CEE you there!
Foreign direct investment in Central and Eastern Europe
Part 1
Introduction

For many years, a large number of multinational companies made decisions to invest in or relocate to Central and Eastern Europe (CEE). Many CEE countries found themselves the subject of the amorous advances of such investors and competed vigorously to attract an investor’s attention, to get the investor to the altar, and to exchange solemn vows.

However, since 2009, the process of courtship has become longer and more complex with investors now more nervous about the stability of the region and the consequences of its rapid growth prior to 2009, as well as some governments being more concerned about budget deficits and more reluctant to hand over dowry in the form of cash grants.

Nevertheless, CEE remains attractive for many with investors noting that “New Europe” offers emerging market growth combined with ready access to wealthy European consumers. In the case of Poland and Hungary, the number of FDIs rose 40% and 38% respectively from 2009 to 2010.

Enough of marital metaphors – the “usual suspects” have been the Czech Republic, Hungary, Poland and Slovakia with their respective fortunes waxing and waning from year to year but with an increasing interest also in other countries in the CEE region such as Romania and Serbia. With each large investment, the governments and populations of each of these countries wait with bated breath for the decision of the investor.

That decision can be vital to a region’s (or even a country’s) fortunes and progression out of the financial crisis; indeed, the future employment prospects of hundreds or thousands of people may hang in the balance. A large automotive project, for example, can bring with it a long chain of suppliers, bringing enormous financial benefits and jobs to a country.
Most investors that we have spoken to undertake a CEE tour, filling in their matrix of factors to take into account in each country, be they labour costs, tax rates, site availability and suitability, access to skilled labour or of course, the availability of investment incentives. In view of what is at stake for all parties involved, we consider it vital to try to provide some sort of guide to foreign direct investment (FDI) in CEE.

This publication is addressed to senior project managers (and, ultimately, board members of companies) who are considering investing in the Czech Republic, Hungary, Poland or Slovakia (the so-called Vyšegrad 4), as well as the other “tiger” in the region, Romania.

It is designed to facilitate decision-making and to begin to draw together information which generally tends to be available only on a country-by-country basis.

We recognise of course that investors also increasingly consider other countries in the wider C&SEE, such as Serbia, the Ukraine, Bulgaria, Turkey and Croatia.

For the purposes of this publication, however, we continue to focus on the five countries mentioned above.

**Warning!** Rules change, time limits and thresholds change, and of course governments change. The information in this publication will in every case need to be double-checked at all times to ensure that it is up to date.

This publication does not seek to portray any country in any more favourable light than another – it simply seeks to set out as objectively as possible some of the key points of interest for an investor looking to invest in CEE.
Part 2
Trends in FDI

Various bodies, such as the CEEMEA Business Group and Ernst and Young, have observed trends in FDI in CEE, including, for example:

- The move from traditional manufacturing to service industries (banking, IT, telecoms etc.) in the late 1990s and early 2000s and the recent move back to manufacturing (for example, despite the overall number of FDIs falling, the automotive and pharmaceutical sector have remained buoyant).
- Use of CEE countries for IT, outsourcing or co-outsourcing, “BPOs”.
- The change from predominantly greenfield and brownfield investment to more existing foreign investors reinvesting profits in CEE.

These trends can be prompted by macro-economic conditions or cycles (labour markets and costs being such that Western European manufacturers feel that they simply cannot survive unless they restructure their cost base by moving manufacturing to a cheaper location), or otherwise cutting costs by (outsourcing call centres etc.), or more political considerations, such as the Lisbon Strategy (see Part 3). In each case, however, the unavoidable conclusion must be that the final decision to invest or relocate can be undertaken only if it makes sound financial sense.
According to a survey by Ernst & Young1, CEE (the region including, among other countries, the Czech Republic, Hungary, Poland, Slovakia and Romania) is regarded by international executives as the third most attractive foreign investment locale after Western Europe and China and is the second most favoured place for investments in manufacturing industries.

Whilst the CEE suffered a slide in investor confidence in 2009, the regaining of a top three spot in 2010 implies that investors see the current economic and political problems in the region as temporary.

In fact, capital inflows into eight countries, the Czech Republic, Croatia, Hungary, Poland, Romania, Slovakia, Ukraine and Turkey increased 9% in 2010 over 2009.

The proactive response to the economic crisis of governments in CEE underscores the region’s dedication to creating an attractive future. The fact that GDP growth is expected to accelerate over the next three years in the Czech Republic, Hungary, Poland, Slovakia and Romania supports the investors’ revived enthusiasm.

FDI projects in CEE are usually labour intensive and create a significantly higher number of jobs per project than their counterparts in Western Europe.

Poland and the Czech Republic and to a lesser extent Slovakia, have emerged as the leading economies of the CEE. Whilst the overall number of jobs and FDI have fallen in Poland, investors continue to put their money in Poland’s diverse economy and the service sector remains stable. Equally, the Czech Republic is seen by many investors as a stable westernised market and the ideal place for establishing global headquarters.

CEE countries remain highly competitive in terms of cost base compared to their western counterparts.

This, twinned with a supply of highly skilled labourers, and extraordinary language capabilities has meant it has kept its competitive advantage in manufacturing.

Examples of automotive manufacturing investments alone in recent years include Kia and PSA Peugeot Citroen’s investment into Slovakia, Daimler, Audi, Suzuki, Hankook in Hungary, TPCA and Hyundai in the Czech Republic, Ford’s expansion into Romania, FIAT’s entry in to Serbia, and in electronics, HP, Dell, Hon Hai and AU Optronics’ confirming longer-terms plans for the CEE. These are only a tiny proportion of announced investments and expansions.

1 Ernst & Young’s European attractiveness survey, June 2010
Choosing a country for investment

For any company looking to locate or relocate within CEE, clearly many different factors may be relevant to the decision of which country to choose; and, depending on the nature of the business and the proposed project, an investor will no doubt give different weight to different factors.

A project manager will consider a number of possible real estate sites within a variety of countries, be they sites offered by the relevant countries or sites found through their own sources. From this point of view, if the project will lead to a high turnover of bulky products, it may be crucial for the factory to be situated near a good transport infrastructure, whereas the choice of a site for a project involving research and development or service industries may depend much more on the availability of skilled labour nearby. Many high volume projects dealing with, for example steel, will require the site to include a railway siding with access to high speed rail corridors.

From a country point of view, low labour costs and low tax rates may be crucial. On the other hand, many investors believe that labour costs in traditionally low cost countries will shortly reach EU norms anyway (although statistics have shown that this has not generally been the case), or that another neighbouring country may easily lower its tax rates on demand to match low rates offered in some countries (which has more or less happened), or that the preferred target country may raise taxes (such as VAT) after the next election. With regard to any incentives being offered, many investors consider them a non crucial factor, whereas in other projects their availability may directly tip the balance in one country’s favour. Clearly, the list of available factors to consider will vary widely depending on the needs of the project and of the investor.

Short of crystal ball-gazing, reading tarot cards, consulting oracles and mediating with spirits, the most an investor can do is work out what are its key “drivers”, weigh those factors, build in some margin for labour costs increasing, take a view on the likely stability of tax rates, work out which site in the end will offer the most realistic prospect of commencing business within the shortest timeframe possible (and with the least opportunities for hitches and headaches) and, where appropriate, negotiate as much “here and now” incentives as comfortably as possible within the context and framework of avoiding adverse EU Commission scrutiny.

