

# **More than Just a Rich Country Club: Membership Conditionality and Institutional Reform in the OECD\***

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## **Abstract**

Conditional membership may be one of the most important sources of leverage for IOs. What underlies the terms of selection and the willingness of applicants to pay the price of entry? The influence of accession conditions has been studied in the context of EU and NATO, where sizable benefits motivate major concessions by applicants. This paper examines a much less powerful organization, the OECD. The organization provides both public goods in the form of policy information and club goods in the form of status. Through a process of self-selection by applicants and screening by members, the organization has managed gradual expansion while preserving its value as an elite club of like-minded states. Informality of accession criteria has allowed flexibility to raise and lower the bar for entry. Statistical analysis highlights broad conditions related to income, democracy, and geopolitics that correlate with earlier entry into the OECD relative to other countries while there are less clear patterns for the role of trade and financial openness. Case studies of Japan, Mexico, Korea, and the Czech Republic are used to examine how prospective OECD membership motivated reforms in regulatory policies and trade. These countries sought to benefit from the status of association with the advanced industrial democracies. On the basis of shared liberal orientation and geopolitical alignment, these outsiders were accepted into the club. At the same time, a case study of Brazil highlights how its refusal to seek OECD membership reflects a political preference to remain distant from the advanced industrial nations even as its economy and policies are more integrated with these states.

# 1 Introduction

The protests in the streets of Ukraine were sparked by the question of whether the government would join an association agreement with Europe or a customs union with Russia. This controversy is about more than the tariff cuts or financial aid promises accompanying either of these agreements. The choice of international agreement became the touchstone event to define the core identity and future direction of Ukraine. Would the country associate with Europe or Russia? The example highlights the fact that entry into international economic agreements is about much more than economic policy. I argue that states join organizations as much for the status of association with a particular group of states as for the need to cooperate on a particular set of policies. This counters the logic of functional theories about the demand for institutions and highlights the nature of selection bias that confronts empirical research on institutions.

The endogeneity of entry into international agreements has been a central challenge to research on institutions. Theories explain the demand for institutions in terms of their ability to resolve information problems and facilitate mutual gains through cooperation. States that stand to gain from cooperation are more likely to choose to establish and join the institutions, which necessarily means that the effect of the institution is in part due to screening effects (Downs, Rocke and Barsoom, 1996; Martin and Simmons, 1998; Simmons and Hopkins, 2005; Lupu, 2013). Analyses of institutional effectiveness that compare members to non-members are subject to criticism for failing to control for the propensity to join the institution. To address these challenges, it is necessary to understand the politics of joining organizations. Research highlights the need to give attention to both the supply and demand side influences on membership decisions when studying accession for organizations including the WTO (Pelc, 2011; Davis and Wilf, 2015b), the EU (Schneider, 2009; Gray, 2009), and NATO (Kydd, 2001). Broad trends for regional patterns in membership decisions are also evident at the aggregate level (Greenhill and Lupu, 2015).

This paper contributes to understanding selection into organizations through investigation of one organization, the Organisation for Economic Co-operation and Development (OECD). I examine how

membership evolves through an informal process of self-selection and screening, and I demonstrate how this process of conditional membership brings policy reform. I challenge the conventional view that states join organizations because of a functional demand for cooperation on the specific policies regulated by the organization. Rather, they join due to common interests that reach well beyond those within the purview of the organization and adopt policies that may not fit their specific economic circumstances. My argument contends that states seek status by associating with a group of like-minded and powerful states. Joining the OECD represents a choice of social category within the international system that brings with it both norms of behavior and benefits for reputation.

The OECD grew out of the Organization for European Economic Co-operation (OEEC), which had been the organization established in 1948 to oversee implementation of the Marshall Plan aid. European governments were divided over the form of European integration with rival positions for an intergovernmental free trade agreement (EFTA) and a more centralized approach to delegate supranational authority within the European Coal and Steel Community, and the OEEC membership was split with seven in the former group and six in the latter. At the same time, the tensions of the Cold War had placed necessity behind efforts to strengthen NATO and even proposals to form an economic council within NATO to take over the OEEC role (Carroll and Kellow, 2011, p. 48). Against this background, twenty countries agreed to transform the OEEC into a new organization that would include the United States and Canada while shifting to focus from European development to a broader mandate of economic cooperation. The organization incorporated the codes of liberalization and peer review monitoring practices that had been central to the OEEC and adopted the goal to achieve fifty percent increase of GNP for the aggregate membership over the first decade from 1961 to 1971 (Carroll and Kellow, 2011, p. 51).

Against this background, the OECD pursues broad mandate to promote development. As such its policy scope extends across a range of different economic policy dimensions including aid, trade, finance, and investment where its mission overlaps with other multilateral and bilateral agreements. It has played a central coordinating role for development aid and stands as the only multilateral organization to develop agreements on bribery and taxation. More broadly, its reports include environmental, labor,

and education policies. Through monitoring reports and production of consolidated data on policies, the organization functions as a think tank and center of information sharing among members and the broader international community.

The organization has weaker enforcement than the WTO but actually appears to have a larger effect on trade liberalization among members. In one study, Rose (2005) finds that OECD membership increases the average value of bilateral trade by over fifty percent, which is more than the increase attributed to belonging to either the GATT/WTO or IMF. In a specification of gravity model that includes dyadic and importer and exporter year fixed effects and controls for membership in alliances and EEC and its successor, Davis and Gowa (2013) find that there is a large, positive, and significant effect of the OECD on bilateral imports; the effect size is almost half the magnitude of that for EU membership, and four times larger than the effect of GATT/WTO participation (the latter is statistically insignificant).

The challenge to understanding the effect of OECD, however, is that selection into the organization is highly correlated with decisions to undertake economic reforms and to improve relations with existing members. On the one hand, trade liberalization prior to joining would cause a downward bias that could mean the above results underestimate the effect on trade.<sup>1</sup> On the other hand, if these reforms are undertaken for reasons unrelated to joining the organization itself, the positive effect attributed to membership is spurious correlation. Membership may screen for those states that already have positive economic reform preferences (e.g. Downs, Roocke and Barsoom, 1996; Von Stein, 2005; Gray, 2009). Furthermore, membership selection is not only a function of economic reform trajectory but also political relations. It is no accident that Turkey was a founding member of OECD because it had been among the recipients of Marshall Plan aid as NATO member, while East European membership in OECD came after the end of the Cold War opened political relations with the West. Democracy has also become a criterion for membership. To the extent that economic reform trajectory, positive political relations with the West, and democracy are all likely to correspond with benchmark measures of economic outcomes such as trade, it is very difficult to identify the causal effect of membership. More understanding of selection

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<sup>1</sup>Rose (2005, p. 688) makes this point directly.

into membership is necessary to provide basis for future research into the value added of institutions.

The evolution of the OECD from twenty founding members in 1961 to thirty-four members today reveals several puzzles. How did an organization with no formal conditions required for accession maintain core features as a group of like-minded countries while expanding beyond its origins as economic counterpart to NATO? Contrary to conventional wisdom, the rich country club includes developing states and has been open to non-democracies as well. Turkey was a founding member, Mexico joined in 1994, and Colombia is currently in accession negotiations. Nevertheless, the OECD remains a small club with high entry barriers. But this presents a second puzzle. Why would countries make reforms on entry to an organization that offers benefits to members and non-members alike? The liberalizing reforms completed by members are nondiscriminatory in their effect, and economic information is widely shared as policy advice. Joining an organization such as the WTO or EU provides differential market access, but in its role as a think tank, OECD services are equally available to all states. It is only through examining the status value of the OECD that one can appreciate the club good nature of the organization that both attracts countries to join and mandates restrictive entry barriers. In addition to income, similarity along the dimensions of democracy and foreign policy underlie the appeal of the OECD brand.

This paper analyzes the OECD accession process with attention to the supply and demand side of the membership decision. I develop an argument about strategic status-seeking in which states choose whom to emulate when deciding to join international institutions. The appeal of closer affinity with the rich democracies of the Western alliance attracts applicants who want closer association. This dynamic allows for more agency by applicant states than is commonly seen in the literature on diffusion where states respond to competitive pressures or common culture and region as basis for policy convergence. At the same time, the supply side restraint, which may be dictated by non-economic considerations at the whim of current members, creates space for agency on the side of the IO such that membership is more than simple reflection of preferences. Existing members act as gatekeepers to exclude those who do not appear likely to fit in the club. Screening on basis of shared democracy and geopolitical alignment assures that peer pressure will be sufficient enforcement mechanism. Those that join must

meet both criteria: preference to become like the advanced industrial democracies and sponsorship by existing members. Using case studies of “outsiders” who join the club, Japan, Mexico, South Korea, and Czech Republic, I illustrate how leaders valued the status of entry as part of rationale for making policy concessions. The Mexican and Korean cases both serve as warnings that the rush to membership can be destabilizing – banking reforms and capital inflows that accompanied membership also laid the conditions for their subsequent financial crises. These accession case studies are contrasted with Brazil’s decision to remain outside the OECD. Among non-member states, Brazil stands out for its broad and sustained engagement with OECD activities. Despite OECD encouragement to consider membership, Brazilian leaders have been reluctant to join the organization.

The next section briefly reviews theories about institutional accession and membership. Then I develop my argument that membership decisions are based on similarity of liberal orientation and positive value to status of association with a like-minded club. Section 4 presents descriptive statistics of the common characteristics of members. In section 5, I analyze selection into the organization with a duration model of time to OECD entry that highlights the importance of political variables. Democracy and geopolitical alignment bring more rapid membership even when controlling for key economic measures and regional location. Trade and financial openness are surprisingly not predictive of which states join the OECD. Using case studies, section 6 explores more closely the decisions to join in terms of the motives of the applicants and the specific policy reforms they agree to undertake as the price of membership. Section 7 discusses the case of Brazil as a potential applicant that weighs association with the OECD as a political cost given its preference to associate with developing countries. Section 8 concludes.

## **2 Conditionality and IO Membership**

**Depth versus Breadth** Making substantial policy reforms in coordination with other states is hard, and some argue larger numbers will only complicate the effort. The classic depth-breadth problem directly raises the question of membership in international organizations. What is the right size of an organization and how should it determine which states are allowed to join?

As a feature of institutional design, membership varies across the dimension of exclusivity and rigidity of entry conditions. These help define whether a subset of countries forms an exclusive “club” or whether a large group of countries aspires to achieve universal membership. Koremenos, Lipson and Snidal (2001, p. 783) write: “If an institutional arrangement restricts the benefits of cooperation to members, actors have an incentive to pay the price of admission to the club. One of the most important features of institutions is to define those boundaries of membership.” Different kinds of cooperation problems give rise to restrictive membership. First, when states face free-riding problems they may opt to restrict membership. In the provision of public goods such as open markets, the non-excludable and non-rivalrous nature of the project gives rise to free-riding because states can benefit equally regardless of their input. A small group can more easily achieve cooperation through joint effort and monitoring. Second, exclusivity is necessary when states face congestion problem for the provision of a club good (Buchanan, 1965; Cornes and Sandler, 1996a). This is the situation when the common project holds some characteristics that are partly rivalrous in consumption, with the classic example being a swimming pool. Here discriminatory pricing can help to reduce entry. Finally, when information is incomplete, membership costs can increase confidence that a state will cooperate once it joins (Koremenos, Lipson and Snidal, 2001, p. 784).

The small-club configuration may also be endogenous to the power distribution. When the interests of the great powers diverge more vis-a-vis other states than amongst themselves, Drezner (2007, p. 67) argues that they will adhere to club standards; “Club IGOs, such as the Group of Seven countries(G7) or the OECD, use membership criteria to exclude states with different preference orderings and bestow benefits for in-group members as a way to ensure collective action.” He points to examples such as the 1997 OECD Anti-Bribery Convention which was quickly concluded among OECD members after a failed attempt to negotiate on this issue at the United Nations (ibid., p. 77). Once negotiated within the smaller group, the United States and Europe effectively exported these standards to a wider range of countries. Gray, Lindstadt and Slapin (2015) contend that the diversity of the founding group of countries determines how the organization will enlarge. Each state calculates whether an entrant could shift the

voting dynamics on policy issues that are regulated, and one would expect organizations that begin with a small and homogenous group to expand by selecting members that would not change nature of the organization.

Expanding membership beyond the small club offers several advantages. Larger membership can promote cooperation by supporting diffuse reciprocity, issue linkage, and broader total gains (Keohane, 1984; Koremenos, Lipson and Snidal, 2001). To the extent that an institution supports the interests of powerful states, it must elicit the cooperation of other states – the more the better.<sup>2</sup> Likewise, theories that emphasize the role of socialization of members as key function of an international institution suggest broader membership will support cooperation (Johnston, 2001).

One solution to this depth-breadth trade-off is to form institutions that involve *similar states* and add other states after convergence of preferences. The small club can maximize cooperation by expanding to the point at which the returns from a new member joining equal the costs. Downs, Rocke and Barsoom (1998) theorize that this form of *sequential liberalization* can achieve the most overall cooperation. Gray, Lindstadt and Slapin (2015) model enlargement scenarios in which the location of the original group and applicants on a unidimensional space determine probability for enlargement.

In a second approach, states construct differential membership through varying the entry conditions and commitments across the membership (Gilligan, 2004). The price of membership changes as a function of their demand curves - an applicant worth more to members will be charged less than the applicant that has little value added for cooperation. In a study of the European Union eastern enlargement negotiations, Schneider (2009) shows that the concessions offered by new entrants varied widely and long transition periods introduced what in effect was discriminatory membership.

**Toward a more comprehensive definition of interests** Enlargement forces decisions about what constitutes similarity of interests. Both the sequential liberalization theory of Downs, Rocke and Barsoom (1998) and functional theories of international institutions (e.g. Keohane, 1984; Martin, 1992; Jupille,

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<sup>2</sup>Stone (2011) connects *voluntary* participation as the foundation of legitimacy for an international organization, but does not focus on the breadth of participation.

Mattli and Snidal, 2013) focus on the preferences and information problems that characterize an issue area. Based on these theories, policies of states *within the issue area of the regime rules* would form criteria for selecting partners for enlargement. One might expect liberal trade policies as condition for participation in multilateral trade rules and security interests to shape alliance participation.

But we observe more complex patterns – where alliance ties determine membership in trade agreements, economic flows influence alliances, and democracy determines both economic and alliance affiliation. For example, Davis and Wilf (2015b) document that geopolitical alignment based on common alliances and similar voting record in the United Nations plays larger role to shape GATT/WTO accession than trade openness or dependence on the markets of member states. Officials of NATO enlargement candidate countries reported selling their application more on basis of political alliance than as defense agreement (Jacoby, 2004, p. 133). McNamara (1999) contends that the choice by countries to join the euro zone depended on political choice more than the interests of economic actors or shifts in capital mobility. More generally, democracy leads states to join IOs and influences the type of organization they join (Mansfield and Pevehouse, 2006, 2009). Many of these decisions regarding some of the most prominent IGOs have been influenced by rationales that are extraneous to the issues directly at stake. As a consequence some states have encountered subsequent problems - the eurozone troubles today as case in point. Others moved forward toward integration that could not have been justified on narrow interest alone. All of the examples illustrate that similarity of interests should be understood across multiple dimensions that exceed the boundaries of interests within the regime issue area.

