' operation.*

Standards per pupil for schools and school facilities in 2004** (in Sk)**:

Schools	***Wages***	***Operations (minimum – maximum)***	***Total (minimum – maximum)***
Primary schools with grades 1 to 4 only, with combined grades; also, primary schools with grades 1 to 9, with a total number of pupils under 150 if it is the only primary school in a founder's municipality with the given teaching language (the so-called low-number-class schools)	*25 932*	*4 870 - 5 734*	***30 802 - 31 666***
Primary schools with grades 1 to 4 only, without combined grades; also primary schools with grades 1 to 9, with a total number of pupils from 151 to 200 if it is the only primary school in a founder's village with the given teaching language	*20 986*	*4 772 - 5 636*	***25 758 - 26 622***
Primary schools with grades 1 to 9 (remaining primary schools that do not fall in the previous two categories)	*16 835*	*4 041 - 4 905*	***20 876 - 21 740***
Secondary grammar schools (the so-called gymnasium)	*20 187*	*4 107 - 4 971*	***24 294 - 25 158***
Sports secondary grammar schools	*31 686*	*4 335 - 5 199*	***36 021 - 36 885***
Secondary specialised schools	*28 096*	*4 264 - 5 128*	***32 360 - 33 224***
Secondary arts schools and secondary nursing schools	*32 618*	*4 353 - 5 217*	***36 971 - 37 835***
Conservatories	*70 295*	*5 097 - 5 961*	***75 392 - 76 256***
Secondary vocational schools	*30 735*	*4 965 - 5 829*	***35 700 - 36 564***
Practical training centres	*12 729*	*3 960 - 4 824*	***16 689 - 17 553***
Special primary schools	*67 100*	*6 332 - 7 196*	***73 432 - 74 296***
Special secondary schools	*43 491*	*5 866 - 6 730*	***49 357 - 50 221***

School Facilities			
Primary arts schools	*6 280*	*2 223 - 2 748*	***8 503 - 9 028***
Nursery schools	*18 138*	*2 794 - 3 319*	***20 932 - 21 457***
Orphanages	*19 503*	*3 147 - 3 672*	***22 650 - 23 175***
Special nursery schools	*45 345*	*5 013 - 5 538*	***50 358 - 50 883***
School catering facilities			***18*** *(Sk 3 per each additional meal dispensed)*
Children school clubs			***4 000***
District counselling facilities			***560***
Regional counselling facilities			***270***
Special pedagogical counselling facilities			***2 160***
Children integration centres			***6 360***
Educational and psychological prevention centres			***700***
Therapeutic and educational sanatoriums			***250 000***
Diagnostic centres			***250 000***
Re-education orphanages for children			***250 000***
Re-education orphanages for youth			***215 000***
Facilities for practical education			***15 000***
School farms			***15 000***
Free-time centres			***4 000***

Special-interest school centres	***4 000***
Language schools	***1 000***
State language schools	***2 000***
Country schools	***Sk 100** (per bed/day)*

Climatic zone	Heating standard for schools	Heating standard for school facilities
1.	2 159	1 313
2.	2 282	1 388
3.	2 406	1 463
4.	2 529	1 538
5.	2 652	1 613
6.	2 776	1 688
7.	2 899	1 763
8.	3 023	1 838

Source: Ministry of the Education of the Slovak Republic

The Act also covers specific elements that cannot be included in standardised funds allocation (commuting children to and from school, education of children coming from socially disadvantaged groups, personnel expenses for Roma assistants and teachers in the preparatory classes). The MŠ will directly allocate funds to the founders of such schools based on their application for funds. The use of these funds will also be restricted. It is assumed that during the new regional schools financing system implementation, a need may arise to include further specific elements. The Act also foresees the allocation of special funds to schools, whose students have made extraordinary achievements in the areas defined (competitions, knowledge tests, etc.).

***The original powers** (public school facilities) will be financed from the General Financial Relationship Chapter. The funds will be allocated directly to school founders without any restrictions as to their use. A part of capital expenditures aimed at the reconstruction of school buildings and the modernisation of equipment will also be financed through the standardised funds allocation.*

Upon a request and within the limits of the Use-Restricted Funds Chapter, the MŠ will be allowed to allocate, to a state school founder, funds to deal with accidents or to implement development projects. Development projects to be supported will be selected by the Ministry.

*The Act also stipulates that **the same funds allocation standards** will be used for the same types of schools and school facilities regardless of whether these are state or other entities (**private, Church**). The MŠ based this approach on the equality principle where all founding bodies are equal in terms of their entitlement to funds from the state budget and at the same time on the non-discrimination principle where citizens who are willing to contribute to the education of their children should not be discriminated against. There is though a difference with regard to capital investment (non-state entities are not entitled to the reimbursement of capital investment from the state budget) and to the transition period (no transition period for non-state entities). Critics of the equality principle argued that, on one hand, both state and non-state schools are equal in terms of funds from the state budget, but, on the other hand, private and Church schools have more opportunities to undertake business activities than state schools, which at the same time, have more legislative duties.*

*There is a new element in the financing of special-interest educational activities, which are **educational vouchers**. Schools and particularly school facilities provided special interest education to pupils, such as, e.g., free-time centres, special-interest school centres, children school clubs and others (see the table above). Educational vouchers represent a special annual contribution per pupil from the state for free-time education beyond the regular school educational process. Educational vouchers are dispensed to pupils by these schools at the beginning of a school year. Public school facilities will then receive funds totalling to the amount of vouchers received from pupils. The value of a voucher will be set by the MŠ annually when budgets are determined. The funds allocated based on the educational vouchers will be use-restricted and dispensed through the Regional School Offices. The entitlement to receiving vouchers arises to* *those schools and school facilities that regularly provide less than 80 hours of free-time education to children across the whole school year. Voucher holders will be pupils who, after enrolling in an activity, will hand over their vouchers to respective schools or school facilities. The financial means based on vouchers will be provided to facilities above and beyond the finance provided through standardised funds allocation or any other ways allowed by the Act. Educational vouchers pursue the aim of making public school facilities more motivated in organising valuable and varied free-time activities for a greater number of children and young people. In the opinion of the MŠ, the vouchers will raise the interest of pupils and their parents in free-time education and its quality and will hence improve conditions for prevention in villages and towns as regards the protection of children against negative influences.*

The Act will not affect the 2004 state budget. Its impact on the budgets of municipalities and the VÚCs will be varied, depending on whether average standard per pupil in a municipality or the VÚC set according to the new act is higher or lower than the funds per pupil allocated from the state budget before. Since, in 2004, the volume of funds for regional education will rise, the effect of the new Act on the budgets of municipalities and VÚCs will generally be positive.