This is not to say that any decision to invest or relocate is speculative, however — detailed planning and obtaining advice are crucial and no board will or should give the go-ahead for an investment unless all of the factors described in this brochure have been vigorously and diligently researched and presented to the board in a coherent fashion.
There are areas where lawyers and financial advisers can only provide “soft” guidance. One of these areas is politics. There are numerous examples of investors (all over Europe, not just in CEE!) being sidelined and forced to watch in dismay and frustration as squabbles develop, with politicians scoring points off each other while billion dollar investments wait in the wings. Frequent dismissals of ministers and officials is a turn-off, as are public spats about who has mishandled which investor and why. Clear and decisive action is necessary – otherwise can there be any surprise if an investor eventually gets tired of waiting and watching and wanders over the border to the gleefully open arms of another country?

We have set out in Table A a number of key factors which may be relevant for an investor. One factor which we have not included is the availability and cost of utilities. In relation to this investors should note that the majority of utilities in the five states are effectively privatised. Therefore, when considering its contracts for gas, water, electricity etc., an investor should remember that it is dealing with private companies who will not be offering incentives as a state-owned body might.

Clearly, it is not our role as legal advisers to provide a detailed economic analysis of the issues mentioned below and, of course, this type of information is soon out of date.

However, there are a number of sources of up-to-date information and analysis, for example the various state agencies which manage investment, and independent bodies such as the CEEMEA Business Group, and embassies and chambers of commerce which should always be consulted by an investor to get a good idea of the markets in which it is considering investing.

There are, nevertheless, a couple of aspects of FDI where the involvement of lawyers is crucial. The two main areas are in the negotiation and receipt of incentives from the various governmental bodies, and in actually acquiring the land where the project will be based. We will look at these issues in greater detail in Parts 3 to 6.
“Sources note the firm’s ‘real corporate strength’, and inbound investment expertise. Clients are ‘delighted with the service — the team’s regional knowledge is excellent and the responses are very quick’.”

Chambers Europe 2011
## Key factors for FDI Investors

### Real estate costs

<table>
<thead>
<tr>
<th>Country</th>
<th>Cost of land</th>
<th>Taxes</th>
<th>Construction costs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Czech Republic</td>
<td>This will very much depend on the region of the investment and the size of the site</td>
<td>Transfer tax payable by the transferor at the rate of 3% of the price determined by a sworn expert, or the consideration, whichever is higher. Real estate tax is payable annually. The rate depends on the type of real estate and territory, but is minimal.</td>
<td>These will very much depend on the nature of the project</td>
</tr>
<tr>
<td>Hungary</td>
<td>The general transfer tax rate is 4%</td>
<td>Real estate tax, depending on the type, location, purpose and use of real estate, payable annually. Stamp duty payable when submitting official applications or issuing certificates or permits.</td>
<td></td>
</tr>
<tr>
<td>Poland</td>
<td>Transfer tax for real properties up to HUF 1,000,000,000 is 4% and 2% thereafter (if when the real property’s value exceeds HUF 1,000,000,000). However, the amount of transfer tax may not exceed HUF 200,000,000. This rule also applies to the transfer of shares in a company which owns real property in Hungary. The purchase of land for the purposes of building may be exempt from tax if the acquirer of the land undertakes the building of residential property within four years. Local taxes including real estate tax or land tax may also be applicable.</td>
<td>Land registry registration tax between 0.15% and 0.5%</td>
<td></td>
</tr>
<tr>
<td>Romania</td>
<td>Real estate tax paid annually on any real estate owned – rate depends on the type of real estate and territory.</td>
<td>Notaries’ fees: between approx. 0.44% and approx. 2.2% of the price.</td>
<td></td>
</tr>
<tr>
<td>Slovakia</td>
<td>No tax payable on the purchase of land. Real Estate tax paid annually on any real estate owned – rate depends on the type of real estate and territory.</td>
<td>Land registry registration tax between 0.15% and 0.5%</td>
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## Taxation

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<tr>
<th></th>
<th>Czech Republic</th>
<th>Hungary</th>
<th>Poland</th>
<th>Romania</th>
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</thead>
<tbody>
<tr>
<td>Corporation tax</td>
<td>19%</td>
<td>10% for incomes up to HUF500,000,000,000 and 19% for incomes exceeding HUF 500,000,000</td>
<td>19%</td>
<td>16%</td>
<td>19%</td>
</tr>
<tr>
<td>VAT (general rate)</td>
<td>20%</td>
<td>25%</td>
<td>23%</td>
<td>24% standard rate and 9% reduced rate applicable to the supplies of certain goods and services</td>
<td>20%</td>
</tr>
<tr>
<td>Personal income tax rate</td>
<td>15%</td>
<td>16% - 20.32%</td>
<td>18% - 32%</td>
<td>16%</td>
<td>19%</td>
</tr>
<tr>
<td>Export tax</td>
<td></td>
<td>VAT payable on import from a non-EU country; import from EU countries subject to common EU VAT rules</td>
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<tr>
<td>Availability of State support</td>
<td></td>
<td>Please see Parts 3 to 5</td>
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</tbody>
</table>

### Availability of EU Structural and Cohesion Funds

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<tr>
<th></th>
<th>Czech Republic</th>
<th>Hungary</th>
<th>Poland</th>
<th>Romania</th>
<th>Slovakia</th>
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<tbody>
<tr>
<td>Amount allocated for period 2007-2013 (EUR million)</td>
<td>26,692</td>
<td>22,452</td>
<td>67,284</td>
<td>19,667</td>
<td>11,588</td>
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</tbody>
</table>
### Labour issues

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<tr>
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<th>Czech Republic</th>
<th>Hungary</th>
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<th>Romania</th>
<th>Slovakia</th>
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<tbody>
<tr>
<td><strong>Minimum monthly</strong></td>
<td>465</td>
<td>430</td>
<td>504</td>
<td>239 (since 1 January 2011)</td>
<td>448</td>
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<tr>
<td><strong>wage (USD)</strong></td>
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<tr>
<td><strong>Average gross</strong></td>
<td>1,436</td>
<td>1,156</td>
<td>1,173</td>
<td>609</td>
<td>1,176</td>
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<tr>
<td><strong>monthly wage</strong></td>
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<tr>
<td><strong>(2010) (USD)</strong></td>
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<tr>
<td><strong>Social security</strong></td>
<td>Approx. 11% (including 4.5% health insurance) for employees and 34% (including 9% health insurance) for employers</td>
<td>Approx. 17.5% for employees and 27% for employers</td>
<td>Approx. 42% for employers</td>
<td>Approx. 16.5% for employees and between approx. 27.75% and 37.75% for employers (depending on working conditions)</td>
<td>Approx. 13.4% for employees (including 4% health insurance) and 35.2% for employers (including 9% health insurance); (depending on the type of employment)</td>
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<tr>
<td><strong>costs</strong></td>
<td></td>
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<tr>
<td><strong>Level of employ-</strong></td>
<td>Although some strict pro-employee rules prevail, post-command economy style labour codes are being adapted to provide pro-employer flexible working structures. Detailed advice on these issues is available from A&amp;O offices (see also the A&amp;O publication on CEE Labour Law, obtainable from <a href="http://www.allenovery.com">www.allenovery.com</a>)</td>
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<td><strong>ment protection</strong></td>
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<tr>
<td><strong>legislation</strong></td>
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<tr>
<td><strong>Other</strong></td>
<td>Detailed advice should be sought as, for example, the mandatory or typical voluntary retirement, death, disability and medical benefits paid by employers will depend upon the relevant industry sector and region of investment</td>
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<tr>
<td><strong>employment costs</strong></td>
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<tr>
<td><strong>Availability of</strong></td>
<td>Czech Republic</td>
<td>Hungary</td>
<td>Poland</td>
<td>Romania</td>
<td>Slovakia</td>
</tr>
<tr>
<td><strong>workforce</strong></td>
<td>7%</td>
<td>10.8%</td>
<td>12.1%</td>
<td>6.87%</td>
<td>12.9% (June 2011)</td>
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<tr>
<td><strong>Recorded</strong></td>
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<tr>
<td><strong>unemployment</strong></td>
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<tr>
<td><strong>(2010)</strong></td>
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</tbody>
</table>
## Transport