**The value of association status** States join organizations because they want to form closer bonds with other states, and joining international organizations represents a clear and public means of identifying with a particular group of countries. I argue that states make a strategic choice to associate with fellow states that are similar on dimensions that they view favorably. In the public choice theories of club goods, “discriminatory clubs” account for situations where members consume both the shared good and the attributes of other members (Cornes and Sandler, 1996b, p. 385). As an example, members in a social club care not only for the entertainment activity itself but also about the status of other members.

Discrimination is often based on common characteristics whether race/geography or class/income.

Status by association carries benefits for reputation that are taken seriously by both economic actors and potential security threats. Gray (2013) argues that states achieve a reputation through associating with other states in common regional associations, and demonstrates that private investors cue off of this signal in their assessment of country risk. She finds that association with states holding low risk profile will lower the risk of the new entrant to the regional organization even when controlling for basic economic and policy indicators. Moreover the converse is also true; Gray documents that investors attribute higher risk to those states that join an organization of high risk states. Brooks, Cunha and Mosley (2014) argue that investors look for categories to simplify the process of assigning risk to countries, and they find evidence of peer effects in sovereign interest rates whereby a country is impacted by the rates applied to other countries in its similar region or credit rating group. In security studies, reputation has been examined in terms of alliance credibility for deterrence. Boehmer, Gartzke and Nordstrom (2004) find that membership in structured IGOs with formal rules and procedures reduces the probability of conflict onset. They posit information transmission improves the bargaining environment so that states can avoid conflict. The most pertinent information conveyed by IGO membership is the voluntary decision by a group of states to establish closer relations through their participation in a formal organization.

*Club-style* rules for accession facilitate flexible definition of similar interests in the bargaining process that brings in new members. They can be contrasted with universalistic or meritocratic entry. This type of entry process combines exclusivity with low precision about the conditions to join. Rather than establishing clear objective criteria for accession, states may prefer to decide what issues matter and to determine who qualifies to join the regime at any given time on a case by case basis. From the perspective of institutional design, flexibility for terms of accession corresponds to theories about incomplete contracting (e.g. Abbott and Snidal, 2000; Rosendorff and Milner, 2001). Following this logic, vague provisions in international agreements arise because current members are unable to reach agreement on criteria for membership and because they recognize that their own preferences may change over time. In particular, powerful states will prefer to retain control over membership as key window

for discretionary use of power to shape the organization (Stone, Slantchev and London, 2008; Stone, 2011). In the case of membership, flexibility for terms of accession accommodates the decision to lower standards for one acceding state while raising standards for another. Over time and applicants, members can shift their priorities for what constitutes suitability for membership.

### **3 Selecting for Similar Type in the OECD**

These arguments are at the forefront of decisions about enlargement for the OECD. From a functional perspective, the organization can better serve its own mission to coordinate economic policies for growth and prosperity if it includes more countries. At the end of his term as OECD Secretary General, Donald Johnston made the pointed remark that “how are you going to shape the global economy if you’re basically working with a minority of it”(Woodward, 2009, p. 105). At the same time, inevitably the addition of more countries introduces greater heterogeneity of preferences which can block decisions. Sociological perspectives are also not free of this trade-off. Broadening membership adds further legitimacy and greater weight of peer pressure, but also reduces the sense of community and shared norms. Committee meetings that are overcrowded with participants are less likely to yield discourse and build small-world networks. Finally, the status premium of OECD membership could be lost if the group expands too broadly.

The OECD has undertaken gradual expansion based on similarity across multiple dimensions. Table 4 in the Appendix lists members by year of accession with figures on their income, democracy, and alliances. The accession process involves exclusion through screening mechanisms and attraction through the provision of club goods. The requirement for commitments to liberal economic policies keep out states that would diminish quality within the group. The appeal of association with the rich club attracts states to meet the entry requirements. But this only applies to those countries that share liberal orientation in their foreign policy and political values. Through an informal process, geopolitical alignment with the United States and democratic regime have become conditions of membership.

### 3.1 The OECD Accession Process

The OECD does not establish precise conditions or formal accession process in its rule framework.<sup>3</sup> The OECD Convention sets out the following rules in Article 16:

The Council may decide to invite any Government prepared to assume the obligations of membership to accede to this Convention. Such decisions shall be unanimous, provided that for any particular case the Council may unanimously decide to permit abstention, in which case, notwithstanding the provisions of Article 6, the decision shall be applicable to all the Members. Accession shall take effect upon the deposit of an instrument of accession with the depositary Government.

These general terms allow considerable discretion for the current members to admit or exclude applicants. The OECD typically requires new members to have both market economy and democratic political institutions. Yet founding members included states under authoritarian rule (Spain and Portugal) at the time, and democratic reversals in Greece and Turkey were not grounds for exclusion. Likewise, even as Cyprus has met the demanding conditions for economic and political reforms necessary to join the EU, it remains excluded from OECD due partly to objections by Turkey on basis of tense political relations.

A 2004 agreement in the Ministerial Council Meeting accepted a working group proposal that was intended to provide more specific guidelines for selecting candidates for accession, and yet instead reflects the ongoing discretionary nature of admitting countries to the club. Carroll and Kellow (2011, p. 123) conclude that the criteria for suitability can be boiled down to four points: “there had to be ‘like-mindedness’; the state had to be a ‘significant player’; there needed to be ‘mutual benefit’ from membership; and there had to be regard given to ‘global considerations’, particularly keeping some sort of agreed ‘balance’ between European and non-European members.” The report states that like-mindedness should be judged by fundamental yardsticks for a country having market economy and democratic principles while additional factors should include: economic performance, good governance, human rights, participation in other IGOs, provision of development assistance, and observance of the OECD acquis.<sup>4</sup> The chairman of the working group, Ambassador Seiichiro Noboru expressed dismay at the failure of subsequent Council meetings to consolidate the principles into more concrete admission criteria.<sup>5</sup> But

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<sup>3</sup>See Davis and Wilf (2015a) for discussion of how GATT/WTO also allows considerable discretion over accession.

<sup>4</sup>OECD (2004), “A Strategy for Enlargement and Outreach,” Report by Chair of the Heads of Delegation Working Group on the Enlargement Strategy and Outreach, Ambassador Seiichiro Noboru.

<sup>5</sup>Telephone Interview by author, 28 October 2014.

the OECD member states have chosen to retain their flexibility with informal principles for screening applicants. Ambassador Noboru noted that the European states that seek admission for more EU members favored more explicit requirement for democracy and market economy while Japan, Canada, and Australia were insistent that states need to be significant players, by which they hoped to encourage entry by the BRICS that held larger share of world GDP than the many small EU states seeking entry. The United States wanted to keep the organization small to avoid budget increases, but sought entry for Israel. The report notes explicitly that the “significant player” criteria does not take precedence over “like-mindedness.” Flexibility allows states to navigate such differences among members.

At first it would seem that income represents a critical threshold to define a subset of countries eligible to join. Yet this belies the early membership of Turkey as founding member and entry of Mexico in 1994. Both fall within the World Bank classification category for “upper middle income” developing countries. Furthermore, recent entrants are far down the list of countries in terms of economic size measured by total GDP. Woodward (2009, p. 105) refers to “minnows” like Estonia that ranked between Uganda and Jordan in terms of World Bank rankings of GDP in 2007 when they were invited to initiate accession talks for joining the OECD. Of course, their per capita GDP is much higher. The latest announcement of new candidates for accession issued by OECD in May 2013 included Colombia, with Costa Rica on the list for future expansion.<sup>6</sup> These countries are both poorer on a per capita income basis and smaller in total GDP than Brazil, Malaysia, Russia, and Singapore that are noticeably not joining soon. The other new applicants include Lithuania and Latvia that would join Estonia as small but relatively wealthy entrants.

The European origins of the OECD continue to privilege those from the region even as the organization embraced Japan and Australia early on. Today members span all continents, with the exception of Africa, and South Africa is among the countries involved in the ‘enhanced engagement’ with OECD that is intended to prepare countries for membership. Thus we can see that even while there is a common set of characteristics shaping the organization, they do not represent rigid criteria for democracy, wealth, or location.

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<sup>6</sup>OECD “OECD Partners and Enlargement,” at <http://www.oecd.org/about/membersandpartners/enlargement.htm>.

### **3.2 The price of admission**

The three dimensions for screening out applicants are dues, transparency, and policy reform. The first is the easiest, for despite the label as “rich country club” the OECD has progressive budgeting. Member dues are assessed based on paying a share of the OECD budget according to proportion of national income, such that larger states pay more up to a cap of 25 percent of total budget (Carroll and Kellow, 2011, p. 15). The G7 group of large states provide three-fourths of the core budget and also fund ‘pet projects’ through voluntary contributions (Woodward, 2009, p.46).

The requirement for transparency represents hurdle for some governments. States agree to provide information to the OECD, and thus to expose their performance to public assessment. Although membership in IMF and WTO may have already elicited considerable economic reporting from countries, the OECD economic surveys and other studies are far more wide-ranging in scope. The peer review process builds on this information to provide the primary enforcement mechanism of the organization as states’ policies are examined in detail within a given area with the purpose to evaluate whether the state is meeting the best practice standards that have been established through OECD decisions (Woodward, 2009, p. 57). The widely used economic surveys represent an extensive review of economic data through a process that incorporates the members self-assessment as well as analysis by the secretariat and questioning by other members before completion of a final public report. OECD output ranking governments according to common benchmarks can become ammunition for domestic groups to use against their own government where its progress is found lacking. For states that have record of political interference to ‘cook the books’ of accounting, compliance with objective data categories and reporting represents unwanted transparency.

The most important objective requirement of membership is for the applicant to conform with OECD policies. The Codes of Liberalization (formally two agreements, Code of Liberalisation of Current Invisible Operations and the Code of Liberalisation of Capital Movements) form the core OECD agreements. They embody the commitment of the organization to pursue open trade and capital markets. Lowering trade barriers and establishing convertibility of the currency and free capital movement were primary conditions. The Codes call for more comprehensive liberalization of finance and investment policies than membership in other multilateral economic organizations, although reservations allow for states to carve out exceptions. Subsequent agreements such as the 1994 decision on “National Treatment for Foreign-Controlled Enterprises” and the “Anti-Bribery Convention” have since expanded commitments

to FDI and other areas. In all cases, states are allowed to make reservations that carve out individual exceptions. Governments notify members of their policies related to the Codes, and are subject to peer review. The organization lacks formal procedures for sanctions, and instead relies on a states' concern for reputation and the role of persuasion to shape policy choices.

### **3.3 Why bother? Understanding Demand for Membership**

Many of the public goods provided by the OECD in its role as policy think tank are available to all states. Each year the organization publishes more than 200 reports (Woodward, 2009, p. 57). The organization actively disseminates its reports. Even the peer review assessment OECD Economic Survey has been undertaken by countries that are not members such as China and Brazil. Furthermore, the policy changes enacted by governments to conform with OECD recommendations do not discriminate among members and non-members in their application. When governments seek to liberalize trade and capital according to the Codes of Liberalization, they do so on most-favored-nation basis rather than as preferential access limited to fellow OECD members.

Therefore one must look further to understand why applicants would be willing to jump these hurdles for membership. On the demand side, states seek the benefits of association. Status conferred by membership stands out for importance in the cases of new entrants. While to some the stereotype of the OECD as a 'rich country club' is derogatory, joining the ranks of this group offers an imprimatur of acceptance in the top ranks of international society. In particular, OECD membership means self-identification as an advanced country aligned with the United States and Europe. This status of association is at the same time rival given that more members in the organization will only dilute the signal attained by those who join. As a discriminatory club, the OECD offers both provision of shared goods in the form of policy expertise and regulation, and also the benefits of association that are a function of the status of other members.

From a market perspective, the value of association with the rich club can pay off in real terms through the channel of investor confidence. One benefit from membership that was especially important for the countries that joined in the 1990s came in the form of lower interest rates on capital. Due to rules determined by the Basel Committee on Banking Supervision decision to apply zero risk weighting for bank loans to all OECD governments, accession to the OECD would substantially lower the cost of capital for Mexico and Korea (Claessens, Underhill and Zhang, 2008, p. 317). In part due to recognition that this led to excessive capital inflows into Korea that contributed to its financial crisis shortly after joining

OECD in 1996, the 2004 revision to Basel rules on banking introduced a more complex risk assessment procedure that would end the zero risk weighting for emerging market OECD members that had been enjoyed by Czech Republic, Hungary, Mexico, Poland, Slovakia, South Korea, and Turkey (Ibid., p. 327). Nevertheless, nothing will stop the informal assessment of risk in markets that takes into account OECD membership as a sign of quality. Countries that are considering accession refer to expected improvement in credit as one motivation for joining. For example, on its website the Russian Ministry of Foreign Affairs mentions in the description of reasons for Russia to seek OECD membership “One of the most important functions of the OECD for Russia is the OECD’s determining of states’ credit ratings, on which the borrowing conditions in global financial markets depend.”<sup>7</sup> Similarly Lithuania’s president issued the following statement after a meeting at OECD about its application to begin negotiations for accession: “Joining the OECD would make Lithuania more attractive to foreign investors, improve our debt ratings and reduce borrowing costs.”<sup>8</sup> The OECD does not issue credit ratings or have any direct role aside from the signal of membership.

Market actors responding to uncertainty may rely on the OECD as a brand. The status premium of OECD membership holds value in financial markets and in competition for investment. More generally, the literature has shown that organizational membership can impact country risk ratings and bond yields. Dreher and Voigt (2011) find that independent of the quality of domestic institutions, membership in international organizations improves the risk rating. Gray (2013) argues that investors face uncertainty and rely on cues about countries reliability based on their peer group and provides evidence that membership in international organizations can increase bond ratings. Her theory contends that independent of actual policies, the reputation of a country as measured by bond ratings will rise or fall in accordance with whether they associate with good or poor quality countries in regional economic associations. Yet such branding has its limits. Dreher and Voigt (2011, p. 340) find that the subset of OECD members *do not* receive any boost from their membership in other international organizations. Presumably their status as OECD members and the accompanying features that characterize this unique group obviates any role for

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<sup>7</sup>The Ministry of Foreign Affairs of the Russian Federation. “Rossiia na puti integratsii v mirovuiu ekonomiku: Rossiia i OESR (Russia on the road to integration into the global economy: Russia and the OECD)” (2005, July 19). Retrieved Feb. 2, 2014 from [http://www.mid.ru/ns-vnpop.nsf/osn\\_copy/6ED794F5B1C4B629C325704300315446](http://www.mid.ru/ns-vnpop.nsf/osn_copy/6ED794F5B1C4B629C325704300315446)

<sup>8</sup>Bryan Bradley, “Lithuania Seeks OECD Invitation to Start Accession Talks in May,” Bloomberg (Apr 9, 2013) accessed at <http://www.bloomberg.com/news/2013-04-09/lithuania-seeks-oecd-invitation-to-start-accession-talks-in-may.html>.

additional information from IO membership.

