

New Foreign Direct Investment screening regime implemented in the Slovak Republic

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The Slovak Republic has implemented a new comprehensive FDI screening procedure, with the aim of achieving a delicate balance between maintaining the incoming flow of foreign investment, while offering an effective tool to identify foreign investors and investments which pose a potential threat to the security and public order of the Slovak Republic & the European Union.

Effective as of **1 March 2023**, the new Act No. 497/2022 on Screening of Foreign Investments ("**New FDI Regime**") replaced the current investment screening regime under the Act No. 45/2011 Coll. on Critical Infrastructure ("**Former FDI Regime**"). The implementation of the New FDI Regime marks a major regulatory development in Slovak FDI procedures, as the country's FDI laws are now comparable with the standards & procedures applied in other EU jurisdictions with modern systems. Concerns over protecting EU economies from incoming threats have increased in the last few years. This led numerous EU member states to implement procedures which screen incoming investments to identify and prevent potential threats.

The Slovak Government implemented its first and rather simplistic FDI screening in 2021 in the face of potential investments from non-EU countries in companies operating critical industrial infrastructure. In essence, the Slovak Government retained the final decision over investments in companies designated as elements of critical infrastructure. However, the New FDI Regime extends the scope of FDI screening from the narrow protection of elements of critical infrastructure under the competence of the Ministry of Economy to new fields.

This article aims to provide a comprehensive overview of the changes implemented under the New FDI Regime and concludes with our practical insights on how the New FDI Regime may materialise in practice.

Accordingly, the analysis is split into the following parts:

- Introduction to the New FDI Regime;
- Overview of key definitions, applicable procedure and sanctions;
- Closing thoughts on expected impacts in practice.

The New FDI Regime became effective as of **1 March 2023** and is applicable to transactions closed on/after the effective date - 1 March 2023. Transactions closed before 1 March 2023 will not be affected by the new law and will be regulated by the Former FDI Regime.

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1 New FDI Regime – *Assessment & Procedures*

The New FDI Regime will apply to non-EU investors (both natural as well as legal persons) acquiring targets with the seat in the Slovak Republic, irrespective of the target's legal form, capacity, scope of business and method of financing. Under certain conditions, Slovak or EU-based investors may be subject to FDI screening if the financing is provided by a non-EU investor or if the investor acts in concert with such non-EU investor.

"It is reasonable to expect that the New FDI Regime will enhance legal certainty and legitimate expectations with respect to foreign investment in Slovakia. However, there are still procedural ambiguities to be resolved. "

1.1 **Foreign Investment** as defined under the New FDI Regime enables foreign investors to do the following:

- acquire the target entity,
- exercise effective participation in the target entity,
- acquire or increase effective participation in the target entity,
- exercise control over the target entity or to acquire a right to substantial assets of the target entity.

The **threshold** for obtaining effective participation amounts to the share capital or voting rights of a foreign investor in the target entity and is at least **25% for foreign investments** and at least **10% for foreign critical investment** (respectively).

1.2 **Foreign Critical Investment**

Foreign investment in targets operating in certain fields may constitute Foreign Critical Investment under the New FDI Regime, which requires prior approval by the Ministry of Economy. **Foreign Critical Investment** constitutes a foreign investment by a foreign investor in a target entity operating in the following fields designated by the Government Regulation No.61/2023 Coll. on Designation of Foreign Critical Investments (**Government Regulation**):

- manufacturing of firearms and related equipment,
- production, research, development, or innovations of military technologies and equipment,
- production, research, development, or innovations of dual use items,
- production, research, development, or innovations of biotechnologies in the healthcare sector,
- operation, management, and other use of features of the critical infrastructure,
- provision of services in the field of cyber security,
- providing digital services related to the online market, online search engines and cloud computing,
- production and R&D related to encryption technologies and their components,
- operating in specific fields of the broadcasting media,
- operating an online content sharing platform with annual revenue exceeding EUR 2 million,
- publishing of large-scale periodic press or news agency,

- operating online news web-portal,
- acting as a news agency.