<table>
<thead>
<tr>
<th>Country</th>
<th>Czech Republic</th>
<th>Hungary</th>
<th>Poland</th>
<th>Romania</th>
<th>Slovakia</th>
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</thead>
<tbody>
<tr>
<td><strong>Road</strong></td>
<td>Highway constr</td>
<td>Currently approx. 1,350km of highway</td>
<td>Highway construction programme to build 1,500km of new highway and 1,550km of new motorway to be completed by 2013. Currently over 873km of highway and 806km of motorway</td>
<td>Currently over 332km of highway</td>
<td>Currently over 400km of highway, mostly in the west. Highway construction programme to increase coverage to over 800km (to be completed by 2017)</td>
</tr>
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<td></td>
<td>uction programme to be completed by 2013, to increase coverage to over 2,100km. Currently over 1,000km of highway</td>
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<td>Currently over 1,000km of highway</td>
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<tr>
<td><strong>Rail</strong></td>
<td>Currently approximately 9,600km of railway. Rail network jointly operated by a state-owned body and a public company. Most important railway routes under reconstruction to increase traffic speed</td>
<td>Currently around 7,800km of railway. By 2007 the entire rail transportation system was opened to foreign railway companies. Rail Cargo Austria purchased MÁV Cargo in 2008</td>
<td>Approximately 23,500km of railway and 1,600 railway stations</td>
<td>Currently over 20,730km of railway. Rail network jointly operated by a state-owned company and private companies</td>
<td>Over 3600km of railway. Rail network owned by state company, operated by two state-owned companies (passenger and freight service) but private companies have access to the rail network. Company operating the freight service (Cargo) is to be privatised</td>
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<tr>
<td><strong>Air</strong></td>
<td>There are five public international airports and twelve private international airports. Main airports are at Prague, Brno, Ostrava and Karlovy Vary</td>
<td>International airports in Budapest (privatised in 2006), Sármellék (FlyBalaton airport opened in 2006) and in Debrecen (opened for international flights in 2004). Due to the ongoing investments at the Budapest Airport, the cargo capacity of Budapest Airport will be doubled to 250,000 tonnes/year until 2012 and the passenger capacity will be increased to 15 million passengers/year until 2014. Several smaller airports can be used for cargo transport. There are also some ongoing airport investments in Börögönd and Vát-Porpác</td>
<td>There are six international airports, including Frederic Chopin Airport in Warsaw</td>
<td>There are two main airports - Banuasea Bucharest and Otopeni Bucharest and eleven other international airports (e.g. Timisoara, Cluj, Constanta)</td>
<td>The two main airports are Bratislava (in the west) and Kolací (in the east). A smaller international passenger airport is in the north in Poprad. There are several other international airports which can be used for freight transport. A 30-year concession for the operation of the Bratislava airport is to be granted next year</td>
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<tr>
<td><strong>Water</strong></td>
<td>Linked to European waterway network by a single connection (the Labe Vltava Waterway) allowing access to Hamburg and ports on the Danube</td>
<td>The Danube is the main means of water transport, but other waterways are used. The main ports along the Danube are Budapest, Dunaujváros, Győr, Csepel, Baja and Mohács</td>
<td>Borders with the Baltic Sea. There is also a plan to join a Polish port to the trans-European North-South transport corridors, including a connection to Berlin and a connection between Gdansk and Odessa. The main ports are Gdansk, Gdynia, Szczecin-Swinoujście and Kolobrzeg</td>
<td>Borders with Black Sea and Danube, allowing access to upriver countries. The main sea ports and/or ports along the Danube are Constanta, Galați, Braila, Tulcea and Giurgiu</td>
<td>Some use of water transport, mostly along the Danube. Three ports (Bratislava, Komárno and Stúrovo), all on the south-west border. A project to develop the Váh waterway and a number of new ports is underway</td>
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Access to the Target Market(s)

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<th>Czech Republic</th>
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<tbody>
<tr>
<td>The whole CEE region is situated in the centre of the pan-European market, with each of the five states having particular geographical benefits</td>
<td>The Czech Republic borders the Western European markets of Germany and Austria</td>
<td>Hungary is closest to the Southern European markets, and also has good access to Western Europe through Austria</td>
<td>Poland borders the major Western European markets of Germany and the Baltic Sea, together with access to the Ukraine and the Baltic and CIS markets</td>
<td>Romania has borders with two other EU states, Bulgaria and Hungary, and also direct access to the Ukraine, Serbia and Moldova. Direct access to the Black Sea and to the Danube</td>
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Economic stability

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<tr>
<th>Czech Republic</th>
<th>Hungary</th>
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<th>Slovakia</th>
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<tbody>
<tr>
<td>Forecasted average annual real GDP growth between 2011 and 2012</td>
<td>2.8%</td>
<td>(Between 2011 and 2013 – approx. 3.5%)</td>
<td>3.3%</td>
<td>3.9%</td>
</tr>
<tr>
<td>GDP per capita in 2010 (USD at market exchange rates)</td>
<td>25,000</td>
<td>13,024</td>
<td>18,800 (estimate)</td>
<td>11,500</td>
</tr>
<tr>
<td>Inflation (average in 2010) (forecast for 2011)</td>
<td>1.5%</td>
<td>4.9%</td>
<td>2.6%</td>
<td>6.09%</td>
</tr>
<tr>
<td>Interest rates (average in 2010)</td>
<td>3.9% (long term interest: 3.9% (source: European Central Bank))</td>
<td>4.0% (Lending: 7.9% Money market: 6.2%)</td>
<td>3.5%</td>
<td>6.66% (National Bank of Romania)</td>
</tr>
<tr>
<td>Currency</td>
<td>Czech Koruna (CZK) 1 USD = 17.22 CZK (as at 17.05.11) (source: Bloomberg)</td>
<td>Hungarian Forint (HUF) 1 USD = 180.678 HUF (as at 18.05.11) (source: Bloomberg) No exact target date for the adoption of the Euro is stipulated. However Hungary may meet the Maastricht criteria by 2020</td>
<td>Polish Zloty (PLN) 1 USD = 2.79 PLN (as at 19.05.11) (source: Bloomberg) Aiming towards adoption of the Euro in 2015</td>
<td>Romanian Lei (RON) 1 USD = 2.83 RON (as at 07.06.2011) (source: Bloomberg) Aiming towards adoption of the Euro in 2015</td>
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Regulatory framework

<table>
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<th>Czech Republic</th>
<th>Hungary</th>
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<tbody>
<tr>
<td>Detailed advice should be sought on the regulation applicable to the particular type of project</td>
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</tbody>
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Sources:

2 Obviously these would change for 2011, please check rates
Part 3
Focus on incentives I: EU rules

Introduction

Various countries around the world seek to attract foreign investors by offering them subsidies, tax breaks, preferentially priced land and many other types of financial and non-financial assistance and advantages (incentives). Of course such incentives can be of real benefit to an investor and can play a very important role when deciding where to locate or relocate.