To preserve its brand value, the OECD must remain exclusive. This particular aspect of member benefits exhibits characteristics of a club good subject to crowding effects. Should too many countries be allowed to join, there would no longer be new information from membership status. Expansion to include countries of lower quality on core economic policies would risk damage to reputation of OECD as the gold standard for business environment. To extent that states value the gains from association with a particular high status states, they do not want to allow in those that would lower the stature of the association with OECD.

### **3.4 Seeking status through association**

Beyond improving their credit ratings, states are drawn to apply when they want to become more like the members. Membership offers a direct pathway to follow members policies. The greater access to policy learning is cited by many participants as key benefit of engaging in OECD. In extensive interviews with OECD member governments and the organization secretariat, Carroll and Kellow (2011, p. 38) remark that all without exception emphasize policy learning. Being “in the room” for committee meetings and technical discussions matters for both influence to shape the output of decisions and for opportunities to receive information. Staffing the organization is largely from members who send their officials to attend committee meetings or to serve within the organization. These national representatives play a critical role in the information exchange that is central to the OECD mission. Emile van Lennep, former OECD Secretary General, said “ninety-nine percent of our work concerns the exchange of experience and the elaboration of lines of action” (Woodward, 2009, p. 24). Through directly participating in this process, member states can tap into the wealth of knowledge from the experience of their peers and the technical materials prepared by the Secretariat.

Rather than passively responding to economic competition or following role models defined by social relationships, governments select into a group as a deliberate choice to expose themselves to peer pressure within a particular group. States seek status through association with the elite club. This process combines aspects of learning and emulation as well as competition. The accession decision goes beyond learning described in the policy diffusion literature because it involves accepting a broad set of principles and participation in an ongoing dialogue over future policy direction.<sup>9</sup> To the extent there is any assessment of policy efficacy, it is the sense that OECD members are the “advanced nations” with

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<sup>9</sup>On diffusion literature, see Simmons, Dobbin and Garrett (2006).

valuable information on a wide range of policy issues. Joining their circle confers status by virtue of membership and offers opportunities to learn how to be successful like these countries have been. Where the sociological tradition rightly gives attention to how countries can be shaped by following a lead country or prevailing policy trend, this overlooks the goal-oriented nature of deciding to join a group of countries. The applicants seek to have their position in international society defined by their attributes as liberal states. As such applicants are seeking to associate with the rich, liberal democracies of the Western alliance. For some, this simply consolidates their current position, but others are trying to change perceptions, whether shedding a regional stereotype or distancing from a former communist legacy.

The association with the OECD appeals to states holding similar political values and foreign policy positions. The key features of the OECD are democracy and U.S.-centered foreign policy. For democratic countries and U.S. allies, the domestic public responds with more favor to steps by their government to deepen interactions with countries that they see as positive examples. In contrast, leaders of an authoritarian government may worry about unfavorable comparisons to OECD countries rallying opposition, and avoid the closer association with OECD countries that would accompany membership. Survey analysis suggests that the public may care more about the reputation of the countries that states form an agreement with than the depth of design in the agreement itself (Gray and Hicks, 2014).<sup>10</sup>

This explanation is distinct from commitment theories whereby states endeavor to buy credibility through increasing the costs of defection. Mansfield and Pevehouse (2009) contend that democratizing states signal their commitment to consolidate political reforms and responsible economic policies by joining organizations that set standards and regulate economic policies. Such logic fits well to explain a part of the demand for joining the OECD, but not the wide variation among democratizing states. Moreover, with its weak mechanisms of enforcement, the OECD is a poor tool for tying hands. At entry countries can make reservations to exclude sensitive policies, and after entry the worst cost of violating OECD principles lies in critical commentary. Real policy commitments are made as part of accession and the peer review mechanism raises costs of defection, but stronger commitment tools lie in other multilateral organizations – the WTO, regional agreements, or bilateral trade and investment agreements include enforcement provisions that incorporate third party arbitration and retaliation/compensation.

The prominence of status from association as goals for accession countries also challenge sequential

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<sup>10</sup>The survey included responses by 471 U.S. respondents to mechanical turk poll that included embedded experimental treatment to vary information on type of agreement and whether signing agreement with “good” reputation (e.g. Canada) or “bad reputation” (i.e. Iran).

liberalization theory. Rather than selecting on convergence of preferences on economic policies alone, applicants seek to join before they have all of the OECD policies in place. To achieve membership, they initiate substantial reforms as part of accession process and aspire to change future policies through the interaction with members. In sum, there is a juxtaposition of forward-looking goals for change and an organization that will do little to lock-in such policy reforms. This does not fit either the story of states binding their hands nor one of rubber stamping.

The status-seeking emulation motive for accession does not relegate the action to symbolic politics. Applicants must undertake policy reforms to earn entry to the club. Current members recognize the cost of admitting new members when there are only weak enforcement mechanisms. They have incentives to carefully screen for countries with strong commitment to OECD principles *and* responsiveness to OECD peer review. Demanding liberalization during accession negotiations is the most effective way to assure that entrants will not lower levels of cooperation. Making sure that governments will be responsive to OECD peer review and not dilute the OECD brand encourages attention to conditions outside of economic policy reforms. Here the members look for friends, who can be rewarded through membership and are expected to remain cooperative.

Both the demand and supply side of membership suggest that non-economic conditions of similarity will attract members to an organization. Specifically, political regime type and geopolitical alignment form important criteria to shape membership decisions. On the basis of common interests, states seek status by association and are welcomed into a club that relies on weak tools of enforcement and offers benefits that include both public goods and club goods.

## **4 Common Features of the Like-Minded Club**

A brief overview of the characteristics of members and non-members in the OECD confirms the expectation that income for the “rich country club” is higher than non-members on average. Figure 1 shows the average per capita GDP for OECD members relative to non-members over time. Nevertheless, it is also important to examine the distribution of income shown in figure 2. The box plot of OECD members is centered at the mean income of 22.55 thousand U.S. dollars (over the full period 1961 to 2012 taking the average income for all members in each given year), with a large cluster of high income outliers above the fourth quartile. The non-member distribution is more skewed with a lower mean income of 6.65 thousand U.S. dollars and longer tail of high income states. This clearly demonstrates that while the OECD members are rich on average, there are also many wealthy non-members, including those with oil

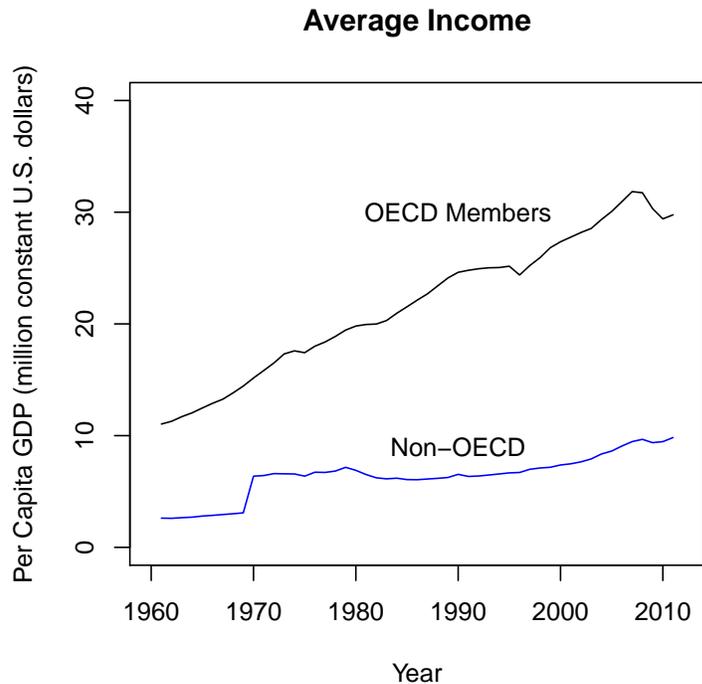


Figure 1: *Income Trend*: The figure displays the mean per capita GDP of OECD members and non-members over time.

wealth, tax havens, and some industrial economies such as Russia.

Figure 3 shows the dominance of democratic regime types among OECD members where the modal polity score is the highest level of 10 for consolidated democracies. Nevertheless, authoritarian governments have been members of the OECD. Non-members over this period from 1961 to 2012 have authoritarian regime as the modal polity score, but many states achieve high democracy scores without entry to the liberal club.

Within the non-member grouping are important actors that have embraced many of the liberal economic and political policies advocated by OECD. India and Brazil stand out as two democracies that are major emerging markets of importance to the global economy but remain outside the OECD. As the target of outreach by OECD they participate in “enhanced engagement” and undertake peer monitoring by requesting an economic survey report on their economic policies, and yet India has explicitly stated it does not seek to formally join OECD and Brazil also eschews negotiations toward accession. For both their international status derives from leadership of the developing world, rather than seeking entry to the advanced industrial world despite taking all efforts to achieve economic growth. Singapore long ago achieved income levels that surpass that of many OECD members and would easily meet most of the

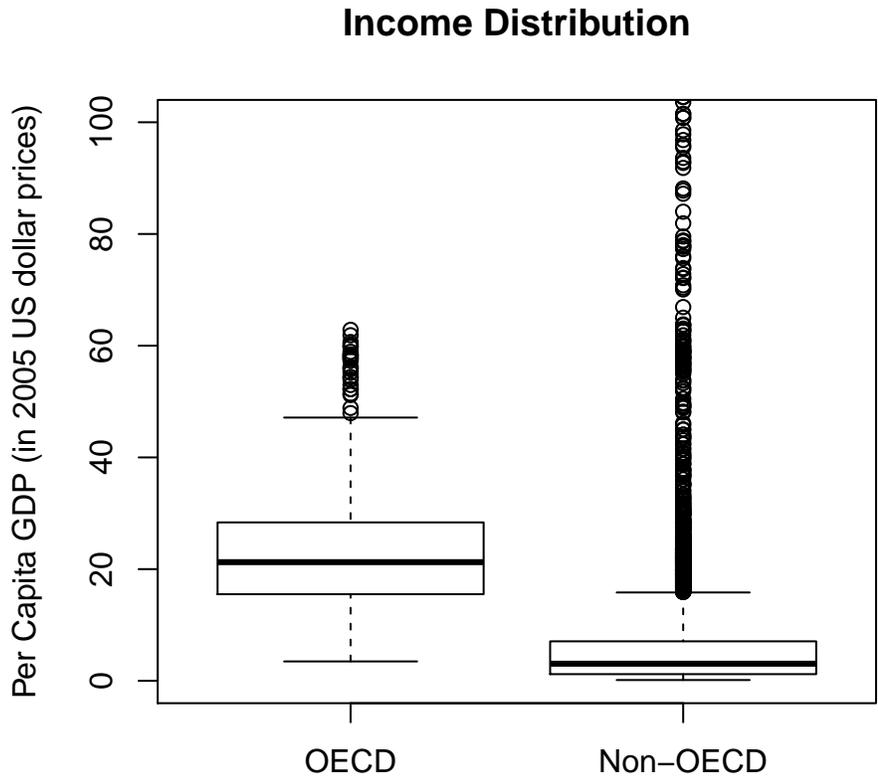


Figure 2: *Income Distribution*: The figure displays the distribution of per capita GDP for OECD members and non-members over the period 1961 to 2012.

policies for liberal market economy. Its non-democratic status may be one obstacle, but Carroll and Kellow (2011, p. 122) emphasizes that Singapore has not applied because regional identity makes Singapore seek to avoid any step that could upset its neighbors or detract from the image as a 'Chinese island in a Malay sea.'

This leads to the third dimension of similarity that shapes the OECD members: geopolitical alignment. Figure 4 clearly displays the pattern of shared alliances among OECD members, who on average have alliances with ten fellow OECD members.<sup>11</sup> The organization had its origins within the effort to use economic cooperation to build cohesion in the Western Alliance and all NATO members joined the OECD. This accounts for why Turkey as a non-democratic and poor country joined the ranks of OECD

<sup>11</sup>The alliance data is from Correlates of War Formal Alliances Version 4.1 with correction to add the second post Cold War NATO enlargement.

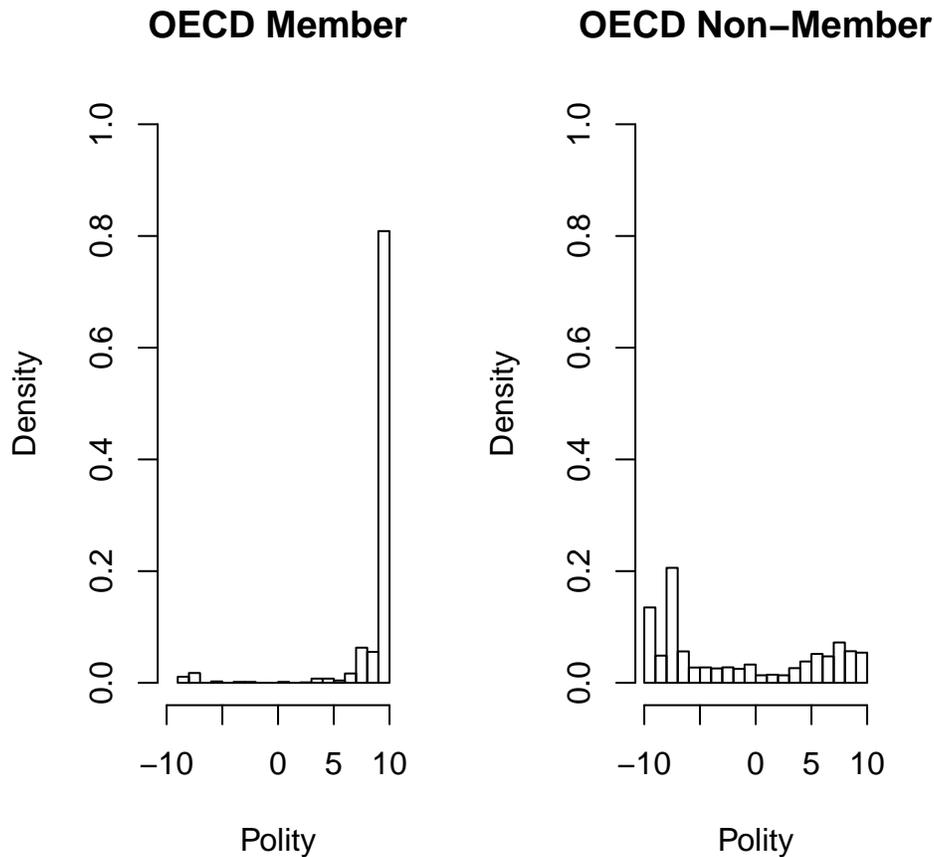


Figure 3: *Political Institutions*: The figure compares the frequency of government institutions across the range of Polity score index in which -10 is authoritarian and 10 is fully democratic.

founding members in 1961. Nevertheless, the founding group also included nonaligned Switzerland, Austria, and Sweden and many non-NATO countries would form those who joined the organization in subsequent enlargement. The sequence of joining NATO and OECD has varied; the Czech Republic, Poland, Hungary, and Slovakia joined the OECD before they were invited to join NATO accession talks whereas Estonia and Slovenia became NATO members before joining OECD. Six members of NATO have not yet become OECD members (Albania, Bulgaria, Croatia, Latvia, Lithuania, and Romania). Other countries such as Japan and Korea are not in NATO but stand as firm U.S. allies. Indeed, most OECD members share an alliance with the United States, with the exceptions of Ireland, Switzerland, Austria, Finland, Sweden, Israel, and New Zealand. Two-thirds of the OECD members are U.S. allies, and twenty percent of non-members are U.S. allies.