The amount of funds allocated to school founders will depend on the number of pupils. Therefore, in the Ministry's opinion, municipalities and the VÚCs will be motivated to use them more efficiently and to rationalise the school network. Likewise, schools should be motivated to providing quality education, as an increased interest in a particular school will lead to more funds. The founders' authority to reallocate a part of the funds during a school year will provide founders with a stronger tool for implementing their own educational policy and affecting regional development. The Minister of the Education believes the new Act on the Financing of Primary Schools, Secondary Schools and School Facilities will ensure transparency and explicit rules in school financing. He thinks this act will play a pivotal role in the reform of primary and secondary schools.

Some teachers think that "narrow-minded standards of any kind may evoke an impression of a more efficient use of funds, but they will, in fact, only adversely affect the quality of the educational process", as the rationalisation will result in more pupils in each class than before and so teachers will not be able to approach pupils individually.

The Act on the Financing of Primary Schools, Secondary Schools and School Facilities has become effective on 1 January 2004.

Evaluation of the Experts' Committee:

The Act on the Financing of Primary Schools, Secondary Schools and School Facilities puts into practise several reform elements. The experts appreciated the standardised allocation system per pupil – i.e. the application of the principle "the money follow pupils". This feature is a positive aspect in financing education. The Act is expected to ensure a better and more transparent use of funds and to create pressure to increase the efficiency of regional schools. This should further be supported by a stronger competition between school operators.

The Experts´ Committee suggested that a similar reform should be adopted for universities.

Media

Recovery Programme of the New Slovak Television (STV) Company's Director (1200 Employees Dismissed, Program Production Reduced, STV Moved into Smaller Building)

Following the recommendation of the STV Council supported by seven out of its nine members, in mid January 2003 the Slovak Parliament, with 125 votes, elected Mr Richard Rybníček the new company director (CEO) of the Slovak Television (STV). Mr Rybníček, the STV's thirteenth man in the position, did not keep anybody waiting with his first decision: he laid off statutory representatives and appointed members of the Crisis Management. Next, he abolished the much-criticised "gold cushion" for the TV management, i.e. exorbitant severance payments to employees at the first and second level of the company management. These are now only entitled to standard severance payments in accordance with the Labour Code, i.e. to two average monthly salaries. In early May Mr Rybníček also terminated about 100 articles of the 2002 Collective Agreement (note: by the HESO Project evaluated as the second worst measure in 3/2002), which guaranteed many extraordinary advantages to the employees and laid an inadequate financial burden on the institution.

In order to decrease the STV's indebtedness, a number of restrictive measures followed. First, the Crisis Management temporarily centralised financial flows. More efficient use of vehicles (technical and production staff will from now on use a single vehicle for business trips), more efficient HR management, cancellation of some programmes, and no new agreements are together expected to save annually about Sk 5m. Tenders totalling Sk 50m were suspended, travel reimbursements that will not be paid to 176 employees should bring home about Sk 500,000. A contract was terminated with a firm that employed 2 workers for shovelling snow 24 hours a day in the winter. Furthermore, a contract giving Arbo Media exclusive rights for selling advertising time was cancelled, as the CEO found it disadvantageous, causing hundreds of millions of losses. If not terminated, the contract would have lapsed on 31 December 2003. Besides the contract with Arbo Media, the former STV management signed a number of other inconvenient agreements for a definite period of time that could not be terminated. In January and February 2003 STV received invoices from production firms, concluded by the members of the previous management in late 2002, totalling Sk 90m. (Based on its audit, STV was advised not to sign any other similar agreements). The CEO decided to submit these, and all other similar, invoices to the Financial Police. He described the situation in the STV archives as catastrophic and initiated criminal proceedings for the negligence of the archives and set aside Sk 500,000 for saving the works preserved by copying them onto digital media. Not the least, with effect till the end of June, the new CEO limited remuneration to external creative staff to the minimum level, which provoked storms of protests from the Association of Film and TV Directors, a part of the actors' community and TV translators.

Without doubt, more discussed measures taken by the new CEO included the layoff of great numbers of STV employees, limiting own TV production and the STV's new financing. Having the support of the STV Council, in March 2003 Mr Rybníček announced the so-called Emergency Regime, which was supposed to have lasted until the end of the year. Mr Rybníček argued that at the then level of indebtedness (Sk 650m), without taking recovery measures, the STV would have collapsed. The Recovery Programme included restrictions in the STV's own production and a radical cut in the numbers of employees. By the end of June, the STV had planned to make 1,200 employees redundant (950 in Bratislava, 150 in Košice and 70 in Banská Bystrica), and succeeded in doing so despite many protests. The management forecasted to save Sk 23m a month on wages and social security payments. The massive layoff was financed through an extraordinary subsidy for restructuring of Sk 250m. The funds were provided by the National Property Fund of the SR (FNM), having been approved by the Cabinet in May 2003. The STV spent Sk 124.4m for severance payments to the redundant staff and the remainder of Sk 125.5m was used for the STV development project, especially, for paying off the losses of previous years (the first stage of writing off of the STV's debt). At present the STV has over 800 permanent employees (versus 420 employees in TV Markíza), of whom 60% are technical and administration workers. With over 800 employees who will ensure the minimum broadcast, the STV will annually save up to about Sk 300m. With regard to a 6-month notice period and in spite of the termination of many provisions in the Collective Agreement, the majority of the redundant employees were entitled to huge severance payments totalling to Sk 250m. The TU thought that a massive decrease in the number of employees together with the miserable status of equipment could lead to the collapse of the STV. Mr Rybníček was also aware of the problem, but was convinced that 800 employees will manage to fulfil their tasks. He admitted, though, to changing the number of redundancies, but not to any significant measure.