1.3 Applicable Screening Procedures

The distinction between foreign investment classified as critical or non-critical (outside the scope of the fields designated in the Government Regulation) plays a crucial role with regards to the applicable screening procedures:

- **Mandatory Screening Procedure:** applies in case of foreign critical investment designated by the Government Regulation. Approval from the Ministry of Economy is required prior to the closing of a transaction constituting foreign critical investment under the New FDI Regime.
- **Optional Screening Procedure:** applies in case of foreign so-called non-critical investments, which do not fall into the fields designated by the Government Regulation. The foreign investor may choose to consult the foreign investment with the Ministry of Economy, or alternatively, the Ministry of Economy may choose to review the transaction at a later point within two years of its completion. The New FDI Regime does not expressly require the foreign investor to obtain approval prior to the closing of the non-critical foreign investment.
- **Ex officio Screening Procedure:** the Ministry of Economy may initiate a screening procedure on its own initiative based on a recommendation from other consulting authorities, the Police, or the Information Agency when there is reasonable presumption that the investment may pose a threat or disruption to the security or public order of the Slovak Republic or the EU (within two years after the closing of the investment).

The initial assessment lies within the discretion of the investor to assess whether the scope of business of the target is likely to fall within the fields designated by the Government Regulation as foreign critical investment. With respect to the degree of plausibility of its designation, the investor needs to balance 1) the delays associated with obtaining prior approval from the Ministry of Economy, against 2) the risk of not opting to request prior approval, which could lead to the investment being prohibited and reversed at a later stage.

In connection with these procedures, the New FDI Regime provides for new investigative powers granted to the Ministry of Economy. Provided that there is a presumption of activities which are not in line with the requirements of the New FDI Regime, the Ministry of Economy may pursuant to a submission or on its own initiative conduct controls on the premises of the relevant entities, more commonly known as *dawn raids*.

The Ministry of Economy has the ultimate discretionary power to issue the final decision on foreign investments under the New FDI Regime, considering the following factors:

- circumstances concerning the target,
- circumstances concerning the foreign investor, including the persons controlling the foreign investor and persons controlled by the foreign investor,
- broader circumstances under which the foreign investment was planned and executed.

This is a welcomed change as the Government approval (under the Former FDI Regime) was subject to no statutory period and placed the potential investor in a high degree of uncertainty with respect to the feasible timeframe of such screening. The investments are assessed on the grounds of the security and public order of the Slovak Republic and the EU.

1.4 Sanctions

The New FDI Regime stipulates a range of considerable sanctions for breaches of the obligations of foreign investor. The sanctions applicable mostly to the foreign critical investments may be levied up to the value of the foreign investment itself, or up to 2% of the aggregate net turnover generated in the last accounting period by the foreign investor, the person controlling the foreign investor, and the person controlled by the foreign investor (whichever would be the highest). In case the value of the foreign investment is not possible to calculate based on the said methods, a fine of up to EUR 1,000,000 may be levied.

Foreign investors may face considerable sanctions in case of a breach of obligations under the New FDI Regime.

2 Expected impacts in practice

Ruling out potential FDI screening based on publicly available information will likely remain a challenging task for legal counsel advising on foreign investments. This could be particularly problematic with respect to entities operating in industries closely related to the fields listed in the Government Regulation as critical foreign investments. To be on the safe side, foreign investors may elect to apply for optional screening procedures to avoid any uncertainties concerning the designations of their foreign investment.

Ruling out the plausibility that a foreign investment would be classified as foreign **critical** investment on the basis of publicly available information will likely remain a major challenge.

Although not tested in practice, even the optional screening procedures are likely to take at least one (1) month under the New FDI Regime. This could present a considerable hurdle in fast-paced international cross-border investments. The silver lining might be the fact that such investments are likely to be subject to FDI screenings in other EU jurisdictions requiring approvals from other competent authorities under similar timeframes. As a safeguard against undue delays, the New FDI Regime provides that in case the foreign investor does not receive a notification of commencement of the screening procedure within 45 days as of receiving the screening request, presumption that no risk of negative effect of the foreign investment was identified applies.

Lastly, the New FDI Regime may impact secured finance transactions concerning securities held by non-EU security agents. This is due to the fact that the enforcement of a pledge may qualify as a foreign investment when the non-EU security agent (foreign investor) would obtain ownership or right to dispose with important assets of a target constituting foreign critical investment. At this stage, there is paucity of practice, secondary legislation and academic commentary, which would all provide further guidance on the outlined ambiguities.

While implementation of the comprehensive New FDI Regime is generally a positive step towards modern FDI legislation with the flexibility to react to potentially hostile foreign economic interventions by means of investments, the law is still a work in progress, and practical application could soon shed more light on the procedural ambiguities.

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