Another perspective on geopolitical alignment appears in the outliers who otherwise appear to fit

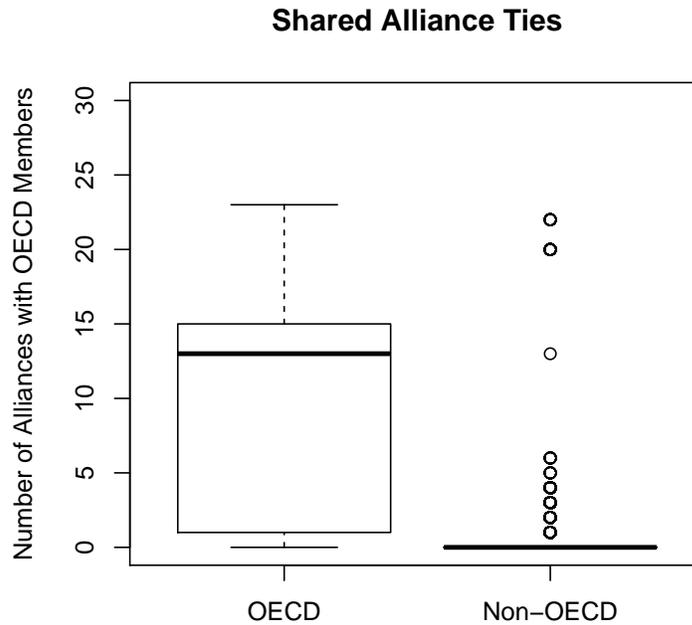


Figure 4: *Alliance Ties*: The boxplot graphs display the distribution within the OECD membership in comparison to the non-member countries in terms of the number of shared formal alliances with OECD members.

the member profile - Indonesia, Malaysia, and South Africa have income that surpasses several current OECD members and have now consolidated democratic institutions. Yet as leaders in the nonaligned movement, they have greater geopolitical distance from OECD. Similarly, another prominent leader of nonaligned movement, India, has explicitly said it will not seek OECD membership.

A more general measure of geopolitical alignment is voting similarity in UN General Assembly roll call votes.<sup>12</sup> Voting within the United Nations represents a critical behavior for identifying states with similar interests (Voeten, 2000). Looking at the trend of UN voting patterns for the OECD and non-OECD subset of countries over time in figure 5 shows the consistency across different periods in the higher similarity of OECD members in their voting affinity with the United States (left graph) and three major European states (right graph). Figure 6 displays the distribution of UN voting similarity for OECD and non-OECD countries when pooling observations over the entire period from 1961 to 2012.

<sup>12</sup>The data here are from the s3un variable in Anton Strezhnev; Erik Voeten, 2013-02, “United Nations General Assembly Voting Data”, <http://hdl.handle.net/1902.1/12379> UNF:5:NpHV5DXWPNWMWOrLGTjQYA== Erik Voeten [Distributor] V5 [Version 5]

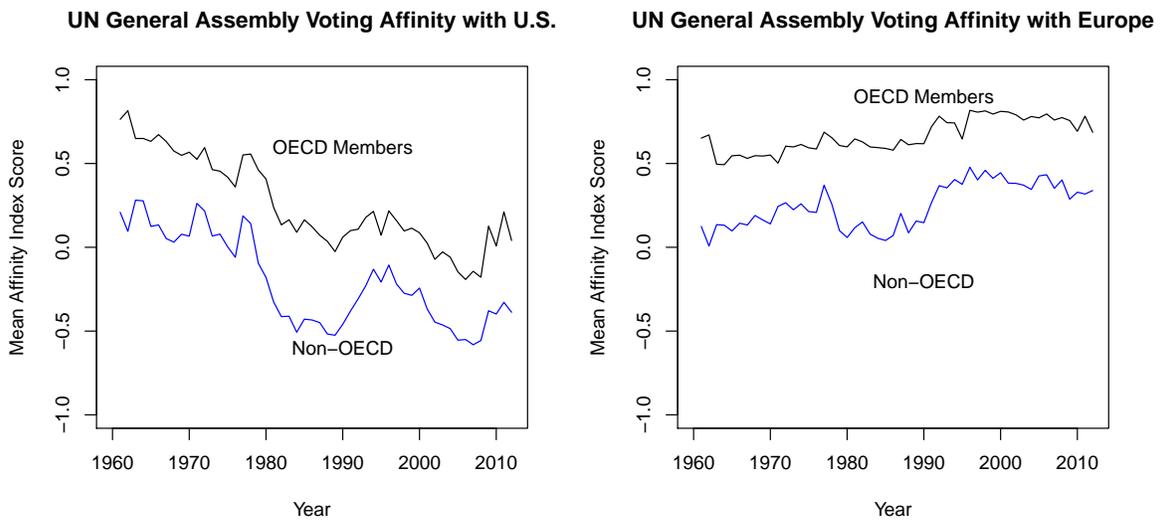


Figure 5: *UN Voting Pattern Over Time*: The graphs display the mean affinity scores for UN voting across the OECD membership in comparison to the non-member countries. The affinity index ranges from -1 to 1 and is calculated based on voting across the three categories of affirmative, abstain, and negative votes with higher values reflecting greater similarity in voting. The figure to the left represents similarity with the United States and the figure to the right represents similarity with the United Kingdom, France, and Germany (taking the average of similarity with each of the three European states).

The higher similarity of OECD members with both the United States (left graph) and three major European states (right graph) further supports the geopolitical similarity of members. Yet one also observes clusters of countries outside of the OECD that have very convergent UN voting records, as seen by the group above the fourth quartile in the non-OECD sample. Likewise, UN voting among OECD members encompasses a wide range of values. This may be a like-minded club, but it allows for diversity of opinion on some issues that arise in UN General Assembly voting.

The importance of foreign policy orientation can be seen in the example of Russia. The government surprised many when it submitted its application to join the OECD in May 1996, following up on declaration by Russian President Boris Yeltsin in a speech during Halifax meeting of the G7 countries in June 1995 that Russia would join the OECD. In a close election with resurgence by the Communist Party, Yeltsin may have seen the call to join the OECD as an easy way to appeal to those in Russia seeking further reforms, and skeptics reported the development as an election stunt.<sup>13</sup> Joining the OECD would have shown that Russia was becoming full partner with the West and confirmed its new direction. The

<sup>13</sup>(1996, May 22). "OECD backs Britain on jobs." *The Independent* (London, England) Retrieved February 2, 2014, from NewsBank on-line database (Access World News).

declaration that Russia wanted to join OECD was more aspirational than realistic. As Russian foreign policy shifted, the economic hurdles remained, and accession negotiations did not formally begin until 2007. Studies within Russia acknowledge the challenges to meeting economic reforms necessary while an OECD report in 2011 highlighted problems with state involvement in economy, weak rule of law, and restrictive trade and investment policies as obstacles.<sup>14</sup> To date, Russia has completed several chapters of the negotiations toward accession but has not joined. Clearly economic reforms loom large as one reason for staying out, but shifts in the progress toward membership also follow the tide of foreign policy relations. The the Russian-Georgian war led to claims on both sides about unnecessary delays in accession through politicization.<sup>15</sup> The Russian intervention in Ukraine led the OECD governing Council to announce it would postpone activities related to Russia's accession.

In summary, the descriptive statistics support the general view of OECD membership representing wealthy democracies of the Western alliance system. On the margins, however, the criteria for advanced income, democracy, and geopolitical alignment were substitutes such that meeting one dimension would compensate for falling short on another dimension. The rest of this paper will examine more closely how states on both sides of the membership question weighed their readiness to join across these issue areas.

## **5 Statistical Analysis of OECD Accession**

To more fully examine the correlates of membership in the OECD I use a duration model to estimate the time for a country to join the OECD from the date of its establishment in 1961. The question of interest here is why Turkey would be among the original members to join in year 1 while Mexico would join thirty-three years later and others such as Singapore remain outside of the organization. In the context of hazard model estimation, the model estimates the rate of "failure" by which is meant membership in the OECD as the dependent variable.

I first look at how different groups have distinct baseline survival trend when describing the rate of failure. Figure 7 shows the estimated survival curves using Kaplan-Meier estimates. The first graph on the left shows the significant difference for European countries relative to non-European countries

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<sup>14</sup>(2011). Economic Survey of the Russian Federation 2011. The OECD website. Retrieved February 2, 2014 from <http://www.oecd.org/russia/russianfederation2011.htm>.

<sup>15</sup>(2008, September 26). "Politics should not affect Russia's accession to OECD." BBC Monitoring International Reports Retrieved January 28, 2014, from NewsBank on-line database (Access World News); (2008, September 19). "Commentary of Russian Foreign Ministry on Rice's speech at German Marshall Fund." BBC Monitoring International Reports Retrieved January 28, 2014, from NewsBank on-line database (Access World News).

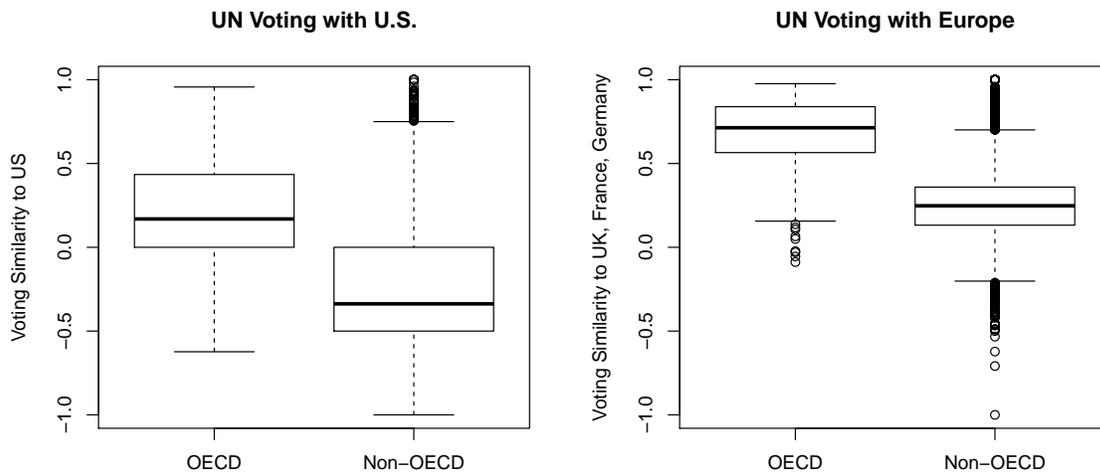


Figure 6: *UN Voting*: The boxplot graphs display the distribution within the OECD membership in comparison to the non-member countries in terms of their voting in the United Nations. The affinity index ranges from -1 to 1 and is calculated based on voting across the three categories of affirmative, abstain, and negative votes with higher values reflecting greater similarity in voting. The figure to the left represents similarity with the United States and the figure to the right represents similarity with the United Kingdom, France, and Germany (taking the average of similarity with each of the three European states). The data pools data from 1961 to 2012.

as the former are less likely to remain outside the OECD for each year following the establishment of organization. For the display of descriptive comparison of the variation in survival probability, U.S. allies offers easy comparison as dichotomous measure for geopolitical orientation. The right graph reveals the smaller but nonetheless statistically significant difference between the survival probability of U.S. allies and non-allies with the former more likely to have joined at any specific period in time. The figure highlights the clear pattern for European countries and U.S. allies to be among the first OECD members.

Given the expectation that there is not a constant rate of failure, the cox proportional hazards model is appropriate specification that allows me to include time-varying covariates while also controlling for the clear strong pull of European geography.<sup>16</sup> The sample includes 150 countries for the period from 1961 to 2011. Standard errors are clustered on country to take into account possible correlation of error terms across years within the same country. Because the organization has its roots in European development and location in Europe continues to form strong bias toward membership, I stratify based

<sup>16</sup>I apply the Efron method of ties. Countries enter the dataset in 1961 with the founding members experiencing failure in year one. All countries exit the dataset after year of failure when join OECD or in 2012 for those that do not join and are right-censored.

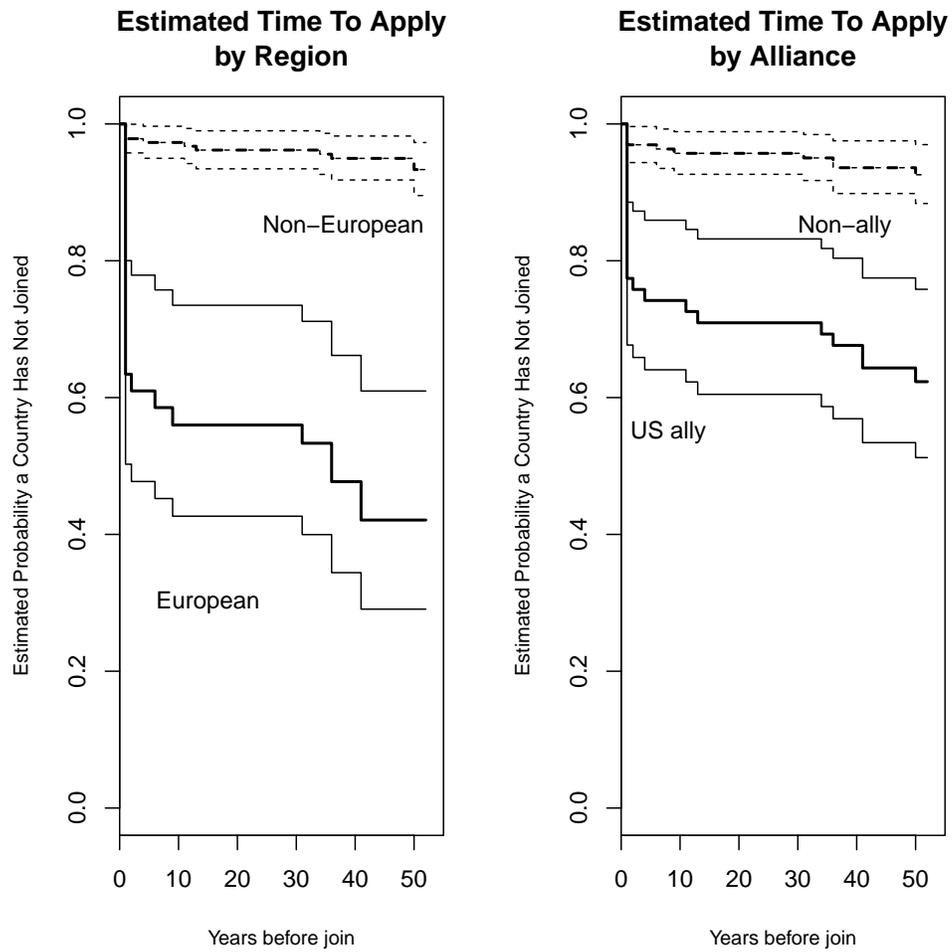


Figure 7: *Estimated Negotiation Survival Curves*: Using Kaplan-Meier estimates of survival, the figure shows the estimated probability for a country to remain a non-member

on European and non-European countries to allow for a distinct baseline hazard (this model specification is similar to adding a fixed effect for the region).