The CEE countries are no different in this respect. Nevertheless, following their accession to the EU on 1 May 2004 and 1 January 2007 in the case of Romania, each of these countries must ensure that any incentives it grants to a specific investor comply with EU law. It would be a fundamental mistake to assume, however, that just because the five countries are all in the EU, the incentives they will offer and the process an investor will have to follow to receive them will be the same or even similar. Sometimes a simplistic view is that “Surely EU law will dictate that each country may offer only the same amount of incentives?”. In fact, on the contrary, five very different systems have developed – indeed many countries take pride in making the offering of incentives as something of an art form which they do better than their neighbours. Some countries (for budgetary constraint reasons) may offer less than the maxima that the law allows for, whereas others (in their enthusiasm to attract investment) may be tempted to try to offer more than they are legally entitled to offer. It is therefore crucial for any investor considering investing in or relocating to one or more of these countries to understand both the underlying EU rules and the different approaches taken in each of the jurisdictions.

In this publication we will concentrate on the rules which are applicable to new investment projects in the five CEE states.

General prohibition

One of the fundamental principles of EU law is the promotion of competition (or, to put it another way, the prohibition of behaviour which is anti-competitive) within the EU internal market. Each year, the European Commission spends a great deal of time and money investigating (and taking to court) undertakings it believes have behaved in a way which is anti-competitive and seeking to prevent companies which have dominant positions in their markets from abusing those dominant positions.

Rather unsurprisingly, the giving of incentives to particular businesses is regarded as anti-competitive by the Commission. Undertakings operating in the same market will be competing on price and the quality and range of their products. If one of these companies is granted aid by a state (be it “free” money, tax allowances or any other preferential treatment) then it will be able to reduce its prices, improve the quality of its products or gain some other competitive advantage without having improved its efficiency or having invested its profits in research and development, for example.
Under EU law there is, therefore, a general prohibition on any Member State granting any kind of incentives capable of distorting competition and affecting trade between Member States – so-called state aid. To ensure there are no loopholes, the concept of aid is interpreted by the Commission and the European courts very broadly to cover any public aid that:

- is granted by a state or through state resources
- confers an economic benefit selectively on the recipient (whether a specific undertaking or a whole sector)
- distorts or threatens to distort competition
- affects trade between Member States

This very broad interpretation leads to the following conclusions: (i) aid granted by state owned or controlled companies, local or regional authorities or even private bodies (where they are benefiting from/redirecting public resources) is covered; (ii) the purpose of the aid is irrelevant when applying the relevant state aid rules; and (iii) the form of the aid is irrelevant, as both direct and indirect assistance is covered.

One development which has narrowed the scope of state aid is the development in case law of what amounts to being granted through state resources. For a finding of state aid, it is not sufficient that certain public authorities confer an advantage on a company. Rather, state aid also requires a financial burden for that state. Accordingly, in the case of France Telecom, a public declaration to support France Telecom and subsequent support for a proposal of a shareholder loan (which was never accepted) did not amount to state aid.

When considering the third of these, it is very important to understand that anything offered by a state could constitute state aid and potentially be prohibited, for example:

- Subsidies, contributions and grants
- Coverage of all or part of the interest on loans repayable by the aid recipient
- Coverage of part of a debt repayable by the aid recipient
- Temporary financial support
- The issue of a state or bank guarantee
- A tax or social security payment allowance
- The sale of immovable assets owned by the state or a municipality at a discount
- Free or subsidised advisory services
- Rescheduling of tax payments

It can never be possible to give a definitive list of everything which could be caught.
Exemptions

However, the promotion of competition within the internal market is not the only policy promoted by the EU. Another is the improvement of the standard of living in the poorer regions of the Member States to seek to reduce and eventually eliminate the internal disparities of income and opportunity between the regions.

This and other policies have led to a number of exemptions to the prohibition on state aid, including exemptions for aid granted across industries and regions for research and development, training, employment, environmental protection, etc. (horizontal aid) and exemptions for aid to facilitate the development of certain economic activities or of certain economic areas (sectoral aid).

These exemptions are interpreted narrowly by the Commission and the courts and any proposed aid must fulfil the following conditions:

- The duration, intensity and scope of the proposed aid must be proportionate to the level of intended benefit.
- The outcome of the aid must be in the Community’s interests and not simply in the interests of the relevant Member State.
- The measures undertaken must not conflict with any other provisions of the EC Treaty.
- The aid must meet the conditions set out in the specific EU rules and must not exceed the limits set out (limits may be the maximum percentage of the investment costs which the state may meet (aid intensity) or an absolute maximum figure which the state can grant).
The standstill principle and the block exemptions

State aid is thus allowed in certain exceptional circumstances. The basic rule applicable to such aid is that a Member State must refrain from implementing any state aid measure unless it has been notified to the Commission and authorised by the Commission (the so-called “standstill principle”). Any aid granted in breach of this principle qualifies as unlawful aid and should be recovered from the beneficiary. Yet in order to simplify and streamline the procedures, the Commission is authorised to adopt so-called “block exemptions”, which declare certain categories of aid automatically compatible with the common market and thus exempt from the notification obligation. For a number of years, a rather complicated system of several block exemption regulations was in place, further enhanced by several guidelines and notices issued by the Commission. In 2008, a major step forward has been taken by merging all the exemption instruments into one document called General Block Exemption Regulation. In addition, if the aid granted to one undertaking does not exceed EUR 200,000 over a three-year period (EUR 100,000 to an undertaking active in the road transport sector), it is also exempted from the notification obligation (the de minimis exemption).

The above development divided state aid measures into two basic categories:

- measures that are exempted from the notification requirement
- measures that are subject to the notification requirement

A state aid measure falls under the first category if it is covered either by the General Block Exemption Regulation or by the de minimis block exemption. The second category will be dealt with further in this document.

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3 COMMISSION REGULATION (EC) No 800/2008 of 6 August 2008 declaring certain categories of Aid compatible with the common market in application of Articles 87 and 88 of the Treaty (General block exemption Regulation)
Regional aid

Out of the exemptions covered by the General Block Exemption Regulation, probably the key exemption for an FDI investor is the exemption for aid to promote economic development in areas where the standard of living is abnormally low or where there is serious unemployment compared to the EU average (regional aid).

Because the grant of the aid is linked to the region of the investment, the Commission has determined which regions may receive aid and how much aid each of those regions can receive. The current percentage of the total investment costs which may be granted by a state in the regions of the five CEE countries are set out in Table B. Investors should note that the aid intensity figures given in Table B relate to regional aid specifically and that different levels will apply to other types of aid.

Note that it is extremely important to understand exactly how to calculate the value of the investment costs in determining to which figure the percentages mentioned below should be applied.

The costs which may be included in calculating the investment made will depend on the type of aid granted and the type of investment; for example, in relation to a new construction project the eligible costs will include the costs of land, construction and new machinery.

Investors should not be tempted to include a wide range of non-eligible costs in calculating how much aid they might be allowed and advice should be taken in calculating these figures, especially as the information provided regarding eligible costs must be transparent, itemised and accompanied by documentary evidence. Beware quoting high headline figures on a proposed project, as this will quickly lead to disappointment and confusion if the eligible costs are far lower.

There is particularly good news for small or medium-sized enterprises (SMEs) looking to invest in any of these regions as, under EU law, the percentage of the investment which a state may grant as aid to large enterprises is increased by a further 10% for aid granted to medium-sized enterprises and by 20% for aid granted to small-sized enterprises.

For large scale investments, however, the percentage of the investment which a state can make will be decreased depending on the size of the investment (i.e. the larger it is, the smaller the percentage a state can grant will be – see the “Guidelines on national regional aid for 2007-2013”).

There are also EU rules relating to economically sensitive areas (for example, the automobile and steel industries) where the percentage of investment which can be made by a state is reduced or aid may be prohibited.

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4 Enterprises which meet the following criteria: (i) having fewer than 250 employees, (ii) having either an annual turnover not exceeding EUR 50 million or an annual balance-sheet total not exceeding EUR 43 million, and (iii) being independent. Within the SME category, a small enterprise is defined as an enterprise which employ fewer than 50 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 10 million.