Restrictions should also have led to decreasing the production of own programmes by approximately 1,000 hours. In terms of costs, it was to bring Sk 223.8m of savings by the end of 2003 (30% of total annual own production direct and indirect costs). In 2003 the STV broadcast 10,372 hours. Own production made up 9,000 programmes totalling 2,533 hours, of which the company outsourced 3%. The Recovery Programme led to production cuts by 2,453 programmes amounting to 986 hours. The CEO hence planned to save about Sk 181m. Despite all the restrictions, the STV managed to retain its character of a public institution. It increased the number of reruns and the use of archive materials and primarily focused on news casting, reporting, entertainment and sports.

By the end of 2003, the new CEO had also planned to move out of the 28-story building in Mlynská dolina, which was expected to be left nearly empty, and to begin using the premises next to the high-rise. The only offices to be left in the original building were dubbing and broadcasting studios. At present the first stage of the move has been completed, which has, as stated by the STV spokesman, made the use of the high-rise more efficient. The STV currently uses only the lower 13 floors, hence rendering the rest of the building empty, being heated to only minimum necessary levels and being cut from the supply of all other energies. The final solution regarding the premises and redundant fixed assets should be taken by the STV Council this year.

After learning new facts in the first days of the new CEO in the office, the STV Council unanimously supported Mr Rybníček's radical project. The Recovery Programme was also seconded by Mr Ivan Mikloš, Minister of Finance. In May 2003 the STV was granted the already mentioned one-off subsidy of Sk 250m for severance payments to 1,200 employees and for debts. In mid December 2003 the Cabinet consented to further means (from the state financial assets) of Sk 400m for settling the most pressing debts from previous periods (the second stage of writing off of the debt). The remaining liabilities were supposed to have been paid by the STV from its own resources and from savings achieved when paying off old debts (e.g. by negotiating penalty exemptions or the decrease of principal) or from operational profit. In 2003 the STV asked for a subsidy from the state budget of Sk 987m for a final one-off write off of the STV's debt (including severance payments) provided that the STV would not require any further operational subsidies in future, nor would it generate any new debts.

Critics, however, expressed concerns about a potential influence of one of the private television companies, where some of the members of the Crisis Management had worked before, as well as about a conflict of interest.

The CEO asserted that as from 2004 the STV was to be able to produce and broadcast new programmes and to finance its activities solely from its own resources (including advertising) and from subscribers' fees. This aim has been achieved. The fees have been raised by the amendment to the law drawn up by the Ministry of Culture of the Slovak Republic (see HESO 2/2003), increasing it by 33%, from Sk 75 to Sk 100 (in the case of radio fee, from Sk 30 to Sk 40). The amendment also restricted the number of people entitled to the exemption. Pensioners comprised the largest group of people who has not had to pay the fee, who, as from 1 July 2003, were to pay the fee at a half rate. The new CEO has also decided to cut off the STV financing from the state budget, however, admitting to the possibility that some selected programmes may be subsidised, e.g. broadcasting from the Parliament sessions. Mr Rybníček's intention in all his measures was to make the STV stop producing losses as from 2004.

In the beginning of 2003, Slovak Television found itself in a critical financial position. In 2002 it had produced a loss of Sk 380m, the sum of its losses for previous periods as of 31 December 2002 totalled Sk 689m (trade liabilities amounted to Sk 584m). Together with new liabilities, the debt was nearing Sk 1bn. Moreover, the STV was sued for approximately Sk 625m, including penalties. The annual company's budget was about Sk 1.5bn, Sk 635m of which was consumed by wages and salaries, including social security payments. At the beginning of 2003 the company was short of Sk 20m per month of working capital. If the new management had wanted to pay off the company's old debts by the end of 2003, it would have had to expend Sk 76m a month throughout the year.

Evaluation of the Experts' Committee:

The experts assessed the new CEO's Recovery Programme very positively. Likewise, they appreciated his pioneering attempt to carry out changes in the STV, which were regarded as revolutionary. Prior to the changes, the STV was a company on the verge of loosing its ability to compete, suffered from great redundancies in terms of employees, and had low quality TV programmes and blamefully inefficient use of its resources. The action taken by the new STV boss was inevitable and the harshness of his measures directly related to the length of the period when the adoption of the recovery programme had been put off. The STV had long been neglected, its indebtedness disregarded. Hence, the debt had been growing as the Government constantly paid for it *(see, e.g., HESO 2/2001, 2/2002)*. The management of a public institution must reflect financial criteria and evaluate its achievements. A success of the STV restructuring to an efficiently operating institution would give a lesson to the whole state administration and serve as an example of transformation for all inefficient state companies (e.g., the Slovak Rail). A high accumulation of changes in the STV requires a high quality and resilient crisis management. The support provided by politicians and the STV Council was welcomed. It showed that many were aware of the catastrophic situation in the STV, however, few knew how to deal with it, or had enough strength and will to do so. The experts hope that the previous STV managements will be held accountable for the situation they caused in the company. It will also be important to begin lawsuits against those who are responsible for inconvenient contracts. Terminating the contracts is not enough. A positive aspect was the cancellation of the extraordinarily high severance payments to the STV management. However, it is deemed necessary to also curb unsubstantiated advantages to all STV employees approved by the previous company management and included in the Collective Agreement, as it is immoral to make severance payments from taxpayers' money, prolong vacation or shorten working time in excess to what is stipulated by law. In the experts' opinion, the new CEO has not yet presented his vision of the STV as a public institution in new economic circumstances. Some experts are therefore sceptical in terms of whether such a vision exists and whether there is a concept defining to what degree "the new STV" is to be a public institution and to what degree it is to undertake commercial activities. A new concept of the STV's public character, and a new method of financing arising therefrom, will have to be set.

Several experts expressed a negative opinion on two issues: rise in subscribers' fees (regarded as an additional tax burden laid on households), which was a part of the recovery package, and provision of funds for severance payments to employees from the state budget. The STV restructuring should, in their opinion, be funded from the company's internal resources. The only systemic solution would be the transformation of the STV from a public institution to a business enterprise, privatising it and removing compulsory subscribers' fees.