The key relationships highlighted above in descriptive statistics are tested in the regression analysis with focus on how not only income but also alliances and democracy exert positive pressure on countries to join the organization. My main variable to measure geopolitical interests is an alliance with the United States (COW alliance data), and I also examine the effect of UN voting affinity with the United States. I use the polity 2 index to measure democracy. Membership in the European Union is included as a control variable. Three variables control for economic determinants of membership. Income is measured as per capita GDP (Real GDP at constant 2005 national prices in million 2005US\$ from Penn World Tables), and is expected to have positive effect conforming to the notion that OECD represents rich country club. Liberal trade and financial policies form key benchmarks for economic policies conducive to participation in the organization; I include measures of trade openness (imports and exports share of GDP) and an indicator of whether a country has ratified IMF Article 8, which indicates a commitment to maintain an open current account.<sup>17</sup>

A test for whether covariates meet the proportional hazard assumption shows that this assumption is not met by the polity measure of democracy, which indicates that the residuals are not constant over time. Therefore it is necessary to model the effect of democracy as conditional on time through adding an interaction term between polity and the log of time since 1961 (Box-Steffensmeier and Zorn, 2001). All other covariates in the model meet the proportional hazard assumption without interaction.<sup>18</sup>

Table 1 presents the coefficient estimates indicating the direction and significance of effects (coefficients in the cox proportional hazard model are not otherwise informative about substantive effect size). The results confirm that U.S. allies have higher probability to join at any given time than those not having common security interests. Table 2 shifts to replace the alliance variable with UN voting affinity to the United States as measure of geopolitical similarity. In both specifications, there is significant and positive effect on the predicted time to join the organization.

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<sup>17</sup>IMF Article 8 signature has been described as important signal to investors of open environment for trade and investment (Simmons, 2000; Nelson, 2010).

<sup>18</sup>Including GDP in some additional specifications, however, is problematic because it does not meet the proportional hazard assumption. The model does not converge when including multiple covariates interacted with time. I focus on the polity variable where conditional effects on time are most plausible in theory.

Variable	coef	exp(coef)	robust se	z	p
U.S. ally	0.84	2.32	0.39	2.14	0.03
Polity	-0.06	0.94	0.05	-1.37	0.20
Polity x log(time)	0.12	1.12	0.04	2.77	0.01
EU	-0.76	0.47	0.48	-1.59	0.10
Per capita GDP (log)	1.95	7.04	0.31	6.21	0.00
Trade openness	-0.01	0.99	0.00	-1.21	0.20
IMF Article 8	0.68	1.98	0.41	1.66	0.10
observations	4699				
countries	150				
accession events	33				

Table 1: *Cox Proportional Hazards Estimates For Time to Joining OECD*: Results of a Cox Proportional Hazards Model estimating the time to join for all countries with U.S. alliance measure of geopolitical alignment.

Variable	coef	exp(coef)	robust se	z	p
UN voting affinity with U.S.	1.42	4.15	0.72	1.96	0.05
Polity	-0.06	0.94	0.04	-1.43	0.20
Polity x log(time)	0.10	1.11	0.04	2.59	0.01
EU	-0.35	0.70	0.41	-0.86	0.40
Per capita GDP (log)	1.65	5.18	0.30	5.52	0.00
Trade openness	-0.00	1.00	0.00	-0.88	0.40
IMF Article 8	0.49	1.63	0.42	1.17	0.20
observations	4699				
countries	150				
accession events	33				

Table 2: *Cox Proportional Hazards Estimates For Time to Joining OECD*: Results of a Cox Proportional Hazards Model estimating the time to join for all countries with UN voting affinity measure of geopolitical alignment.

Democratic institutions have a more complicated relationship that is conditional on time. Only later in the time period does the polity score measure become significant to increase the hazard rate. The OECD members shifted to embrace democracy as informal condition for membership after starting as a group that included non-democratic founding members Greece, Portugal, and Spain. During the evolution of the OECD, democratic institutions became an important factor to increase the speed with which countries join. This may reflect both the role of democracy as a principle for geopolitical alignment and the fact that political institutions can shape preferences for economic policies.<sup>19</sup> Unfortunately it

<sup>19</sup>See for example, Milner and Kubota (2005); Mansfield, Milner and Pevehouse (2008); Steinberg and Malhotra (2014).

Variable	coef	exp(coef)	robust se	z	p
U.S. alliance	1.52	4.55	0.91	1.67	0.09
Polity	1.43	4.19	0.62	2.32	0.02
Polity x log(time)	-0.33	0.72	0.16	-1.99	0.05
EU	-1.38	0.25	1.32	-1.04	0.30
Per capita GDP (log)	2.69	14.69	0.54	4.97	0.00
Trade openness	-0.01	0.99	0.01	-0.96	0.30
IMF Article 8	2.37	10.74	0.68	3.49	0.00
observations	4632				
countries	132				
accession events	15				

Table 3: *Cox Proportional Hazards Estimates For Time to Joining OECD*: Results of a Cox Proportional Hazards Model estimating the time to join for countries joining *after* 1961.

is difficult within the research scope of this paper to differentiate among these dual pathways in which democracy could shape OECD membership. To the extent that democracy is a determinant of membership, it is challenging to assess the effect of membership in the organization itself on democratization.<sup>20</sup>

As expected, income speeds membership. Trade openness if anything slows entry into OECD, although the effect is not statistically significant and the variable could also reflect the smaller share of trade in GDP for many advanced industrial democracies. Article 8 signatories are more likely to have joined, although these results are not as robust in the significance of the effect. These variables represent rough proxies for a countries capacity to accept the OECD Codes of Liberalization. These results offer only weak support for the view that selection into the organization represents screening for countries based on high levels of openness and prior commitments for financial policies. The insignificant coefficient for the EU suggests that geographic location in Europe matters more for OECD membership than membership in the EU; for several countries, joining the OECD was the precursor to EU entry.

The relationship is not driven entirely by the original group of members. Table 3 shows the same estimation for the period after 1961. With only fifteen countries joining, the results are weaker. Nonetheless, alliances and democracy are consistently positive factors for these countries accession. Here in the sample of countries that joined later, the effect of democracy appears in the positive direction for the base

<sup>20</sup>See Mansfield and Pevehouse (2006)

term of the polity measure rather than as interaction with time of eligibility.<sup>21</sup> Article 8 signatories are significantly more likely to have joined, while trade openness remains insignificant. The model specification with geopolitical alignment measured by UN affinity is not significant in this subset, but remains positive (results not shown).

In summary, the regression analysis has revealed the multiple dimensions upon which countries consider membership. Those that are the most likely to have joined early are not only wealthy, but also those with alignment to the United States in security and UN voting. Over time, democracy has emerged as a factor that also speeds some countries to higher rate of joining.

## **6 Case Studies of OECD Accession**

Four case studies shed light on the features that shape the demand and supply of membership for OECD accession. Japan represents the first example for the organization to step outside of the transatlantic scope of its origins. The Mexican and Korean cases stretched the organization both in regional scope and in economic conditions as the OECD welcomed developing country members. A final case examines the Czech Republic as the first of the former Communist countries to join the OECD.

### **6.1 Japan**

Japan's accession in 1964 was the first expansion of the OECD beyond the founding group of twenty. For the OECD it was a major step to show that the new organization would not remain tied to its roots as an organization for post-war recovery in Europe. To Japan, the entry was a mark of its arrival among the lead industrial countries. Prime Minister Ikeda had trumpeted an income-doubling plan that would be the hallmark of his four years in office from 1960 to 1964. To achieve this goal he launched a series of

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<sup>21</sup>In table 1, the base term for polity was insignificant and only as interaction with time did it achieve significant effect. The acceptance of authoritarian governments into OECD occurred largely with the founders (Greece, Portugal, and Spain), and so the full sample analysis reveals growing emphasis on democracy for the later applicants relative to the early joiners. When omitting the founding group, table 3 shows the direct effect of democracy as positive and shows an opposite interaction effect - passage of time reduces the impact of democracy.

economic reforms that achieved remarkable high growth. His foreign policy also placed new emphasis on the need for Japan to build ties with Europe to balance already strong ties with United States and form “three pillars” in support of free world (Iwanaga, 2000, p. 214). As part of this strategy, Ikeda went on 1962 tour of European capitals and expressed interest in Japan’s membership in OECD.<sup>22</sup>

Beginning in 1960, Japan had joined the Development Assistance Group, which would soon thereafter become the Development Assistance Committee in the OECD. As a country limited by its constitution from substantial military policy contribution to international security, foreign aid has evolved from its role as a quasi-reparation policy after the war to an area for Japan to appear as leader in international affairs and engage in more burden-sharing with the United States. For a trade dependent state, promoting development in other countries was also central to its own prosperity. This sometimes raised challenges to extent that trade interests encouraged giving aid tied to projects that would benefit Japanese firms, while the OECD monitoring of aid policies pushed all countries including Japan to reduce the amount of tied aid. The government made the decision that greater prominence through participation in OECD aid coordination was worth the cost of inviting scrutiny over its aid policies.

Joining international organizations has played important role for Japanese foreign policy in the post-WWII era as it tried to end pariah status as defeated nation and engage fully in international community. By the 1960s as its economic growth had taken off, membership in OECD had symbolic importance. When discussing the prospect of OECD membership in the Diet, Prime Minister Ikeda engaged in a long speech about the praise he heard from other nations for Japan’s economic revival and democracy and expressed the priority of his new cabinet to policies that would raise the level of the economy, education, culture, health and social welfare of Japan; after listing details on the increasing trade volume and liberalization he said the scheduled accession to the OECD and IMF Article 8 demonstrated that Japan’s international role would take even heavier weight.<sup>23</sup> In a detailed book that collects the input from

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<sup>22</sup>A Ministry of Finance official attributed the initiative for OECD membership as arising during the Prime Minister’s trip. “*OECD kamei to shihon torihiki no jiyuka*” (OECD Membership and Capital Account Liberalization), Kinzoukai (August, 1963), p. 24.

<sup>23</sup>Lower House Diet Testimony, 18 October 1963, parliamentary record [008/010]44 no.3.

key government and business leaders to analyze Japan's accession to the OECD, which was published in 1964 by the leading Japanese think tank Japan Economic Research Institute (JERI, *Nihon Keizai Chosa Kyogikai*), the introduction states that "Our country has now come to hold economic power as a first class industrial nation comparable to that of the European and American nations. In light of this economic reality, Japan's participation in the OECD is not only extremely 'obvious' but also 'necessary' for both our country and the OECD"(Shimomura, 1964).<sup>24</sup> Long priding itself as the first Asian country to have achieved high levels of economic development, there was an eagerness in Japan to embrace the role of helping to add Asian perspective within a European-centered organization. For these symbolic reasons alone, membership was celebrated as major accomplishment for Japan.

There were also expectations that joining the OECD would have positive contribution to economic growth through access to information. In the debate in the Japanese Diet prior to ratification of the agreement to join the OECD, Seiichi Inoue stated that there were two reasons for Japan to seek OECD accession: first, because through joining the OECD Japan could increase its voice in international society, and second, because learning from the experiences of other countries would help Japan to weather the currents of the liberal economic order.<sup>25</sup> As one example, the JERI report noted Japan's ongoing struggle to counter high inflation, recommended that "Japan should seriously learn from these OECD countries," which at the time enjoyed lower inflation rates than Japan (Shimomura, 1964, p. 127). Speaking at a forum shortly after conclusion of the negotiations for Japan to join OECD, a Finance Ministry official extolled the main benefit of membership would be through the interaction with officials from other countries in committee meetings where Japan could learn from the practice of other countries so that "reflecting on experience of other countries, Japan should adopt those policies that are good," and also share where it may have excelled with a unique approach to economic policy.<sup>26</sup>

Entering the OECD presented an opportunity for Japan to move toward more active engagement for

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<sup>24</sup>I thank Shiro Kuriwaki for extensive help translating this book.

<sup>25</sup>Upper House, Diet Testimony of the Foreign Affairs Committee, 24 April 1964. Diet Record [001/001] 46 no. 18.

<sup>26</sup>"*OECD kamei to shihon torihiki no jiyuka*" (OECD Membership and Capital Account Liberalization), Kinzoukai (August, 1963), p. 43.

Japan as “peer” (*nakama*) taking its part to shape the international order (Shimomura, 1964, p. 128). Beyond opening its own market, Japan saw OECD membership as adding new leverage in its effort to eliminate the discriminatory trade policies held against Japanese exports by many OECD members.<sup>27</sup> Here the symbolic and material benefits overlap as the JERI report suggests that by becoming member of economic club Japan would gain new forum and voice to protest these policies, which it described as a problem given that Japan was an “equal peer” (Shimomura, 1964, p. 135).<sup>28</sup> An official with the Ministry of Finance warned that the discriminatory trade policies would not be dropped immediately upon Japan entering the OECD, but through gradual process as other countries came to see Japan as one of them and not so different.<sup>29</sup>

Japan underwent a range of significant policy reforms as part of joining OECD. Some of the areas that were highlighted as problems from the Japanese side included pressures to limit such key industrial policy tools as the government support of shipping industry and restrictions on use of the Foreign Capital Law and Foreign Currency Law to screen approval of new technology, which had often been used by government to favor targeted industries and reduce so-called ‘excess competition’ through centralized control of access to new technology from abroad (Shimomura, 1964, p. 92). Concessions to liberalize shipping were among the most difficult at a time when Japan saw its shipping industry to be in crisis, but when it became apparent that refusal on this point would delay accession the government agreed to phase out the policies limiting use of foreign shipping (Shimomura, 1964, p. 68).<sup>30</sup>

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<sup>27</sup>When Japan acceded to GATT in 1955, fourteen GATT members invoked Article 35 of GATT as a means to deny MFN treatment to its trade, and this number increased further as the European colonies also invoked Article 35. By fall of 1961 with support of the United States, Japan had seen the GATT commission report on the problem and the Japanese government was involved in intense negotiations with each of the governments to win their removal of Article 35 exclusion (Komatsu, 1963, p. 165). Although by 1964 several countries had revoked Article 35 treatment, the weak negotiation position of Japan to win MFN status left many discriminatory barriers in place against key Japanese exports.