5 Investment projects with eligible expenditure of at least EUR 50 million.
Percentage of investment which can be granted as regional aid by a state

<table>
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<tr>
<th>Czech Republic</th>
<th>Hungary</th>
<th>Poland</th>
<th>Romania</th>
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<tr>
<td>Prague</td>
<td>0</td>
<td>Budapest</td>
<td>10</td>
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<td>Jihozápad</td>
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<td>Śląskie, Wielkopolskie, Zachodniopomorskie, Dolnośląskie, Pomorskie</td>
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<td>North-Hungary</td>
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<td>East Slovakia</td>
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<td>Moravskoslezsko</td>
<td>40</td>
<td>South-Dunáňtal</td>
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6 The EU is divided into different NUTS (Nomenclature of Territorial Units for Statistics) regions: there are NUTS I, NUTS II and NUTS III regions; the intensity of regional aid depends on NUTS II regions, which are territories with a population of between 800,000 and 3,000,000.

7 Except Warsaw – 30%

8 Only from 1 January 2009 (also before that date, only certain parts of the Bratislava region are eligible).

9 Slovakia is divided into 79 administrative districts. The maximum aid intensity is to be determined in line with the intensity limits applicable to each district, which depend on its unemployment rate, but also on the unemployment rate of the neighbouring districts.
Training aid

A further exemption which an FDI investor may well want to take advantage of is the exemption for training aid, under which a state may grant aid for the training of employees. Again, the percentage of the investment costs which the state may pay will depend on a number of factors, including the type of training and whether the training is given to disabled or disadvantaged people. The eligible costs which can be used to calculate the investment made by the investor are specified and include the trainers’ and trainees’ personnel and travelling costs and the cost of materials and supplies used for the training.

Further exemptions, such as aid for environmental protection, aid in the form of risk capital, or aid for research and development, are covered by the General Block Exemption Regulation. Details of any of the exemptions can be obtained from our local offices.

Notification and clearance

Unless the aid is caught by some of the exemptions, it must be notified to and authorised by the Commission. Where this procedure applies, the Commission may respond in two ways to an application for clearance:

– grant clearance to the proposed package of aid; or
– launch an in-depth investigation of the proposed aid measures.

An investor should be aware that an in-depth investigation may take up to 18 months and may have one of three results:

– the aid package may be granted clearance;
– the aid may be granted clearance provided that certain amendments are made to the package (for example, reducing the amount of aid or altering the timing of the aid); or:
– clearance may be refused.

In the second or third of these scenarios, either the investor or the relevant state may appeal against the decision within the relevant time limit, although any investor must be aware that this can be a very long and expensive process.

The financial crisis has exposed an important weakness of the state aid control system described above. Because of the strict requirement for an ex-ante review (i.e. a review before implementation), the notification and clearance system described above was not suitable for urgent crisis cases such as capital contributions or asset relief measures.

Therefore, since autumn 2009, the Commission has adopted a temporary framework whereby aid measures in favour of banks are declared temporarily available. This framework has been superseded by a new temporary framework applicable until the end of 2011.
A change in strategy

Given the constantly changing nature of the world economy and the changes taking place within the EU itself, the Commission’s approach to state aid has altered over time. The Commission has become very aware that the EU currently invests much less of its GDP in research and development than the US, Japan and its other main “competitors”. It has therefore introduced the so-called Lisbon Strategy which encourages investments in research and development and innovative technologies, rather than in straightforward manufacturing. That is also why the general block exemption regulation\(^\text{10}\) extended the exemption, which was formerly applicable only to SMEs, to all less problematic aid measures in research, development and innovation.

Why should an investor care?

The investor may believe that it does not need to care about these EU rules, as it is the state which is prohibited from granting illegal aid and which must seek clearance. But that would be to take far too simplistic a view.

As mentioned earlier, it can also be tempting for an eager state to offer more incentives than it should and for an eager investor willingly to accept what is offered; however, this could be fatal to the success of a project, and investors should beware.

If incentives are not properly notified or are granted before the Commission’s investigations are completed and clearance has been given (i.e. in breach of the stand-still obligation), the Commission has the power to request information from the state which granted the aid. The Commission may issue interim injunctions requiring the state to suspend the payment of any aid until the Commission has ruled on its compatibility with the relevant rules. If the Commission concludes that the aid cannot be exempted, it will issue a decision to the state directing it to recover the aid from the recipient investor together with interest at a commercial rate running from the time the aid was granted. The really bad news for an investor is that it is unlikely to be able to rely on its presumption that the aid was properly notified and cleared, and there is a 10-year limitation period for the recovery of unlawful aid. Aid possibly granted unlawfully may be brought to the Commission’s attention by the recipient’s competitors, who may also bring claims in national courts, seeking damages for the competitive detriment they suffered from the grant of the unlawful aid.

Even if the state represents to the investor that such investment does not constitute prohibited state aid, the investor should never blindly rely on this as, if the relevant state is wrong, the investor is unlikely to have any recourse. Even if it could build a legal case against the state, most investors would wish to avoid, for practical and many other reasons, suing the country where the investor has made a large investment (though this option cannot always be ruled out). And even if the investor brought and won a claim, it could well be argued by the Commission that any damages awarded were also state aid, again repayable by the investor. There have been recently some high profile examples of this, such as in Romania and in Hungary.

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10 Commission Regulation (EC) No 800/2008 of 6 August 2008 declaring certain categories of aid compatible with the common market in application of Articles 87 and 88 of the Treaty (General block exemption Regulation)
Clearance

As mentioned previously, if an investor has decided to invest in a particular region and has structured its project around receiving incentives from the state, it is crucial that those incentives are either exempt from the notification and clearance obligation, or, if clearance is required, cleared by the Commission; if the incentives package is not cleared, the investor may need to reconsider the site of its investment or the structure and timeframe of the project, thereby incurring further costs and wasting additional time.

It is therefore very important for any investor to take sufficient time, both before approaching a state for aid and while agreeing a package of incentives, to really consider whether the incentives granted to it need to be notified and cleared by the Commission. If so it is extremely important to assess whether it is realistic to expect a clearance and how to present the project and incentives to ensure they are cleared.

Firstly, as any aid granted by the state (even regional aid which could fall within the exemption) could distort competition, it will only be cleared if it genuinely promotes the EU’s policy of improving the economic balance between regions of the EU.

Therefore, when the investor presents its project to the relevant state and when the state applies to the Commission, there must be real focus on the benefits to the region which the investment will bring. Although it is natural that any investor will concentrate on the advantages to its business, it must be able to show that it and its project would be competitive even without the proposed incentives and that any benefits it receives will only be a necessary side-product of, and significantly out-weighed by, the great advantages for the region. If the Commission believes that the main reason for the investor’s relocation is that it will receive aid and that, without it, the investor could not operate and be competitive in the market, the Commission will not give clearance.

It is essential that the investor, and not only the relevant state, focuses on this, as most (around 90%) of the information which must be notified to the Commission relates to the investor and its project. It is crucial that it is presented in the correct way and, of course, given the change in strategy of the EU (and the almost certain change in strategy of the governments in the five states) it is always a good idea for a potential investor to emphasise any research and development, and any technological or innovative aspects of its project.

Secondly, where the investor is a big player in its field and has a dominant position in its market (especially if supply exceeds demand) it would be very difficult, if not impossible, to persuade the Commission to give clearance to incentives granted to such an investor. The Commission would take the view that any incentives granted to a dominant market player would help to strengthen its dominant position and potentially drive competitors out of the market. It would be very difficult to argue that such a distortion of competition was out-weighed by the benefits to the region invested in.