After long years of generating losses, in 2003 for the first time the STV produced a profit of Sk 84.3m (in 2002 its loss reached Sk 410m). The revenues soared by 30%, reaching Sk 472m on the previous year. This substantial increase was mainly achieved through increasing subscribers' fees, as from 1 August 2003, by about 33% and through curbing the number of people exempt from the fees (the number of payers has risen by 210,000 people). The main sources of revenues were: subscribers' fees of Sk 1.179bn, operational subsidies of Sk 367.7m and the sale of advertising time of Sk 199.2m. Compared to 2002, the total expenses dropped by Sk 22.5m, with major savings in wages and salaries, in 2003 down by Sk 122m. Thanks to restrictions regarding overhead and production of programmes during the crisis regime, savings were also achieved in purchases consumed and services.

As the first Slovakia's electronic media company, CRA Rating Agency included the STV in its ratings. The agency appreciated the changes adopted by the new management and gave the company a positive rating in terms of its prospects, which is very high in terms of local circumstances and is at the level of Slovakia internationally.

Members of the Experts´ Committee

Register contains names of all experts who have participated in minimum one quarterly evaluation in 1/2003 – 1/2004.

Rudolf Autner, Slovak Rating Agency, Inc.
Martin Barto, Slovenská sporiteľňa, a.s. (Slovak Savings Bank)
Vladimír Benč, SFPA - Slovak Foreign Policy Association, Prešov (NGO)
Mário Blaščák, Ľudová banka (Volksbank), a.s.
František Bruckmayer, AZZZ SR - Federation of Employers´ Associations of the Slovak Republic
Daneš Brzica, Institute of Slovak and World Economics of the Slovak Academy of Sciences
Konštantín Čikovský, weekly economic magazine TREND
Igor Daniš, Faculty of Management of the Comenius University, Bratislava
Dušan Deván, SITA - Slovak News Agency
Zora Dobríková, Comenius University, Bratislava
Petr Dufek, Československá obchodní banka, a.s., Czech Republic
Alica Ďurianová, economic daily newspaper Hospodárske noviny
Mária Frühwaldová, PricewaterhouseCoopers Slovakia, Ltd.
Peter Gajdoš, KOZ SR - Confederation of Trade Unions of the Slovak Republic
Milan Galanda, ZPLD - Association for Support of Local Democracy (NGO)
Peter Goceliak, Association of Asset Management Companies
Peter Gonda, M.R.Štefánik Conservative Institute (NGO)
Slavomír Hatina, Slovnaft, a.s.
Peter Havlik, The Vienna Institute for International Economic Studies (wiiw) (NGO), Austria
Igor Hornák, OTP Banka Slovensko, a.s.
Igor Hurčík, Slovak Telecom, a.s. (previous occupation: Deloitte & Touche Slovakia, Ltd.)
Martin Chren, F.A.Hayek Foundation (NGO)
Marek Jakoby, M.E.S.A. 10 - Center for Economic & Social Analyses (NGO)
Martin Jaroš, daily newspaper SME (previous occupation: daily newspaper Pravda)
Juraj Javorský, daily newspaper SME
Anton Jura, U.S. Steel Košice, Ltd.
Eugen Jurzyca, INEKO - Institute for Economic and Social Reforms (NGO)
Peter Kasalovský, economic daily newspaper Hospodársky denník, Economic Club (NEF - Informal Economic Forum)
Róbert Kičina, PAS - Business Alliance of Slovakia
Tomáš Kmeť, Investors Group Inc., Calgary, Canada
Lýdia Kokavcová, weekly magazine of economics, politics and society Formát
Jozef Kollár, Ľudová banka (Volksbank), a.s.
Róbert Kopál, AOCP - Slovak Association of Securities Dealers
Ján Kovalčík, TREND Analyses
Adriana Krnáčová, Transparency International - Czech Republic (NGO)
Juraj Lazový, entrepreneur
Branislav Lichardus, VŠM – College of Management in Trenčín, Bratislava, Poprad
David Marek, Patria Finance, a.s. - investment bank, Czech Republic
Katarína Mathernová, World Bank, Washington, U.S.A.
Grigorij Mesežnikov, IVO - Institute for Public Affairs (NGO)
Peter Mihók, SOPK - Slovak Chamber of Commerce and Industry
Marián Minarovič, ÚMS - Union of the Towns and Cities of Slovakia
Karol Morvay, M.E.S.A. 10 - Center for Economic & Social Analyses (NGO)
Jozef Mrva, ZMOS - Association of Towns and Communities of Slovakia
Milan Muška, ZMOS - Association of Towns and Communities of Slovakia
František Okruhlica, University of Economics, Bratislava
Pavol Ondriska, Slávia Capital, o.c.p., a.s. – security broker, investment company
Vítězslav Palásek, Agency for Social Analyses "ASA", Ltd.
Viliam Pätoprstý, Unibanka, a.s.
Miroslav Plojhar, Newton Holding, a.s. - financial non-banking group, Czech Republic
Ivan Podstupka, daily economic newspaper Hospodárske noviny
Ivan Polakovič, fortnightly economic magazine Profit
Juraj Porubský, daily newspaper Pravda
Róbert Prega, Tatra banka, a.s.
Igor Rintel, Coopex Holding
Andrej Salner, SGI - Slovak Governance Institute (NGO)
Emília Sičáková - Beblavá, TIS - Transparency International Slovakia (NGO)
Miroslav Siváček, OPEN, Association of MBA alumni
Juraj Stern, SFPA - Slovak Foreign Policy Association, Bratislava (NGO)
Jozef Stránsky, Trade Union of Workers in Banking and Insurance Industry
Zdenko Štefanides, Všeobecná úverová banka, a.s.

Martin Štefunko, Institute for the Free Society (NGO), Centre for the New Europe, Brussels (NGO), Belgium
Martin Thomay, Institute for the Free Society (NGO)
Ján Tóth, ING Bank N.V.
Luboš Vagač, Center for Economic Development (NGO)
Katarína Vajdová, NPOA - Foundation for Support of Civic Activities (NGO)
Milan Velecký, weekly economic magazine TREND
Tomáš Velecký, daily newspaper SME
VIPA - civic association The Rural Parliament
Peter Višváder, daily newspaper Národná obroda
Jaroslav Vokoun, Institute of Slovak and World Economics of the Slovak Academy of Sciences
Helena Woleková, SOCIA – Foundation for Support of Social Changes (NGO)
Daniela Zemanovičová, TIS - Transparency International Slovakia (NGO)
Eduard Žitňanský, www.Profini.sk - internet daily of Slovak and world economics (previous occupation: fortnightly economic magazine Profit)
Robert Žitňanský, critical weekly magazine Domino fórum

All experts have participated in the HESO project for no reward.