<sup>28</sup>I thank Shiro Kuriwaki for highlighting this important point.

<sup>29</sup>“*OECD kamei to shihon torihiki no jiyuka*” (OECD Membership and Capital Liberalization), Kinyukai (August, 1963).

<sup>30</sup>At the same time, as a global leader in ship-building, the Japanese government was frustrated by subsidies of OECD member governments to their ship-building industries. Accession bargains are a one-way street with the applicant holding no capacity to issue its own demands.

OECD accession brought additional expectations for financial liberalization. Leading up to OECD accession, Japan negotiated with IMF to become an Article 8 signatory, which involved ending many import quotas that had been justified for balance of payments reasons and reforming payment and contract base capital account transactions. Some within Japan argued that these steps were being taken too quickly as the result of the government's eagerness to join the OECD. An official with the Bank of Japan commented in an August 1963 roundtable discussion that there was a sense that Japan was rushing capital liberalization, but that delaying further would only make things more difficult because European states were liberalizing and the gap between them would further widen.<sup>31</sup> The government was very reluctant to liberalize foreign investment. At the time of accession, Japan included reservations that would allow it to maintain its restrictions on direct investment in manufacturing sector, uphold government role for auto insurance policies, and continue to limit participation in securities markets by non-residents. Nevertheless, there was recognition that the reservations to exclude particular policies from liberalization would face ongoing pressure through debate in the OECD (Shimomura, 1964, p. 92).

Given its status as a leading industrial power, the accession by Japan to OECD would only augment the ability of the organization to coordinate policies for the economic order. As Foreign Minister Ohira stated when asked why the OECD accepted Japan's membership, "I believe they correctly evaluated that the world economy cannot be managed by disregarding Japan's economic power."<sup>32</sup> There was little domestic controversy in Japan surrounding accession, although the Socialist Party objected to accession on grounds that the organization was anti-communist and represented an 'economic version' of NATO (the Socialist Party had just lost out in the fierce 1960 revision of the U.S.-Japan Alliance Treaty) (Iwanaga, 2000, p. 216). One Socialist Party member, Soji Okada, said in testimony before the Foreign Affairs committee that Japan seemed to only be trying to pretend to be member of advanced countries, while its preparation was weak and this was too soon for it to join.<sup>33</sup> The internal discussion of OECD accession within Japan reveals that the key benefits were foreign policy influence and increased stature in the inter-

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<sup>31</sup> "OECD kamei to shihon torihiki no jiyuka" (OECD Membership and Capital Liberalization), Kinukai (August, 1963).

<sup>32</sup> Diet Testimony cited in Iwanaga (2000, p. 216).

<sup>33</sup> Testimony of the Japanese Diet Upper House Foreign Affairs Committee, [005/134] 46 no. 18, 24 April 1964.

national community along with concrete economic policy objectives to both push forward liberalization in Japan and abroad.

## 6.2 Mexico

The case of Mexico's accession to OECD must be viewed within the context of its negotiations to join NAFTA. Having already agreed in 1990 to pursue free trade agreement with the United States and Canada, the decision by government the next year to announce its intent to join the OECD was a complementary step to further broaden the scope of its economic reforms beyond the United States and Canada. Indeed, during the anxious period when U.S. ratification of NAFTA was uncertain, some reported that OECD membership would provide an alternative way to lock in reforms of Mexico even if NAFTA were rejected in U.S. Congress.<sup>34</sup> Ultimately, the negotiations to join OECD from 1993 to 1994 followed the formal signing of NAFTA in 1992, and formal acceptance of invitation to join OECD on May 18 1994 occurred during the first year that NAFTA entered into force. Nonetheless, while NAFTA understandably attracts more attention as the key transformation of Mexican economic policies, joining the OECD was itself a meaningful step in the process.

The Salinas government that launched the series of economic reforms within Mexico also took the first step to deepen relationship with OECD. The OECD Observer report at the time of Mexico joining the OECD notes that in 1990 the Mexican government "took the initiative of broadening the scope of its dialogue with the OECD . . . by sending an exploratory mission to learn about the Organisation and the possibilities for strengthening ties with it."<sup>35</sup> Whereas the government had declined an earlier OECD invitation to participate in the OECD steel committee, it chose to join the committee in a September 1990 agreement with OECD and quickly moved forward on privatization of the industry the following year. Speaking to the OECD Council in 1992, Salinas confirmed that Mexico would like to join the organization and take a larger role in the world economy.<sup>36</sup> To the extent that the government was

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<sup>34</sup> 1993 May 12, *The Financial Times*, "Survey of North American Free Trade Impact on Mexico". 1993 June 15, *Wall Street Journal*, "Nafta or Not, Salinas Pursues Free Market."

<sup>35</sup> 1994 Jun/Jul, *The OECD Observer*, "Mexico, 25th member of the OECD."

<sup>36</sup> 1992 Jul 22, *Reuters News*, "Mexico Seeks OECD Membership and Active World Role".

undergoing deep trade liberalization through NAFTA, following on its accession to GATT in 1986, the challenging aspects of OECD reforms were focused in other areas outside of trade. In particular, Mexico expressed early reservations about whether it could undertake liberalization of capital account and in areas of oil privatization and telecommunications.<sup>37</sup> Despite the clear reluctance of Mexico to allow free capital movement, finance stood as area for gains - the likely improvement of Mexico's status on credit markets was noted within Mexico by leading financial groups.<sup>38</sup>

After negotiating with members, Mexico made several reservations but also agreed to reforms in critical areas. In particular, the reservations allowed Mexico to continue to restrict some cross-border capital operations such as foreigners conducting transactions in pesos and in areas of financial services and transport services.<sup>39</sup> At the same time, FDI liberalization went beyond NAFTA commitments with new legislation passed to open Mexico to investment from all countries without restriction to either NAFTA or OECD members and a new stock market law passed to offer access to the domestic market for foreign issuers. Daniel Dutzin Dubin, a Mexican official leading the accession process, said that OECD countries were concerned about the lack of a mechanism for the settlement of disputes, which led to the Mexican government including a multilateral mechanism for the protection of investments in the new Foreign Investment Law.<sup>40</sup> Like Japan before it, Mexico had to agree to liberalize maritime services.

While surging forward on liberal economic reforms, Salinas took a slower pace toward democratization. After Mexico joined the OECD in May 1994, Mexico held elections at end of the year that allowed international observers and were recognized as step toward partial democracy. Yet it would be several more years before Mexico would represent a consolidated democracy. While some consider OECD membership pushing along this process, it is largely in a backup role. Peer review in the OECD does not extend to political institutions, and socialization is the main channel through which it could exercise positive influence on political reforms. Clearly at the time of accession negotiations, members were willing

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<sup>37</sup>1992 Dec 2, Agence France-Presse, "Mexico to hold talks on entering OECD in 1993."

<sup>38</sup>1992 Sep 1, *El Siglo de Torren*, "Disminuir el riesgo de invertir en Mxico al entrar a la OCDE." See also commentary in 1993 Jun 7, *International Herald Tribune*, "Cut in Mexicos Debt Cost Is Likely if It Joins OECD Capital Markets."

<sup>39</sup>Pierre Poret (1994 Aug/Sep), *The OECD Observer* no. 189, "Mexico and the OECD Codes of Liberalisation."

<sup>40</sup>1993 Apr 6, *El Siglo de Torren*, "Cambiar La Ley de Inversion Extranjera, Compromiso de Mexico con la OCDE."

to accept Mexico more on the promise of liberal political reform than through actual completion of the process.

From the OECD perspective, the question of Mexico joining brought conflicted views. There was recognition that expansion could reduce the level of cooperation. Carroll and Kellow (2011, p. 97) cite statements by a Belgian minister calling for postponement of formal dialogue with Mexico (and Brazil and Indonesia) by warning against “watering down and disorganising the group at the expense of the close co-operation among the 24 of us.” At the same time, expansion offered an opportunity to increase influence both through the reforms demanded of applicant countries and through the greater reach that the organization would have based on larger membership.

When it came to selection of whom to favor for admission, it was clear that political ties and not only the assessment of policies mattered. European members emphasized the importance of including East European countries in transition while the United States, Canada, Australia, and Japan led in effort to broaden geographic scope. Colonial legacies also shaped positions as Spain and Portugal took more inclusive positions toward including Latin American countries in OECD work and were advocates for Mexico. From the perspective of market reform and democratization, it was clearly premature when discussion arose about Eastern European governments joining OECD in 1990. Pushed by political interest, the OECD Council took unusual step to establish Centre for Co-operation with European Economies in Transition to promote their ability to fulfill conditions necessary for accession to OECD through assistance and advice.<sup>41</sup> Ultimately Mexico would join one year earlier than the first of the Eastern European applicants (Czech Republic in 1995). The United States and Canada strongly pushed for Mexico while opposing a German request for rapid acceptance of the East European countries.<sup>42</sup>

Upon entry to the OECD, Mexico left the Group of 77 coalition of developing countries that coordinate policies in the United Nations. Having been a founding member and leader among the coalition, this represented a clear shift of identity. Nevertheless, in many multilateral fora Mexico remains an advocate for the developing country perspective. The inauguration in 2006 of Angel Gurría as the first OECD

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<sup>41</sup>Statement of Chair of working group of Council cited in (Carroll and Kellow, 2011, p. 159).

<sup>42</sup>1993 Jun 4, *The Financial Times*, “OECD to Open its Doors to Mexico.”

Secretary General from a developing country put a spotlight on Mexico's ascendance to the pinnacle of international society and the place of the OECD as a global institution.

### 6.3 Korea

Korea's accession to the OECD has been blamed by some in Korea for rushing its liberalization of capital flows and setting the stage for its descent into financial crisis and IMF bailout one year after joining the organization.<sup>43</sup> Fierce criticism in parliament called government officials to testify on why financial liberalization was so mismanaged. The causes of Korea's crisis are too complex to attribute to one source, and such an explanation lies beyond scope of this paper. In many ways the problem is that Korea tried to partially implement capital liberalization, while not implementing the appropriate supervisory structures to regulate against risk. Yet this debate itself reveals that joining the OECD involved significant policy changes. Unlike Mexico where it negotiated to join the OECD largely as a backup to NAFTA, for Korea this would be the first major liberalizing commitment.

Korea first expressed interest in OECD membership under the military rule of President Chun Doo-Hwan in 1983 when it was at the start of its remarkable economic growth miracle. The leading conservative daily reported the president saying that in order for South Korea to be treated as a developed country, one possible way of achieving this would be to join the OECD, a group of countries already labeled as such.<sup>44</sup> The repeated theme was that "challenging" itself through OECD membership would be a way to speed up Korea's economic progress. At the same time, critical commentary warned against expensive dues and costly liberalization.<sup>45</sup> After a year of preliminary investigation into what membership would entail, Myoung Ho Shin, who was then serving as the counselor to the Korean Embassy in Paris met with OECD Secretary General Jean-Claude Paye. He was told that Korea was unlikely to be accepted with an explanation that "the OECD was an exclusive club not one that accepted all who want to join and that the members did not want new members since they already felt there were too many and it was not efficient

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<sup>43</sup>This is widely noted in media commentary in Korea, and also a point in scholarly research (e.g. Lee, 2000; Kalinowski and Cho, 2009).

<sup>44</sup>*Chosun Ilbo*, January 21, 1983.

<sup>45</sup>*Chosun Ilbo*, January 23, 1983.

for dialogue. So he told me no.”<sup>46</sup> This shelved the idea without Korea launching a formal application process. As with a social club, the informal process dictates that countries are invited to apply, and so this exchange set aside Korea’s potential membership for the next decade.

Changes at the OECD signaled that Korea would now be treated as a serious candidate for membership. From 1990 as the collapse of communist regimes foreshadowed the end of the Cold War, the OECD began outreach to both the East European economies in transition and other “dynamic non-members” including Korea that would involve them as participants in OECD committees and help initiate a dialogue towards their eventual membership. The eagerness of European members to welcome the transition economies of Eastern Europe and the pushback from other members wanting broader geographic scope pushed forward both Mexico and Korea as prime candidates for the OECD (Carroll and Kellow, 2011, p. 96). Korea had already started on the path to becoming a liberal market democracy with its first democratic elections in 1987 and decision to accept IMF Article 8 in 1989. The Korean government included OECD membership in its 1991 five-year plan with schedule to join by 1996.<sup>47</sup>

Presidential leadership advanced Korea’s bid for membership in the OECD in 1992. As a former activist for democracy under authoritarian rule and the first civilian to be elected, Kim Young-sam consolidated the democratization process that had begun in 1987. He advocated a “*Segyehwa*” policy for the globalization of Korea in terms of both society and economy. Joining the liberal democratic club of advanced countries to guide international economic cooperation formed one concrete target within this overall program calling on Korea to undertake liberal economic and political reforms in an outward looking process. Kim Young-sam included a pledge to seek OECD membership as part of his election platform in his successful bid for the presidency in 1992. Lee (2000, p. 125) writes that “Kim expected that accession to the OECD could elevate the nation’s status in the international community while also increasing his own political popularity.” Byung-il Choi, the President of the Korea Economic Research Institute, also stated that it was a political decision to apply: “President Kim Young Sam had strong motivation to globalize Korea, using the phrase ‘seggyehwa’ as the Korean language word for globaliza-

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<sup>46</sup>Interview by author, Seoul Korea, 10 July 2013.

<sup>47</sup>1991 Oct 17, *Asian Wall Street Journal*, “South Korea: OECD Application.”

tion. Presidential power at that time was very strong. He may have believed that if during his tenure Korea could join OECD it would make for better society. Some thought that if Korea joined, the code of conduct and information sharing would help lift up the management skills for Korean business.”<sup>48</sup>

And yet it was not the case that membership was easily accepted as the right course for Korea. Within Korea the question of membership was fiercely debated and challenged by the opposition party.<sup>49</sup> The government undertook a proactive effort through creating pamphlets about OECD membership to distribute widely to not only politicians and scholars but through broader outlets to inform the public. Myoung Ho-shin, who would play key role in negotiations for Korea to join OECD in his role as Deputy Minister of International Finance, stated:

We had to educate on why need to join OECD. We said that now is the time for us to have rules and regulations so as to be a really developed country, and so we must learn and get information. We argued that the easy way to learn would be to join the OECD where information exchange and discussion would help us. We say now is the right time and that we are not taking on excessive liberalization and are doing what is within our competence. We also held seminars and summoned groups to come for meetings so we could explain banking policies.<sup>50</sup>

The government sales pitch for joining OECD included in addition to the above-mentioned opportunity to learn from advanced countries the concrete benefits for businesses from improved international credibility and lower interest rates on loans (Lee, 2000, p. 126). The influential *chaebol* saw to benefit from greater access to capital from abroad and favored introduction of competition to strengthen domestic financial industry.