Depending on the investor’s circumstances and well before any detailed discussions with the relevant state agencies, it can really be worth an investor instructing specialist EU lawyers, who can analyse the relevant market and the investor’s position within that market. Spending time and money investigating these issues can save a lot of wasted time and money dealing with the state agencies and arguing with the Commission if it is clear from the outset that aid will never be granted clearance.
Other support offered by the state

When an investor approaches a state for incentives and agrees on a site for investment, the state may offer to carry out works which, although not specifically targeted at the investor’s project, will be of significant benefit.

For example, it may offer to build roads which link the investment site to the nearest highway or improve telecommunications or utilities connections, which it does not consider to be aid because this infrastructure could be used by businesses other than the investor. Remember though, it will never be enough to prove only that third parties would be entitled to use the roads, telecommunications etc.; rather the investor must be convinced that others will use them. It must be clear that these are not being built solely for the advantage of one investor.

Conclusion

The risk of misunderstanding the rationale behind the exemptions from the prohibition on state aid (i.e. understanding why the proposed investment may be entitled to receive incentives), getting the required information wrong, not taking into account the relevant timing and deadlines, or misjudging the approach of the Commission could have consequences that would be disastrous for a company which is investing or relocating for important strategic and financial reasons.

Once again, the crucial issue is for the investor to analyse the facts and the related legal issues before agreeing to make any investment. Time spent analysing the offered improvements and their benefit to other parties is time (and money) well spent.
Part 4

Focus on incentives II:
incentives available in CEE

It is worth reiterating, as will become clear, that each of the five CEE countries has a very different approach to granting incentives. An investor should not fall into the trap of assuming that the incentives available or the application process in a particular state will be the same as in the other CEE countries. Individual agencies will have official or unofficial guidelines which may or may not have the force of law.

We do not propose to give a detailed explanation of all the types of aid provided in each jurisdiction or the conditions an investor must meet to receive them – what will be available to a particular investor will depend on many different factors and detailed advice on the incentives available should always be sought. We have therefore sought instead to provide a guide to the overall approach taken to incentives by each country and to give an idea of what might be available. However, before considering the approach taken in each of the five CEE states, there are some general points which an investor in any of these states should consider:

Presenting your project

Whichever country the investor is considering investing in, it will need to prepare a detailed plan of its project, setting out, amongst other things, the nature of the project, the investment it intends to make (how much and into what), the jobs it intends to create (how many, what types, when and for how long), the technological benefits of the project and the research and development aspects of the project. It is crucial that the investor does this very early in the process as the description of the project will affect what incentives the investor can receive, be the benchmark against which receipt of incentives is measured and help the relevant state agency to explain the proposed incentives package to the Commission and local governmental bodies and committees.
Dealing with the state

It will come as no surprise to learn that dealing with the state in these five CEE states is different to dealing with any other commercial party. Firstly, the scope of the state’s room for negotiation will be limited by many factors, including national and EU legislation, national and in-state regional policies, the budget, the requirement to have any decisions approved by various governmental bodies and committees and the need to “sell” any decisions to the public. There may therefore be political tensions involved.

Secondly, any process which involves state agencies and the European Commission will be inherently bureaucratic and may become long and drawn out. Any investor must be prepared to take the inevitable delays in its stride and potentially factor these into the timeframe for its project. On the other hand, taking early advice and being scrupulously organised can significantly help to reduce delays and keep projects on track.

Finally, there is a more general point. As most investors are aware, dealing with parties in different jurisdictions requires an understanding of the differences in culture, styles of negotiation and approaches to decision-making. It is worth taking time to talk to other local contacts, such as commercial sections in embassies, chambers of commerce and, of course, local lawyers, financial and tax advisers and accountants, to get a feel for any important factors which should be considered.

Financing your project

As a major undertaking, usually operating in numerous jurisdictions, it is likely that any FDI investor will have already considered, if not decided on, the structure of the financing of the project even before it discusses incentives with the relevant state agency. For tax, corporate or structural reasons the investors may have decided, for example, to:

- Manage: manage the project through a local vehicle or a foreign operating company
- Fund: fund the project through intra-group loans, bank debt or equity investment in a local vehicle
- Lease: have the buildings and assets used in the project owned by a local company or by a foreign parent and then leased to the local vehicle

It could therefore come as a very nasty surprise for an investor to discover that, while a state is willing to offer incentives, it will only do so if the project is funded a certain way and if assets are owned within the jurisdiction. If this is likely to be an issue for an investor, it should be raised with the relevant state as early as possible. Many of the countries have a requirement that the project company must be a company incorporated in the relevant jurisdiction – it is questionable whether this requirement is compliant with EU law, but in practice most investors usually comply with this requirement anyway.
EU structural funding

Whatever the rules in a particular country regarding the grant of incentives out of national government funds, an investor should also consider the availability of EU structural funds. These are central EU funds allocated to regions with lower than average GDP to help improve the standard of living. As the five CEE states have some of the poorest regions in the EU, they will each be entitled to quite significant amounts of structural funding over the next few years.

This funding can be used by the relevant state in a variety of ways, to support specific regions, programmes and businesses. As one example, in the Czech Republic for the period 2007-2013, the following programmes (among many others) have been set up:

- Programme for infrastructure for industrial research, development and innovation – providing grants to Czech companies to assist with the establishment of science parks, centres for technology transfer and other links between research and development and industry
- Real Estate programme – providing grants to municipalities and SMEs to upgrade the quality of existing and new business sites and industrial zones (so-called “brownfields”)
- Start programme – providing preferential interest-free loans for small enterprise start-ups

We do not propose to give full details of all the programmes funded in each country as they are numerous and complex. However, it will always be worth an investor investigating the availability of such funding, either because it is able to benefit directly or because the region it is looking to invest in will do so. Advice on the availability of such funding will be available from the relevant state body and local lawyers, although one issue an investor should always bear in mind is that the allocation of EU structural funding will still be subject to the general EU rules on state aid described in Part 3.
In the Czech context, it is important to distinguish between state aid in the broad sense and “investment incentives”. All investment incentives represent state aid, but not the other way round. Under Czech law, “investment incentives” is a technical term used for describing certain specific forms of state aid granted under specific pieces of Czech legislation.

However, it is possible that state aid could be granted to attract foreign investors on an individual basis, which goes further than the investment incentives allowed under the existing investment incentives schemes. Such aid would therefore fall outside the framework of the relevant Czech legislation, but this is rarely (if ever) used.

Investment incentives in the narrow sense represent so-called Czech “aid schemes”. These were approved by the European Commission upon the accession of the Czech Republic to the EU. Consequently, these incentive measures are considered to automatically fulfil all the requirements and conditions applicable under EU law, without clearance by the European Commission being required.

The process of applying for and being granted these investment incentives therefore remains in the competency of the Czech Republic and is transparent and effective. For more details on the procedure, please refer to Part 5.

Due to the qualities of the currently available investment incentives schemes in the Czech Republic (for details, see below), all major investment projects since the introduction of the incentives schemes have been granted on the basis of these schemes.

The main reason for this is that as long as investors stay within the aid schemes they can avoid the lengthy and costly procedures before the European Commission. Nevertheless, should the investor require special individual treatment, it is theoretically possible to negotiate with the Czech state on a case-by-case basis.

However, if the individually negotiated aid goes further than the available investment incentives schemes, the individual aid would have to be notified to and cleared by the European Commission and would be subject to its discretion.

Furthermore, the currently available incentives schemes try to offer investors the maximum amount of aid permitted by the EU state aid framework.

As a consequence, it is uncertain whether the EU would clear an attempt by an investor to benefit from a higher level of state aid unless exceptional circumstances applied.