Ranking of All Evaluated Measures in 1/2003 – 1/2004

*Note: Measures, which are mentioned and described in this publication, are **bold**.*

	***All Evaluated Measures** ranked by Rating Values* *(i.e. Contribution to the Economic and Social Development)*	RATING *[-300; 300]*	Quality *[-3; 3]*	Impor-tance *(%)*	Evaluated *(q/year)*	Passed *(q/year)*
1.	Slovak Parliament Ratified the Treaty of Accession to the European Union	**219,3**	2,31	94,9	3/2003	3/2003
2.	Slovakia's Accession to the North Atlantic Treaty Organisation (NATO) Ratified	**176,5**	2,26	78,0	2/2003	2/2003
3.	**Strategy for Public Finance Management Reform (More Transparency, Hard Budget Constraints, Program Budgeting, Mid-Term Macroeconomic Framework)**	**170,6**	2,26	75,4	2/2003	2/2003
4.	**Draft Amendment to the Labour Code**	**157,2**	1,94	81,1	1/2003	2/2003
5.	Proposal for Measures to Improve The Efficiency of the Companies Register (Certificate of Incorporation within 5 Days, Implementation of Standard Forms, Agenda Moved from Judges towards Higher Judicial Officials, Gradual Transition to Comprehensive Electronic Communication)	**153,7**	2,79	55,2	2/2003	2/2003
6.	**New Income Tax Act (Introduction of Flat Income Tax - 19%, Higher Tax Deductibles, Lump-Sum Tax Abolished, Introduction of 'Lump-Sum Expenses' for Tradesmen, Tax Assignment - 2%, Extra Tax Rate and Dividends Tax Abolished, Simplified Tax Legislature, Exemptions and Tax Reliefs Minimised)**	**142,6**	1,69	84,4	4/2003	4/2003
7.	**Social Insurance Act (Reform of the Pay-As-You-Go Scheme, Raising the Retirement Age to 62 Years, Stronger Benefits-to-Contribution Tie, Automatic Pensions Adjustment)**	**133,8**	1,72	77,8	2/2003	4/2003
8.	**New Act on Companies Register (Certificate of Incorporation within 5 Days, Implementation of Standard Forms, Policy Moved from Judges towards Higher Judicial Officials)**	**132,8**	2,40	55,3	4/2003	4/2003
9.	**Amendment to the Act on Budgetary Rules (Strict Budgetary Restrictions for Budgetary and Semi-Budgetary (Subsidised) Organisations, ESA 95 Methodology for Public Administration Sector, Dissolution of Certain Budgetary Chapters)**	**132,8**	2,28	58,1	4/2003	4/2003
10.	Draft Amendment to the Telecommunications Act (Proposal on Compulsory Accession of Competitors to Local Lines of the Leading Operator, Broader Competencies of Telecommunications Authority, Simplified License Administration)	**127,1**	2,29	55,6	2/2003	-
11.	Act on the Establishment of the Special Prosecutor Office and Special Court to Fight Corruption and Organised Crime	**123,1**	2,10	58,5	2/2003	4/2003
12.	Amendment to the Act on the Administration of Taxes and Fees (Simplified and Stricter Tax Collection and Administration, Possibility of Tax Declaration by Means of Electronic Devices)	**121,8**	2,17	56,2	4/2003	4/2003
13.	**Recovery Programme of the New Slovak Television (STV) Company's Director (1200 Employees Dismissed, Program Production Reduced, STV Moved into Smaller Building)**	**115,4**	2,19	52,8	1/2003	1/2003
14.	**Act on Old-Age Pension Savings (Fully-funded Pension Scheme Introduced)**	**112,3**	1,43	78,4	4/2003	1/2004
15.	Obligation for the Members of Police Force and Customs Officers to Declare Property	**111,2**	2,19	50,8	1/2003	2/2003
16.	Introduction of the so-called Key Witnesses (Amendment to the Code of Criminal Procedure)	**102,7**	2,11	48,6	2/2003	4/2003
17.	**Real Estate Register on the Internet (Authorised Access, Paid Services)**	**101,5**	2,06	49,3	1/2004	1/2004
18.	Amendment to the Criminal Code (So-Called "Three-Strikes-and-Out" Principle, Unconditional Life Imprisonment (without Parole), Bigger Punishments for Murder Crimes, Money Laundering, Corruption, Ban on Human Cloning)	**99,8**	1,62	61,7	1/2003	2/2003
19.	Amendment to the Civil Code (Two-Year Warranty Periode, Consumer Contracts Introduced)	**99,2**	1,76	56,5	1/2004	1/2004
20.	**Concept for Pension Scheme Reform (1st Pay-As-You-Go Pillar, 2nd Fully-funded Pillar, 3rd Pillar of the Voluntary Forms of Pension Insurance)**	**97,4**	1,10	88,3	2/2003	2/2003