This case represents clear example of demands for substantial reforms as condition of membership. Between June 1993 when OECD agreed to negotiate towards Korean membership and the formal application in 1995 and approval in 1996, the government engaged in multiple rounds of talks at the OECD. Although Korea had opened the capital account, the governments of OECD were clear that further financial reforms would be necessary to meet OECD standards prior to accession (Carroll and Kellow, 2011, p. 152). Typical are the comment by U.S. ambassador to the OECD David Aaron in October 1994:

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<sup>48</sup>Interview by author, Seoul Korea, 4 July 2013.

<sup>49</sup>*Kyunghang Shinmun*, March 16 1995.

<sup>50</sup>Interview by author, Seoul Korea, 10 July 2013.

“OECD membership is not the beginning point of the liberalization process, it really has to be seen as something near the climax of that process.”<sup>51</sup>

Demands made on Korea included raising foreign investment ceiling and ending foreign bank restrictions, allowing full currency convertibility, lifting capital controls on international Korean companies, relaxing rules on merger and acquisition, trade liberalization, and labor law revisions. In each of these areas particular OECD members pushed hard for Korean reforms, using the OECD accession process as a form of leverage. The strong political backing in Korea to gain OECD membership created a window of opportunity for outside pressure. Making reforms in the context of OECD accession was more palatable in Korea than doing so under U.S. demands, and certainly Japan could not have requested reforms outside of multilateral venue given the tense bilateral political relationship.

For joining the OECD, the biggest challenge for Korea would be liberalization of the financial sector – the won was not fully convertible and restrictive market regulations prohibited foreign takeover and limited equity holdings. Byung-il Choi, the President of the Korea Economic Research Institute, described the changes: “The government completely controlled the financial sector such that in truth there were no ‘private’ banks. The OECD membership would bring a sea change.”<sup>52</sup> Although the changes of policies were large relative to the closed financial markets in place in Korea, the government limited the scope and pace of liberalization. When the Korean government brought its financial liberalization plan to the OECD for negotiations, days of negotiations ultimately led members to accept its plan for sequencing the reforms according to its own gradual plan.<sup>53</sup> The government favored liberalizing short-term capital inflows first while maintaining controls on long-term investment (e.g. strict limits on foreign ownership of Korean companies), and refused to open bond market participation to foreigners. The rationale was that government could more readily restrain *chaebol* through restrictions on long-term investment and needed to play “traffic cop” allocating funding among the small group of large firms to avoid market distortions. Supervision of banking industry was supposed to help manage influx of short-term capital,

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<sup>51</sup>David Brunnstrom, “Seoul Must Speed Liberalization for OECD Place.” Reuters News, 21 October 1991.

<sup>52</sup>Byung-il Choi, Interview by author, Seoul Korea, 4 July 2013.

<sup>53</sup>Myoung Ho-shin, Interview by author, Seoul Korea, 10 July 2013.

and allowing liberalization here for financing trade and bank transactions promised immediate gains to boost the economy. Korea's large conglomerates stood to benefit from increased access to capital, while restricting long-term capital flows reflected old developmental state bias against foreign direct investment (Kalinowski and Cho, 2009, p. 225). Later, critics would cite this as the mistake setting up Korean financial system for instability, given that the supervision of banking remained inadequate and failures of the newly established merchant banks would form onset of financial crisis and large short-term debt made country vulnerable when foreign creditors lost confidence and decided to withdraw funds. Yet at the time, commentary in the western media focused on how Korea had not gone far enough and would need to continue with its pledge to continue liberalization in coming years. According to the *Financial Times*, "Korea accepted only 65% of the OECD codes on financial liberalisation against an 89% acceptance rate by the average OECD member."<sup>54</sup>

In an example of the shifting benchmark for membership, Korea faced demands on labor law policies. European members were critical of the restrictions limiting number of unions in a firm, barring third-party arbitration of labor disputes, and the ongoing arrests of labor activists. In response to the demand for assurance that it complied with labor laws deemed essential by OECD members (although none were listed as criteria in OECD agreements), the Korean government formed a labor law committee to draft the outline of changes. When the Korean government was late in its proposal for labor policy reforms, the OECD governing Council delayed its final decision meeting on Korean membership, thus holding the issue as a breaking point for the conclusion of the accession deal.<sup>55</sup> Ultimately, members decided to accept a letter of assurance from the Korean government that it would reform its laws so as to follow the core labor standards of the International Labor Organization.<sup>56</sup>

Although much of the draw of membership is aspirational to follow the successful example of members and learn from their policies, Korea also faced a counter-example from the Mexican experience. At the height of Korean efforts to liberalize its financial policies for OECD membership, the most recent

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<sup>54</sup> *Financial Times*, 14 October 1996, "South Korea Braces for Restructuring."

<sup>55</sup> 1996 Oct 10, *Financial Times*, "Labour Law Threat to Korean OECD Bid".

<sup>56</sup> *Financial Times*, 14 October 1996, "South Korea Braces for Restructuring."

member Mexico was undergoing financial crisis that would require massive bailout by United States to underwrite the value of the peso as currency flight threatened to erode the last of the countries foreign reserves. Cautious voices within Korea pointed to the Mexican example as they urged that Korea should wait to undertake reforms. Yet President Kim was undeterred in his push for joining the OECD, although the application was delayed by a few months as Korea negotiated over the need to follow its gradual plan for liberalization.

Once OECD accepted Korean terms, the membership question had to go before the Korean Parliament where it faced considerable debate. Opposition ranged from those who favored accession but sought further delay to lengthen transition for slower liberalization process to those who strictly opposed accession. Financial firms whose interests were directly threatened had formed lobbying coalition. Many leading scholars in Korea also voiced opposition. Several ruling party member legislators joined the opposition parties with criticism that hurrying into the OECD could bring in excessive financial inflows that would make Korea vulnerable to a crisis similar to the Peso crisis experienced by Mexico. For example, one member of the ruling party Park Myung-Hwan said “The price we will have to pay by entering the OECD is too great in consideration of our lack of preparation.”<sup>57</sup> Ultimately, the government proposal was ratified in November 1996 with a vote 159 in favor and 101 against.<sup>58</sup> Korea would become the 29th member of the OECD the next month.

In light of the subsequent financial crisis, many came to regret the price paid to join the OECD. Both the media and scholars blamed the Kim government for having rushed into the organization and undertaken reforms against the economic interests of Korea (Lee, 2000). Nevertheless, even for critics who see the reforms undertaken in the early 1990s as faulty, withdrawal from the OECD is not raised as serious proposal. One scholar noted that when the most recent financial crisis led him to advocate for imposition of short-term capital controls, “the government officials would say no, giving as the reason the OECD commitments. Bureaucrats think of OECD as setting a global standard that we must abide by. As if we need to be good students! Korea is obsessed with country ranking and the comparison of countries

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<sup>57</sup> 1996 Oct 1, Agence France-Presse, “South Korea’s ruling party faces mounting opposition to OECD membership.”

<sup>58</sup> 1996 Nov 26, Agence France-Presse, “South Korean parliament ratifies controversial OECD entry”.

in OECD is taken very seriously. In the 2008 crisis, I argued that there was reasonable necessity to impose restrictions on short-term flows, but their final defense was always the commitment to OECD.”<sup>59</sup> For better or worse, Korean leaders are too proud of OECD membership to consider withdrawal or rejection of its principles.

## 6.4 Eastern Europe

The expansion beyond Europe occurred against the backdrop of strong pressure to include new European members. From 1989, Germany and other European members of OECD called for early entry by East European members; non-European members of OECD pushed forward their own candidates outside of Europe. This regional balancing was also constrained by the conditions of alignment, democracy, and economic reforms rather than geography alone. Clearly it was only the end of the Cold War and move toward market economic policies and democratic reforms that set stage for East European countries to join OECD. This geopolitical shift shaped both the demand to join by East European governments and the willingness to accept them by the OECD members.

The first successful East European country to join OECD was the Czech Republic. In January 1990 with the Cold War drawing to a close, the government of Czechoslovakia expressed interest to join OECD.<sup>60</sup> As the Soviet Union itself sought closer dialogue with the OECD, it opened the door for Czechoslovakia to directly seek membership in an early courtship with Europe. The 1993 split that formed Czech Republic and Slovakia was successfully managed and stable macroeconomic performance raised expectations for Czech Republic joining early. The government oversaw major reforms for privatization and reduction of state subsidies and price controls as part of transition to market economy, and moved forward on trade and investment liberalization. With establishment of convertible currency in October 1995, the government had met the demands from OECD and became an OECD member in December of that year. Yet many areas of reform remained unfinished with concerns voiced about the expected capital inflows causing instability when financial reforms, price liberalization, and privatization

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<sup>59</sup>Byung-il Choi, Interview by author, Seoul Korea, 4 July 2013.

<sup>60</sup>David Marsh and Strasbourg Bonn, “Czechoslovakia asks to join OECD,” *Financial Times* 18 January 1990.

remained incomplete.<sup>61</sup> As with the Czech Republic, the entry of Poland and Hungary in 1996 followed substantial reforms that represented downpayment on transition to market economy.

The U.S. Minister Coucilor for Economic Affairs to OECD from 1992 to 1996, William Weingarten, said about enlargement to include Czech Republic, Poland, and Hungary that the countries wanted “some form of link with the West,” and the OECD played this role; “They basically asked to be tutored, and we were happy to do it.”<sup>62</sup> He also acknowledged that this process required willingness to bend the rules to let countries in so that they could be guided through ongoing transition process with reviews to assess shortfalls.

Notably, EU enlargement and OECD enlargement have not followed a fixed pattern. The statistical analysis showed no significant association between EU membership and OECD membership. For countries like Czech Republic, Poland, and Hungary, entry to OECD preceded entry to EU. Other countries such as Slovenia and Estonia joined EU before they joined OECD. Finally, seven of the twenty-eight EU members are not members of OECD.<sup>63</sup> Poast and Urpelainen (2013) find that new democracies often form new organizations rather than join existing ones as they cannot yet meet entry requirements for the best clubs and so must seek other ways to lock in reforms and signal quality. This argument applies to circumstances of the new democratic regimes of Eastern Europe, but we also observe eagerness on part of OECD members to support the democratization of Eastern Europe through encouraging their entry into OECD and accept incomplete reforms as good enough.

The Eastern European enlargement followed the shift of geopolitical alignment that was paired with economic and democratic reform. This further highlights the challenge to disentangle which aspect was most important for the entry to OECD. Rather than making causal arguments about any variable as explanation of membership, the cases highlight how these were jointly assessed as part of a wide set of criteria for what constituted like-minded states.

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<sup>61</sup>Kevin Done, “Czech Economic Achievements Rewarded,” *Financial Times*, 22 November 1995.

<sup>62</sup>Association for Diplomatic Studies and Training, Oral History Project interview of William Weingarten available at <http://adst.org/wp-content/uploads/2012/09/OECD-Subject-Reader.pdf> accessed May 12 2014.

<sup>63</sup>These are Bulgaria, Croatia, Cyprus, Latvia, Lithuania, Malta, and Romania.

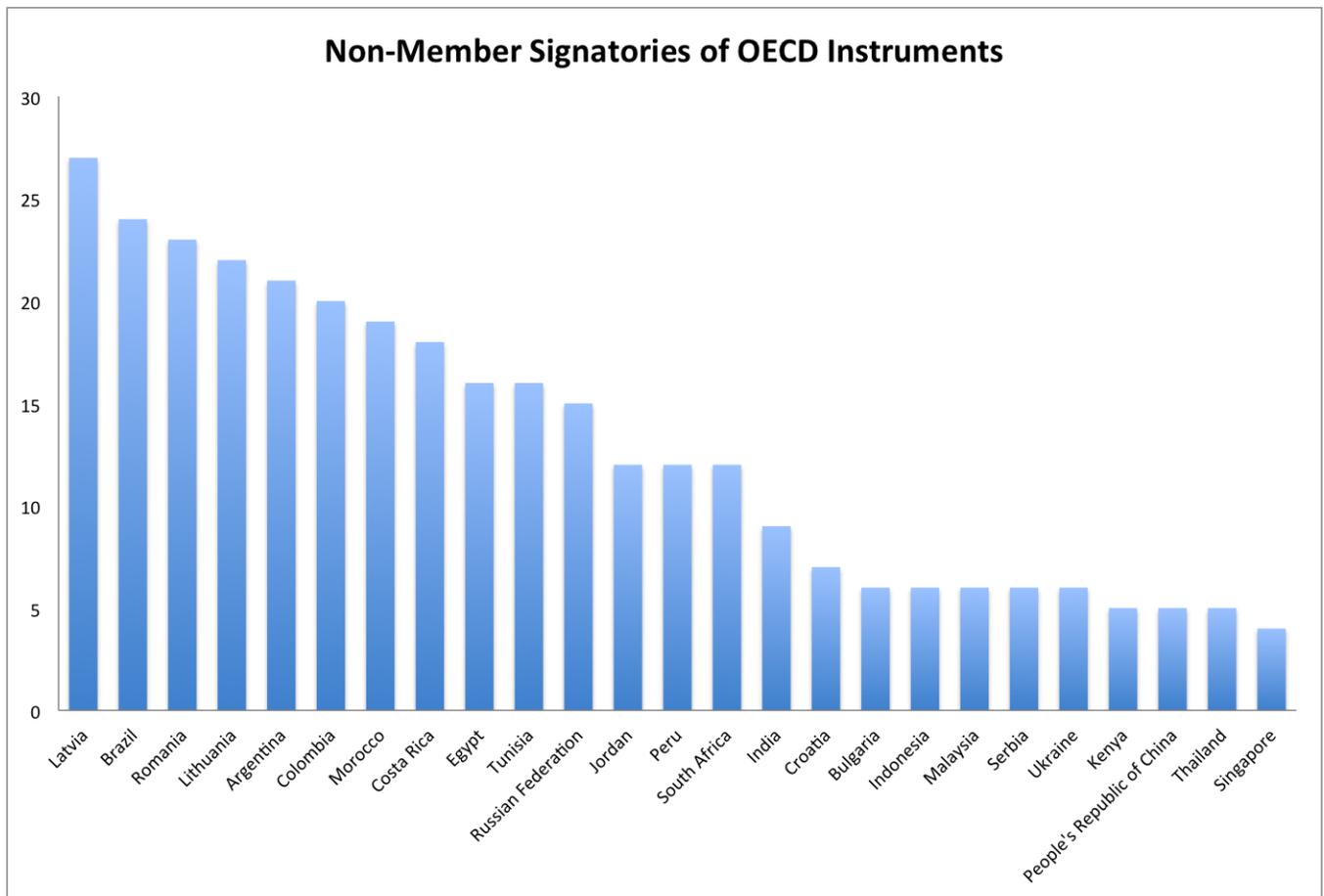


Figure 8: *Signature of OECD Instruments by Non-Members*

## 7 Brazil as a Non-Member Partner

What goes into the decision process of states that represent plausible candidates for membership but have not joined? This section will examine the case of Brazil, which stands out as one of the most eligible non-members. It is one of the states that has been highly engaged with the OECD, as can be seen by their levels of ratification of OECD instruments (figure 8) and participation in OECD committees (figure 9).