Finally, in relation to this, we have also been informed by CzechInvest, the Investment and Business Development Agency in the Czech Republic that it does not envisage that in practice aid will ever be granted outside the aid schemes described next.

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11 Incentive measures granted eg. under the Act on Investment Incentives
Investment incentives

The grant of incentives in the Czech Republic usually follows a very structured approach, with the incentives available to a particular investor depending on specific legislation (working within the framework EU rules that were described in Part 3) dealing with the specific industry sector which the investor operates in. Given this very structured approach and the lack of any real negotiation between the Czech state and the investor, it is possible for a quite detailed picture of the incentives an investor might receive to be provided by local lawyers.

The Czech Republic currently offers incentives only in the manufacturing sector, nevertheless, it is crucial for an investor to consider whether his project meets the relevant legislative conditions before trying to receive incentive for it.

Under the Act on Investment Incentives, the basic conditions that an investor’s project has to fulfil to qualify for incentives to be granted are:

- it must launch a new production or expand existing production;
- there must be an investment of at least CZK 50 million / CZK 60 million / CZK 100 million (depending on the unemployment rate in the region where the investment project is implemented) into the acquisition of long term tangible or intangible assets. At least half of this amount must be an equity investment by the investor;
- a minimum of 60% of the total investment must be in the form of an investment into machinery which is not older than two years, with the overall investment objective of installing a new production line, expanding an existing one or modernising the production process;
- the investor must keep the investment for at least five years from the fulfilment of the general conditions (the same applies for job creation grants where the investor must keep the number of newly created jobs for at least five years from the date the grants are first applied for); and
- the investment project must be environmentally friendly and comply with all Czech requirements on environmental protection.
The incentives specified under the relevant legislation are: (i) tax incentives (for up to five years full corporate tax relief for newly established legal entities, and partial corporate tax relief for expansion of existing production); (ii) job creation grants; (iii) training and retraining grants; and (iv) site support (transferring of public land at a favourable price).

The investor can apply for the corporate tax relief only after fulfilling the general conditions for the granting of incentives and special conditions for the granting of corporate tax relief. This application can be made within three years from the date when the incentives were granted. Therefore, for example, an investor who fulfils the general conditions in the first or second year from the date incentives were granted could nevertheless wait until the third year and begin applying the tax relief in this tax period. This may provide the investor with the flexibility to apply the tax relief in the period where it will be most efficient to do so. Once three years have passed, the five-year tax relief period will begin to elapse automatically, regardless of whether the investor makes a profit or loss. This tax relief is available, in slightly different forms, both to new legal entities established to carry out the investment and for the expansion or modernisation of existing companies.

In areas where the unemployment rate is more than 50% higher than the national average, an investor can be provided with a job creation grant amounting to CZK 50,000 per employee and/or a training grant amounting to 25% / 35% / 45% (depending on the size of the business) of the costs it spent on the qualifying training.

Formerly, incentives were also available to Technology Centres, centres for innovation activity and Business Support Services supporting the employment of highly educated professionals. However the program granting these incentives was closed in July 2008 and therefore there are currently no incentives available in this sector.

The Czech Ministry of Industry and Trade has announced a planned amendment of current legislation regulating this area, which would submit the incentives provided to the manufacturing sector and those earlier provided to Technology Centres and Business Support Services, to a single legal regime. This would bring even more favourable conditions for the investors – longer tax relief period, higher amount of the grant for job creation and decrease in the minimum requested share of machinery on total investment\(^{12}\).
Other available support

Except for the aforementioned incentives, there are also other forms of support available to investors engaged in projects in the Czech Republic. The basis for this support is Operational Program Enterprise and Innovation, within which framework the Ministry of Industry and Trade introduced a total of 15 aid programmes. However each program provides its own criteria, which have to be met in order to receive the support. Eligible projects are those that are implemented on the territory of the Czech Republic outside the capital city of Prague (subject to a few exceptions). Under the aid programs, funding is provided in three different forms:

1. **Non-refundable subsidies**
2. **preferential loans**
3. **guarantees**

The procedure for granting support begins with a public call for completion of the investment proposals which will be co-financed with public funds. The proposals must be filled using the special web application eAccount, and must be electronically signed. The Ministry reviews the proposals in line with the criteria laid down in the aid programmes. After being granted the support, both the Ministry and CzechInvest (Investment and Business Development Agency) provide ongoing monitoring of compliance with the required criteria, and exercise inspections in the places of investment.

Industrial parks/economic zones

Whilst the Government supports businesses to locate their activities in certain areas of the Czech Republic, this does not take the form of “economic zones” as such, in that there are not any special zones which benefit from a special legal status (and associated special laws).

Instead, the Government may work with municipalities to try to encourage development in certain areas through maximising the synergies available to businesses that choose to locate in those areas by, for example, infrastructure projects, or land clearances which make areas more suitable for a particular type of industry. As noted above, municipalities may also seek to sell land to investors at preferential rates to encourage investment in particular areas. On a strategic level, this may tie in with national projects to further increase the attractiveness of certain areas.
Hungary

General structure of incentives

In Hungary, the types of incentive which are available are set out in a series of legislative instruments. The system of incentives is quite structured and any potential investor in Hungary should always make sure that it is aware of the two levels of rules which will apply to any grant of incentives, being:

General Rules
over arching general rules on aid
(applicable EU legislation and the State Aid Decree i.e. the Hungarian government decree implementing such legislation, which determine the legality of any individual instance of aid being granted and which provide a framework for the available forms of incentives)

Particular Rules
particular rules on incentives which are specific to Hungary
(which implement the general framework and govern the details regarding the conditions and the process for providing individual forms of incentives)

The legislative provisions which relate to each type of incentive can be very complex (for example in relation to the conditions the investor must fulfil to be eligible) and it is crucial that an investor gets detailed legal advice on these matters, especially as failure to do so can result in an application being rejected without its merits being considered. The four most important pieces of legislation under which incentives are available to FDI investors in Hungary are:

- the State Aid Decree
- the Investment Incentives Decree, under which investment incentives may be granted by the Hungarian government;
- the Corporate Tax Act, under which tax incentives may be granted generally; and
- the Investment Tax Incentives Decree, under which investment/development tax incentives may be granted.

Under the State Aid Decree a variety of incentives may be granted, namely:
- repayable and non-repayable contributions or grants;
- tax allowances;
- tax base allowances;
- capital contribution;
- real property or the right to use real property (or direct subsidies for the acquisition of real property or the right to use real property);
- subsidised guarantee fees;
- subsidised factoring fees; and
- subsidised leasing fees.
Under the Investment Incentives Decree, the government may grant direct cash subsidies only. The government will make decisions on a case-by-case basis. Investors may apply for the subsidy for a variety of purposes which include (but are not limited to):

- Technology: the technological development of new enterprises
- Promotion: promoting direct capital investment in Hungary
- Training: subsidising training
- Research: investment in research and development (R&D)

The relevant state bodies are entitled to grant incentives under this legislation to achieve a number of purposes and so these incentives will be granted to projects which bring the most relevant benefits to Hungary. In the case of capital contributions, the state generally does not become a shareholder as a result of granting the aid.

In respect of timing - while an investor may want to receive all incentives at the start of its project, it is very likely that the state will want to stagger payments over a period of time, perhaps linking them to the timing of investment by the investor and making them payable over the entire length of the project (to encourage the investor not to pull out of the investment site before the region has reaped all the envisaged benefits).
Sectors favoured by the Hungarian Government

The Hungarian Government views its principal priorities as the development of the economy, employment, traffic, human resources, health and wellness services, the environment and energy, public services and the regions. It is therefore worth any potential investor emphasising any such elements of its project when applying for incentives in Hungary.