21.	**Act on Employment Services (New Instruments of Active Policy on the Labour Market - Motivational and Activation Contributions, Employment Services Provided by Private Agencies, Higher Frequency Attendance at Labour Offices for Inactive Unemployed)**	**96,6**	1,74	55,6	4/2003	4/2003
22.	Introduction of Possibility to Write-off Debts without Debtor's Need to Declare Insolvency	**94,7**	1,93	48,9	1/2003	2/2003
23.	Reduction of the Interest Rates by the National Bank of Slovakia (by 0.5 Percentage Points)	**92,2**	1,73	53,2	1/2004	1/2004
24.	Number of Employees' Work Positions at the Ministry of Finance Reduced by 250 (30%), Dissolution of 44 Organisational Divisions (Procedural and Organisational Audit Project Conducted at the Ministry of Finance)	**89,0**	2,36	37,7	1/2004	1/2004
25.	New Categorisation of Drugs (SKK 1.5bn Savings Expected)	**86,3**	1,61	53,7	4/2003	4/2003
26.	2004 State Budget (State Budgets' Deficit of SKK 78.5bn, Deficit in Public Finances - 3.93% of GDP)	**86,1**	1,08	80,0	4/2003	4/2003
27.	Public Information Portal Občan.sk	**86,0**	2,45	35,1	2/2003	2/2003
28.	Amendment to the Act on Court Executors and Executions Activities (Zero-Tolerance Principle for Serious Crime Offences, Completed Law University Education for Executors Required)	**85,5**	2,12	40,3	3/2003	3/2003
29.	**Act on the Financing of Primary Schools, Secondary Schools and School Institutions (Pupil-Based Budget, Educational Vouchers to Finance Spare-Time Educational Activity)**	**84,9**	1,49	57,0	4/2003	4/2003
30.	**Act on Electronic Communications (Leading Operators' Compulsory Reference Offer for Network Interconnection with Competitors, Broader Competencies of the Telecommunications Authority of the SR, Simplified Entrance into Telecommunications Market)**	**84,4**	1,65	51,0	4/2003	4/2003
31.	Amendment to the so-called Large-Scale Privatisation Act (Final Privatisation of so-called Strategic Enterprises Enabled)	**81,9**	1,34	60,9	4/2003	4/2003
32.	**Tax Reform Concept (Flat Income Tax - 19%, Unified VAT - 19%, Raising Excise Tax, Exemptions Abolished, Tax Legislature Simplified)**	**81,9**	0,96	85,6	2/2003	2/2003
33.	Act on the Mitigation of Material Distress, Act on Subsistence Minimum, Social Assistance Act Amendment (Stricter Provision of Social Benefits, More Directness to Assistance Provided, Incentive and Activating Allowances, Differentiation in Material Distress for Objective and Subjective Reasons Abolished)	**81,2**	1,56	52,1	4/2003	4/2003
34.	Act on Liability for Damage Caused in the Exercise of Public Power (State and Self-Governing Bodies' Liability for Damage Caused by Unfair Decision, Compensation for Damage)	**80,3**	1,82	44,2	4/2003	4/2003
35.	Strategy for Reform of Employment in the Public Sector (Tariff Salaries in Public Service Abolished, Point-Based Job Performance Appraisal System in Civil Service along with Tariff Salary, Introduction of so-called Nominated Civil Service, Zero-Tolerance Principle to Corruption, Ethics Code)	**79,9**	1,49	53,7	2/2003	2/2003
36.	Draft Amendment to the Act on Notaries and Notarial Activities (Proposal to Abolish Regulation of Number of Notary Offices)	**79,6**	2,22	35,8	1/2004	-
37.	Resolution of Slovak Parliament on European Unions' Draft Constitution	**77,1**	1,14	67,4	3/2003	3/2003
38.	Estate Expropriation according to Market Value (Amendment to the Act on Territorial Planning and the Construction Code)	**75,4**	1,84	40,9	3/2003	3/2003
39.	**State Subsidy of SKK 6.5 bn in Case of PSA Peugeot Citroën Investment in Trnava**	**73,7**	1,29	57,0	1/2003	1/2003
40.	National Electronic Communications Policy	**73,4**	1,46	50,1	1/2003	1/2003
41.	Parliament's Resolution to Apply Transition Periods on Free Movement of Labour in EU Member Countries Starting May 1st, 2004 (Disagreement of the Slovak Parliament with Old EU Members' Protective Measures against New EU Members on Labour Market)	**69,3**	1,93	35,9	1/2004	1/2004
42.	New Price Measure in Health Care Systems (Cut in Floor Prices and Increase in Ceiling Capitation Prices, Increase in Ceiling Point Price, Increase in Service Prices for Small Hospitals, One-Day Surgery Extension)	**69,3**	1,37	50,8	2/2003	2/2003
43.	Validity of 10 and 20 Heller Coins Terminated	**67,7**	2,13	31,7	4/2003	4/2003
44.	Amendment to the Act on Civil Service, Act on Remuneration of Certain Employees for Work in the Public Interest, Act on Performance of the Work in the Public Interest (Tariff Salaries in Public Service Abolished, Point-Based Job Performance Evaluation System in Public Service along with Tariff Salary, Introduction of so-called Nominated Civil Service, Ethics Code, Zero-Tolerance Principle in Corruption)	**67,7**	1,49	45,5	4/2003	4/2003