The OECD Council of Ministers in 2007 named Brazil along with China, India, Indonesia, and South Africa as partners for enhanced engagement with a view towards membership. The enhanced engagement process was launched as part of the OECD strategy to become a more global institution through expanding membership and outreach to non-members. The key partners relationship represents

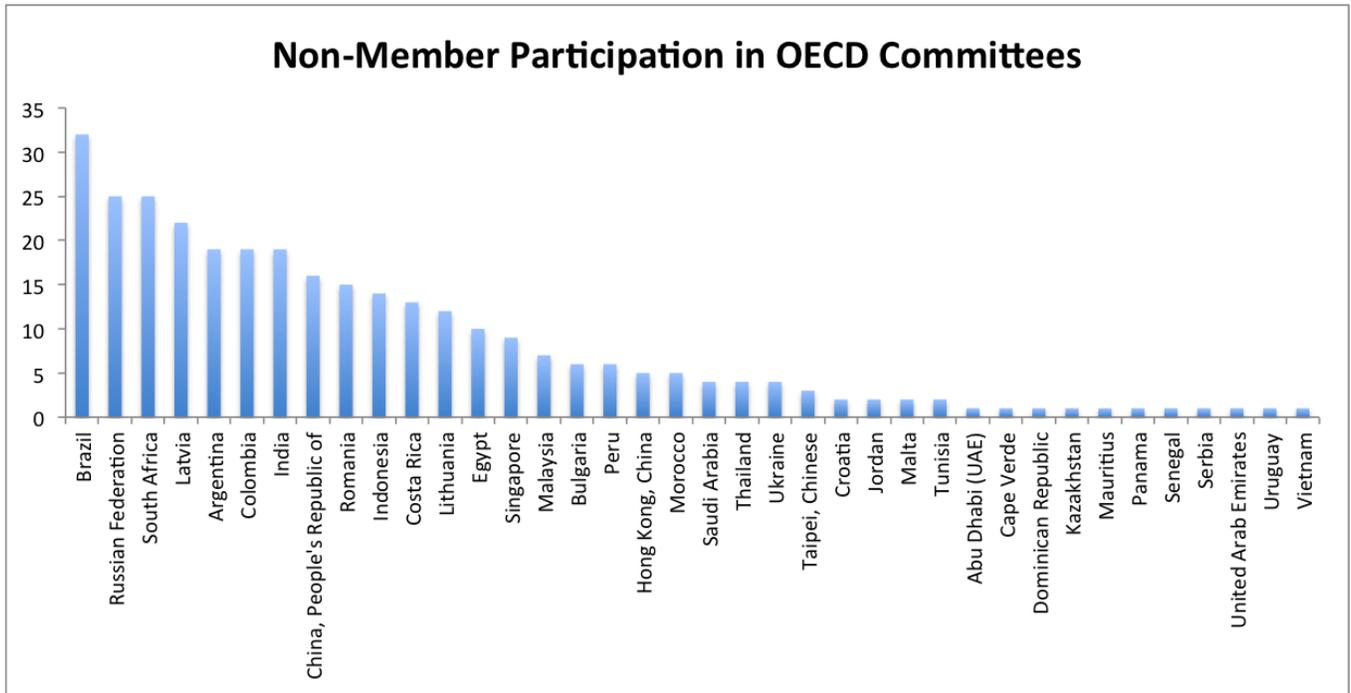


Figure 9: *Participation in OECD Committees by Non-Members*: numbers reflect total participation in 2014 as reported in data given to author from OECD Secretariat.

an invitation to engage with possibility of accession – the common view is that if these countries were to apply for membership the answer from OECD membership is likely to be yes. As the share of the global economy held by OECD members declined with the rise of emerging markets, the organization felt the threat of becoming marginalized. This prompted strategic planning to expand its outreach to non-members. One pathway built on existing channels of working with non-members. A new initiative called “enhanced engagement” targeted five key partners for deeper cooperation. These countries are viewed to have potential to become members from the perspective of the OECD membership but have not made a request for membership. Thus they are not in accession process, but are actively recruited by OECD officials to participate in its activities. The rationale for outreach lies within the OECD Convention, which calls for members to contribute to economic expansion in member and non-member countries and provides for inviting non-member governments to participate in the organization. Although non-members lack decision-making power and are not obligated to pay dues, they have several ways to access policy information and influence debate over standards. Many OECD activities are open to non-members including full participation in OECD committees on the basis of invitation and approval of the members

and attending OECD Ministerial Council meetings. Some voluntarily adhere to OECD instruments and participate in regular economic surveys.<sup>64</sup>

Brazil began active engagement with OECD committees as a non-member in 1996 when it joined the steel committee, and it quickly expanded involvement the next year to participate in the leading committees including trade, investment, and the competition policy committee. It has accepted key OECD instruments including the OECD Anti-Bribery Convention. Since 2001, the OECD has completed six economic surveys of Brazil involving extensive information exchange between the government and organization. Brazil now serves as an associate in the Governing Board of the OECD's initiative for education reform, the Programme for International Student Assessment (PISA). Its ministers frequently attend OECD Council of Minister summits.

Yet despite engaging with the organization, Brazil has shown no interest in seeking full membership. There are questions about whether Brazil could meet OECD standards for entry, and an evident lack of desire to undertake the reforms for the sake of entering the organization (p. 213 Woodward, 2012). The latter is likely the more important reason. The eagerness of the organization to expand and include BRICS for broader legitimacy would lead to flexibility on accession standards to make it possible for Brazil to enter, and the government has already accepted many OECD instruments and shared its economic and social data for public reporting. More than inability to join, lack of interest to join keeps Brazil out of the OECD. The former Brazilian finance minister Rubens Ricupero said in comment for a Brazilian politics and economic site, "OECD membership would be the equivalent of political suicide. Most of the time, on all those issues, the positions assumed by Brazil are not only different from but often opposed to those of OECD member countries. Mexico opted to join the OECD in the euphoria following the celebration of the Free Trade Agreement with the USA and Canada (NAFTA); today, the country is quite isolated and unremarkable in multilateral diplomacy forums."<sup>65</sup>

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<sup>64</sup>See "OECD Global Relations: Engaging with Non-Member Economies" at [www.oecd.org/globalrelations](http://www.oecd.org/globalrelations).

<sup>65</sup>See John Fitzpatrick, "Brazil would commit political suicide by joining the OECD, says ex-finance minister Rubens Ricupero," *PRlog*, at <http://www.prlog.org/10256031-brazil-would-commit-political-suicide-by-joining-the-oecd-says-exfinance-minister-rubens-ricupero.html>. Quoted in Woodward (p. 213 2012)

States have many options for groups to join. A point of resistance to joining the OECD lies in the conflict between leadership of developing nations and OECD membership. One OECD official asked about why the BRICS have not joined the OECD said, “The emerging markets like China and Brazil want to engage with OECD but for the moment are not looking for membership. China joins discussion on SOE reform, but signing instrument is too much for them. Brazil does sign many instruments and is already very closely engaged with the OECD. But until now they have considered membership impossible. For these countries as a leader of developing countries, they see the OECD as anathema. This is more about the image that is attached to the OECD than anything else.”<sup>66</sup> In an interview with Seichiro Noboru, who was the former Japanese Ambassador to the OECD who chaired the OECD working group that produced the 2004 “A Strategy for Enlargement and Outreach”, he commented that “There is an outdated notion among some countries that in order to maintain unity of the G77 they should not join the OECD, since it is regarded as rich man’s club and its activities could not be helpful. But that view is totally wrong and the OECD needs to counter it through outreach efforts.”<sup>67</sup> He continued to note, “The G20 work is of more interest for Brazil and other emerging markets, and it does not cost as much. Joining the OECD has financial cost in terms of budget contribution and also requires that a country make its system open and transparent. Some countries are not quite ready for this. BRICS could gain a lot from joining the OECD.” Others who work with OECD concurred that Brazilians will often say it is about the G77 and they see a political cost to joining OECD because it would be perceived as if they were turning their back on the G77 as Mexico did when they joined the OECD and NAFTA.

Nothing in OECD procedures or norms would require leaving other organizations. Mexico and Korea both exited G77 upon entry to OECD, but Chile remained a G77 member after OECD accession. Many OECD members including Mexico and Korea (but not Chile) are also members of G20. Thus there is not a *necessary* conflict of membership for Brazil when considering its membership in G77, G20, and OECD. Rather it is a relative choice about which grouping it values based on both status of association and the cost benefit analysis of belonging to the organizations.

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<sup>66</sup>Interview by author, OECD Secretariat, 20 October 2014.

<sup>67</sup>Telephone Interview by author, 28 October 2014

For some countries, closer association with the United States and Europe attracts them to join OECD, but this same association repels others. The influence of countries like Brazil in multilateral diplomacy relies on their identification as leader of developing market economies. This has been deemed more important than trying to shape the determination of 'best practices' and standards in the OECD or any positive benefit from association with wealthy democracies.

## **8 Conclusion**

The OECD serves as a clear example that membership is not random as one observes strong patterns of correlation on income, alliance, and democracy. This is important caveat in light of the large number of political science studies that use OECD membership as criterion for analyzing subset of countries without explicit attention to determinants of OECD membership and potential biases or outliers that could arise in their research as result of sample selection. Selection occurs through the attraction of like-minded states and screening for countries that favor economic cooperation. But the impact of the organization is not simply because states that have already made economic policy reforms choose to join. The paper provides empirical evidence of how conditional membership brings policy change. Entrants make substantively important commitments to liberalize trade, finance, and investment policies during accession in order to achieve membership approval.

The OECD represents an unusual organization in its broad scope of policy mandate accompanied by low levels of legalization with peer review as the primary form of enforcement after entry. Yet it appears to have in some areas emerged as an effective organization - whether increasing trade among members or establishing common regulatory frameworks. Failed negotiation for a multilateral investment regime and limited direct effect on member policies serve as reminders that its powers are no greater than what members decide they support as best practice. The influence of the organization in the complex milieu of institutions with a hand in guiding global governance lies in its size and credibility - small enough to offer serious deliberations among members who often share similar preferences and can be trusted to move in the recommended policy direction. This makes the question of enlargement especially delicate

for the organization.

From the perspective of institutional design, there are important implications from the pattern of discretionary accession. The rational design volume of *International Organization* (Koremenos, Lipson and Snidal, 2001) as part of setting up ideal types raises the expectation for organizations to be inclusive or exclusive in membership based on the type of cooperation problem that countries face. As a function of the wide scope of issues addressed in the OECD, this organization defies such categories. The vague formal rules and ad hoc practice applied in accession process suggest that OECD members favor discretion about how inclusive or exclusive to be for any given period or applicant. On the one hand the membership remains a small subset of thirty-four states with a club identity. On the other hand, the OECD has admitted developing countries and widened its geographic scope beyond the transatlantic partnership in ways that allow more heterogeneity of interests. As with any social club, it suits members to retain their own autonomy to define whom to admit. Thus even when the OECD attempted to clarify terms of membership, its guidelines were vague and list of new applicants defy any template of membership criteria. The use of discretionary accession rules conforms to theories that greater levels of uncertainty over exactly what is expected of members can maximize the level of reform (Stone, Slantchev and London, 2008; Schneider and Urpelainen, 2012). This paper contributes to understanding the preferences that underly why some countries seek membership and willingly undertake reforms during accession while others do not.

OECD accession offered leverage for policy change in applicants who were motivated by strong desire to join the organization for the sake of joining, above and beyond their expected gains from specific reforms. Although the countries examined in the case studies had all embarked on a turn toward liberalization of their economic policies and sought OECD membership as one tool to deepen those reforms, they did make some painful concessions as part of accession. Japan gave up key instruments of industrial policy while Korea undertook significant reform of its state-centered banking system. Even Mexico, which had largely completed its substantial economic liberalization as part of concluding NAFTA, found that OECD membership required additional steps. In a process similar to that described for EU en-

largement by Schneider (2009), complex bargaining over interests led to a diverse set of outcomes for terms of accession. Members that were eager to see these countries enter OECD (the United States and Japan) accepted some reduction of liberalization even as more reluctant members (EU) added on new conditions such as labor law revisions. Through the changing demands of the members as well as the applicant use of reservations that excluded policy areas from liberalization, each took on a different set of commitments. And yet the premise was that they would continue their reform process to reduce the reservations and bring themselves up to the OECD standards. In ways that parallel the experience of the GATT/WTO, the OECD has had geostrategic ties as the glue to motivate economic cooperation (Davis and Wilf, 2015b).

Member selection occurred on the basis of the three dimensions highlighted in my hypotheses. As a like-minded club, the OECD consists of countries that share liberal values whether those are achieved by liberal political institutions, economic policies, or commitment to the western alliance. Rather than a rigid package, these criteria form a multidimensional space in which the members have discretion to prioritize one over the other for a particular country or era. From the applicant side, one must clearly add the role of status and emulation. The countries in the case studies were each seeking to gain status by associating with powerful countries who exhibited similar traits. Similarity with current OECD members on the dimensions of political, economic, and geostrategic policies made these states seek membership where others would not. Ambitious political leaders latched onto OECD accession as a symbolic gesture to build support for their economic reform programs because they knew it held resonance within their domestic public. Even as opponents warned of the risks and disparaged the need to make concessions for vain efforts to gain status, leaders pushed through the necessary reforms and ratification to join. At the same time, the case of Brazil illustrates how different alignment could dissuade a state from seeking membership even when it is proffered. The choice to join organizations reflects a broad association with a group of countries, and states choose carefully based on political relations. Functional demand for gains from cooperation are certainly important to members and applicants, but membership decisions go far beyond the issues at stake in the regulations of the regime.

## Appendix

Country	Accession Year	Per Capita GDP	Polity Score	Shared Alliances
United States	1961	42244	10	23
Canada	1961	36335	10	20
United Kingdom	1961	32080	10	18
Ireland	1961	41632	10	0
Netherlands	1961	38391	10	18
Belgium	1961	32994	8	18
Luxembourg	1961	57647	10	18
France	1961	29477	9	18
Switzerland	1961	42317	10	0
Spain	1961	25694	10	18
Portugal	1961	20106	10	18
Germany	1961	35071	10	18
Austria	1961	35891	10	0
Greece	1961	21096	10	18
Sweden	1961	34707	10	0
Norway	1961	58431	10	18
Denmark	1961	32442	10	18
Iceland	1961	29992	10	18
Turkey	1961	13058	9	18
Italy	1962	27239	10	18
Japan	1964	31587	10	1
Finland	1969	32345	10	0
Australia	1971	38042	10	1
New Zealand	1973	24400	10	0
Mexico	1994	12516	8	3
Czech Republic	1995	22894	8	19
Poland	1996	17562	10	19
Hungary	1996	16315	10	18
South Korea	1996	29618	8	1
Slovakia	2000	19516	10	21
Chile	2010	13519	10	3
Slovenia	2010	23743	10	21
Estonia	2010	16740	9	21
Israel	2010	26421	10	0

Table 4: *OECD Members*: The table lists 2011 values for income, democracy, and number of formal alliances with fellow OECD members.

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