45.	Project for the Further Decentralisation of Public Administration and Draft Concept for the Organisation of Local State Administration (Further Competencies Transferred, Abolition of District Offices from 2004, Local State Administration Offices and Offices of Specialised Local State Administration Created)	**66,4**	1,07	62,3	2/2003	2/2003
46.	New Act on Public Procurement (Harmonisation with European Union Law, Stricter Conditions on Using Negotiation Process without Making Public, Joint Procurement)	**65,9**	1,47	45,0	4/2003	4/2003
47.	Amendment to the Act on Postal Services (Harmonisation with EU Legislation, Liberalisation of the Community Postal Services Market)	**63,4**	1,61	39,4	4/2003	4/2003
48.	**Introduction of Employers' Obligation to Pay Sickness Insurance Benefits in First 10 Days of Employee's Sickness Leave (Act on Income Compensation in the Event of an Employee's Temporary Sickness Leave)**	**63,3**	1,19	53,2	2/2003	4/2003
49.	Strategy for the Informatisation of Society in Slovakia	**62,0**	1,16	53,5	1/2004	1/2004
50.	Proposal on Dissolution of Some Professional Chambers Established by the Law	**61,2**	1,59	38,5	3/2003	3/2003
51.	Number of Job Positions in Regional and District State Administration Offices Reduced by 5% as of 1st July 2003	**59,2**	1,69	35,1	2/2003	2/2003
52.	Refunding Part of the Compulsory Insurance for the Period Vehicle Being Decommissioned (Amendment to the Act on Compulsory Car Third Party Liability Insurance)	**56,0**	2,17	25,8	1/2003	1/2003
53.	Refund of Excess VAT Paid to be Received within 6 Months (Amendment to the Act on VAT)	**53,8**	1,27	42,4	2/2003	2/2003
54.	Amendment to the Act on Administrative Fees (Rates Adjustment, Introduction of Extra Fee for Speeded-up Entry into the Real Estate Cadastre)	**52,9**	1,19	44,5	4/2003	4/2003
55.	Project for the Transformation of the Subsidised (Semi-Budgetary) Organisation Slovenská Správa Letísk (Slovak Airports Administration) (Creation of 6 Airport Companies with State and Local-Governmental Interest; SAA Dissolution; Privatisation of Airports)	**52,4**	1,52	34,5	1/2003	1/2003
56.	Block of 12 Measures Adopted in Connection with Looting of Roma Community (Allowances for Public Jobs and Graduate Practice Increased by SKK 500 to SKK 1 500; Repressive and Preventive Fight Against Usury - Possibility of Allowances Payout more Frequently in the Month and Allowances Paid in Kind; Bonus to Organisers of Major Public Job Projects Increased; Grant for Education of the Long-Term Unemployed Person with Individual Disadvantage, Amounting up to SKK 10 000)	**51,6**	1,13	45,9	1/2004	1/2004
57.	Airport Companies Act (Transformation of the Slovak Airports Administration Authority into Six Individual Joint Stock Companies Operating Airports, Partial Privatisation of Airport Companies Allowed)	**51,4**	1,52	33,7	1/2004	1/2004
58.	New Act on Slovak Television (STV) and Act on Slovak Radio (SRo) (Transfer of State-Owned Property Administered by SRo and STV to their Ownership, Entrepreneurial Activities Enabled, Establishment of the Supervisory Committees, General Directors Elected by Councils)	**51,2**	1,49	34,4	4/2003	4/2003
59.	Act on Probation and Mediation Officers (Institute of Probation and Mediation Officers Established)	**50,9**	1,62	31,5	4/2003	4/2003
60.	Reduction of the Interest Rates by the National Bank of Slovakia by 0.25 Percentage Points	**50,1**	1,17	42,9	3/2003	3/2003
61.	Dissolution of the National Labour Office, Local Labour Offices, Social Departments of Regional and District Offices; New Head-Office and Territorial Offices of Labour, Social Affairs and Family Created (Act on State Administration in the Fields of Social Affairs, Family and Employment Services)	**49,6**	1,02	48,5	3/2003	4/2003
62.	**Liberalisation of Prices in Compulsory Third-Party Liability Insurance (Amendment to the Act on Compulsory Motor Third Party Liability Insurance)**	**48,7**	1,20	40,6	3/2003	3/2003
63.	Sale of Buildings and Land of Relocated Medical Facilities in Bratislava with Public Participation	**47,6**	1,74	27,3	3/2003	3/2003
64.	**New Act on Property Transfer Tax (Flat Rate Tax 3%, Inheritance and Gift Tax Abolished)**	**47,0**	1,08	43,6	4/2003	4/2003
65.	Six Per Cent Raise in Pensions	**46,8**	1,02	45,7	2/2003	2/2003
66.	Additional Funding to Cover Operational Costs of the Regional Education Sector in 2003 (SKK 756m)	**44,4**	0,92	48,3	3/2003	3/2003
67.	Proposal on Appointment of Heads and Directors of Local State Administration Offices by Departmental Minister on the Basis of Selection Procedure Results	**44,3**	1,23	36,2	1/2004	-

68.	**Governmental Support to Hyundai/Kia Motors for the Construction of the Car Plant near City of Žilina Amounting to SKK 8,83bn (Contract between Hyundai and Slovak Government)**	**44,2**	0,80	55,2	1/2004	1/2004
69.	Shortening the Patent Rights Period for Original Medicines from 10 to 6 Years (Amendment to the Act on Medicines and Medical Devices)	**44,0**	1,25	35,2	2/2003	3/2003
70.	New Act on Elections to the National Council of Slovak Republic (Parliament) (Increasing the Weight of Preferential Votes, Voting from Abroad Allowed, Election Deposit of SKK 500 000 Introduced, State Subsidy for Political Parties according to the Poll Increased to 1% of Average Monthly Salary, Election Campaigns in Private Electronic Media Allowed, Pre-Election Moratorium Abolished, One Day Elections, Single Electoral District, No Quotas for Women in Parliament)	**42,6**	0,73	58,8	1/2004	2/2004
71.	Cancelling the Railway Service on 25 Regional Railway Tracks	**39,3**	0,89	44,4	1/2003	1/2003
72.	Four Per Cent Raise in Pensions as of February 2004 (Further Raise in December 2004)	**38,0**	0,80	47,7	4/2003	1/2004
73.	National Investment Support Strategy	**37,9**	0,74	51,3	4/2003	4/2003
74.	Reduction in Number of Slovak Trade Departments Abroad and their Employees and Cancelling the Representation of Slovak Private Companies' Delegates Under the Auspices of the Ministry of Economy of the SR	**36,0**	1,19	30,2	1/2003	1/2003
75.	Dissolution of Children's and Youth Fund	**35,9**	1,78	20,1	3/2003	4/2003
76.	Update of the New Project for the Construction of Motorways - Construction of the Motorway across the North of Slovakia	**35,8**	0,54	65,8	1/2003	1/2003
77.	Reduction of Interest Rates by the National Bank of Slovakia (by 0.25 Percentage Points)	**34,0**	0,81	41,8	4/2003	4/2003
78.	Act on Regional State Administration Offices and Local State Administration Offices (Structure of 79 District State Administration Offices Abolished, New Organisation of the Local State Administration, Offices of Specialised Local State Administration Created)	**33,7**	0,57	59,2	4/2003	4/2003
79.	Restoring the Railway Service on 9 Regional Railway Tracks	**33,2**	1,05	31,6	2/2003	2/2003
80.	**New Child Allowance Act (Flat Amount of Child Allowance SKK 500 per Child, Tax Bonus SKK 400 per Child)**	**33,2**	0,71	46,5	4/2003	4/2003
81.	Health Care Sector Debts to be Settled by State Owned Joint Stock Company Veriteľ	**32,8**	0,65	50,7	4/2003	4/2003
82.	Update of the Project for the Construction of Motorways and High-Speed Roads (Motorway in the North of Slovakia by the Year 2010 - 60% of Total Investment, High-Speed Road in the South and Central Slovakia - 40%, Planned High-Speed Road in the South, Involvement of Private Capital in the Construction)	**32,2**	0,52	62,3	2/2003	2/2003
83.	Abolishment of the Rule Allowing Privatisation Incomes to be Used to Finance so-called Significant-Investments (Amendment to the so-called Large-Scale Privatisation Act)	**30,7**	0,73	41,9	1/2004	2/2004
84.	Agreement between Slovak Government and European Commission on Excess Steel Production Limits in U.S.Steel Košice (Tax Breaks Cut by USD 70m, Extra Tax Payment to State Budget Amounting USD 32m)	**30,6**	0,91	33,5	1/2004	1/2004
85.	The Slovak Television Company Allowed to Carry Out For-Profit Business Activities (Amendment to the Act on Slovak Television)	**28,6**	1,03	27,6	3/2003	3/2003
86.	Bank Slovakia Sold (60% of Shares for SKK 360m)	**28,5**	1,40	20,4	2/2003	2/2003
87.	Cutting the State Premium on Construction Savings Scheme from 20% to 15% (Draft Amendment to the Construction Savings Act)	**26,3**	0,65	40,3	1/2003	2/2003
88.	Raising Regulated Prices by Regulatory Office for Network Industries	**26,1**	0,41	63,7	4/2003	4/2003
89.	**Strategy of the Ministry of Finance of the SR and the National Bank of Slovakia for the Adoption of the Euro in the Slovak Republic (Euro Implementation in years 2008-2010)**	**23,3**	0,29	79,0	3/2003	3/2003
90.	13th Salary to Public Employees in 2003 not Paid (Amendment to the Act on Public Service)	**21,6**	0,67	32,4	2/2003	2/2003
91.	Attorneys Act (Unification of the Chamber of Commercial Lawyers of the SR with the Slovak Chamber of Attorneys, Compulsory Membership in Chamber Preserved, Zero-Toleration of Crime Principle for Attorneys, Market Opened to Foreign Attorneys-at-Law)	**17,4**	0,53	33,0	2/2003	4/2003
92.	Proposal to Abolish the Limits on Political Parties' Election Campaign Expenditures	**16,7**	0,40	41,7	3/2003	-
93.	Uniform Cigarette Prices Introduced (New Act on Excise Duties on Tobacco Products)	**16,5**	0,51	32,1	1/2004	1/2004

94.	**Uniform VAT Rate at 19% Introduced (Amendment to the Act on Value Added Tax)**	**13,6**	0,19	71,3	2/2003	3/2003
95.	Abolishing the Duty for Drivers to Use Winter Tires	**12,3**	0,38	32,0	4/2003	4/2003
96.	Hotel Forum Sold (for SKK 425m)	**9,2**	0,50	18,4	2/2003	2/2003
97.	Sale of Receivables of Slovenská Konsolidačná a.s. (Slovak Consolidation Agency) with Nominal Value SKK 42bn for SKK 862.2m (2.05 Per Cent Return)	**8,8**	0,26	34,4	4/2003	4/2003
98.	Raising Viewers and Listeners´ License Fees for the Slovak Television and Slovak Radio by 33%	**7,0**	0,20	35,7	2/2003	2/2003
99.	Twelve MiG-29 Supersonic Fighter Jets Upgrade	**2,6**	0,09	28,9	1/2004	1/2004
100.	Minimum Wage Increase to SKK 6 080 (by 9.2 Per Cent, SKK 510)	**-0,5**	-0,01	42,7	3/2003	3/2003
101.	Privatisation of State Owned Steam-Gas Energy Producer Paroplynový Cyklus Bratislava, a.s. (90% Share for SKK 2bn)	**-1,9**	-0,06	29,8	1/2004	1/2004
102.	**Raising Excise Tax (on Mineral Oils, Beer and Tobacco)**	**-3,7**	-0,07	55,7	2/2003	3/2003
103.	Establishment of the János Selye University in Komárno	**-8,0**	-0,31	25,4	4/2003	4/2003
104.	Increasing State Subsidy for PSA Peugeot Citroën by SKK 408.5m	**-8,1**	-0,20	40,7	3/2003	3/2003
105.	Introduction of Duty for Drivers to Use Winter Tires (Amendment to the Act on Road Traffic)	**-12,9**	-0,39	33,3	3/2003	3/2003
106.	Governmental Subsidy for Farmers to Cover Losses in Production Caused by Unfavourable Climatic Conditions (SKK 400m)	**-15,5**	-0,37	42,1	3/2003	3/2003
107.	Payment of the Lump Sum Benefit of SKK 1000 to Pensioners in order to Compensate the Impact of Reforms from the start of 2004	**-16,7**	-0,44	38,0	1/2004	2/2004
108.	**Buying out the Slovak Railway Companies' Debt by the Government Amounting to SKK 21bn**	**-21,4**	-0,51	41,8	3/2003	3/2003
109.	The Centre for Securities of the Slovak Republic Transformed into Central Securities Depository of the SR (Membership Principle; Two-Level Recordkeeping of Book-Entry Securities; Stock Market Collapse for Several Days)	**-23,7**	-0,63	37,9	1/2004	1/2004
110.	**Act on Retail Chains (Stronger Regulation of Supermarkets)**	**-38,5**	-0,96	40,3	3/2003	3/2003
111.	**Direct Payments to Slovak Farmers Amounting to 52.5 Per Cent of EU Level**	**-38,7**	-0,76	50,7	4/2003	4/2003
112.	So-called Parliamentary Indemnity Extended (Disallowing Civil Law Protection Against Members of Slovak Parliament for their Statements Presented in Parliament, Amendmend to the Constitution of the Slovak Republic)	**-39,2**	-1,20	32,7	1/2004	1/2004
113.	Conduct of Tender for the Supply of Information System for the Social Insurance Agency (Signed without Approval of the Government)	**-45,6**	-1,71	26,7	2/2003	2/2003
114.	Contracts on Consulation Services for Gas Distributor SPP (Slovak Gas Industry) Amounting to SKK 1.2bn	**-47,3**	-1,63	29,1	1/2004	1/2004

Note:

Average Foreign Exchange Rates of the National Bank of Slovakia

Currency	*Amount*	*2003*	*1st Half of 2004*
EUR	1	41,49	40,33
USD	1	36,77	32,86
CZK	1	1,30	1,24