Applicable conditions/procedure

One key fact that any FDI investor should appreciate is that only corporate entities (with or without legal personality) which have their registered seat in Hungary or private entrepreneurs may apply for incentives. It may therefore be necessary for an investor to set up a new company in Hungary to manage the application and project, and detailed advice on how to do this can be obtained from our Budapest office.

Incentives granted under the Investment Incentives Decree will usually be granted under an aid scheme programme (therefore not requiring individual clearance by the European Commission) involving a tender process (for details, see Part 5), where the guidelines produced in relation to the specific tender will include details of the conditions which any potential investor will have to meet in order to be considered. There are, however, some projects which the Government will consider outside the tender system, where the applicable conditions will be the subject of some negotiation between the investor and the Government (and which will require individual clearance from the Commission). Two examples of projects which may receive support outside the tender system are:

(i) major investment projects of great national economic significance that create a manufacturing industry capacity with eligible investment costs exceeding the HUF equivalent of EUR 50 million; and
(ii) regional service centres where the staff costs associated with the new jobs created by the investment project reach the HUF equivalent of EUR 10 million.

In summary, for an investor to qualify under the Investment Incentives Decree, their investment must create a certain number of new jobs. In the case of incentives that cost between the HUF equivalent of EUR 10 to 50 million, such investments must create at least 50 new jobs. Furthermore, the applicant must either have its seat in Hungary or be seated in the EEA while having a branch office in Hungary.

Tax allowances

The general corporation tax rate in Hungary is 10% of the tax base up to HUF 500 million and 19% for the part of the tax base exceeding HUF 500 million. Tax allowances may take the form of: (i) a decrease of the corporation tax payable; or (ii) a tax base adjustment item (i.e. which decreases the tax base instead of the amount of tax).
Development Tax Allowance

The most important form of the tax allowances is the development tax allowance (DTA). The benefit of the DTA is that it entitles the taxpayer to decrease its annual corporation tax by 80% during a period of up to 10 financial years. The amount of the DTA may be determined as a certain percentage of the net present value of the eligible investment costs that corresponds to the aid intensity in the particular region where the investment is made.

Eligible investments for DTA purposes are:

- investments of a present value of at least HUF 3 billion (approximately EUR 12 million);
- investments of a present value of at least HUF 1 billion (approximately EUR 4 million) in preferred regions (i.e. North Alföld, North-Hungary, South-Alföld and South-Dunántúl);
- investments resulting in new employment;
- special investments of a present value of at least HUF 100 million (approximately EUR 400,000) (e.g. investments to improve hygiene at food producers, R&D investments, investments of companies newly listed on a regulated market as from 1 September 2008, movie production investments, investments in the development of electronic telecommunication networks as well as the provision of broadband internet services, and investments in environmental protection); and
- investments of a present value of at least HUF 500 million made by SMEs

Provided that each investment results in the creation of a new facility or the enlargement of an existing facility or the essential change of goods/services supplied or the production procedure.

The permission of the Minister of Finance and the European Commission is required in respect of investments having a net present value of more than EUR 100 million.

In respect of other investments, the taxpayers themselves calculate and establish the amount of the DTA which should be reported to the Ministry of National Economy.

In order to obtain the DTA, a number of further conditions are required to be fulfilled and specific advice should be sought.
R&D allowances

Special tax allowances may be utilised in connection with the employment cost of R&D. Under this scheme 10-25% of the employment cost of R&D is deductible, during four tax years, from the corporation tax to be paid. Such allowances may not be higher than 70% of the corporation tax to be paid after obtaining the DTA. In addition, the direct costs of basic research, applied research and experimental developments decrease the corporation tax base. Under particular conditions, the corporation tax base may be decreased by an amount equal to triple such costs (up to a maximum of HUF 50 million (approximately EUR 200,000) in each year), where R&D activities are carried out by certain research institutes.

A further tax base adjustment allowance applies to royalty income. This may apply, for example, where as a result of an R&D activity an intellectual property is developed or is purchased / licensed and thereafter such intellectual property is licensed/ sublicensed to other parties.

Industrial parks

Hungary offers the widest selection of industrial parks in the CEE region: investors can choose from more than 206 operating industrial parks on the basis of their business, professional, or cultural needs. Establishing a business in such an industrial park is facilitated by highly favourable conditions, including management that is familiar with local circumstances, support from municipalities, and various tax benefits. Another very important point is that investments in industrial parks can usually be implemented in a few months.

The typical services specifically provided by industrial parks in Hungary are:

- the provision of the basic infrastructure needed for production (for example, energy, water and waste-water treatment facilities)
- a wide range of other quality services (for example, banking services, customs administration, consultancy, security guards and office services)
- promoting the development of a supplier base in the park
Availability of local advice

When considering the availability of incentives in Poland, it is important to note at the outset that the President of the Office of Competition and Consumer Protection, the body which administers the grant of incentives in Poland, should provide a potential investor with required information. However guidance may also be sought on the amount of incentives potentially available to an investor or the form which any available incentives might take from the Polish Information and Foreign Investment Agency (PIFIA) and local authorities. All these institutions should make comprehensive and consolidated information available to allow an investor to tailor its position to ensure that it receives the maximum possible amount of incentives available to it.

However, the primary source of information on the potential grant of incentives in Poland is the general rules on state aid set out in the EU regulations. The conditions used to define the concept of state aid are identical to those described in Part 3. As a brief reminder, state aid is aid which would:

- **Granted** be granted by the state or through state resources
- **Benefit** confer an economic benefit selectively on the recipient (whether a specific undertaking or a whole sector)
- **Distort** distort or threaten to distort competition
- **Trade** affect trade between EU Member States

Who can apply for incentives?

Polish regulations are generous as to who can receive incentives. In Poland, any entity that conducts business operations may be the recipient of incentives, irrespective of its organisational or legal form or the way it is financed. An investor can be a person or a legal entity which is attractive to FDI investors, who can choose the type of vehicle to maximise other advantages, for example, the tax or liability exposure of the investment project.
Incentives which may be available

Poland offers several incentives to attract investors, including regional, horizontal and sector aid instruments which are all compliant with the EU rules on state aid. This brochure focuses on regional aid; below is a brief outline of the key features of certain aid measures which should be considered by potential investors.

The value of incentives

The value of incentives is calculated on a case-by-case basis and mainly depends on the individual characteristics of the particular investment. However, the total public funding available for investment is capped by EU rules.

When considering an application for incentives, the relevant body will examine the total amount of incentives granted to investors in Poland in the relevant financial year, either as a monetary amount or as a figure representing the intensity of incentives. Incentives granted to an individual investor are expressed as the amount of money the recipient investor would receive if it was granted a subsidy, either as a gross or net amount. This means that any tax or other advantages given to an investor have the value of the advantage in the hands of that investor. For example, if the investor has a tax reduction, the value of the incentive is the amount of tax the investor does not have to pay.
Multi Annual Support Programmes

These are available only to large investments seen as strategic to the Polish economy. To qualify for this support, the entrepreneur must invest in a priority sector and exceed certain costs invested and number of new jobs created (as set out in Tables A and B below). The Multi Annual Support Programme usually includes several aid instruments e.g. corporate tax exemptions (if the investment is located in a special economic zone), preferential land purchase conditions, cash subsidies and a real estate tax exemption. The entire aid package is negotiated by the investor with PIFIA and the Ministry of the Economy and requires notification to the European Commission.

For aid intended to cover the costs associated with creating new jobs, the maximum level of aid is PLN 18,700 per job created. For aid intended to cover eligible costs of a new investment, the maximum level of aid is 10% of eligible costs.

Table A: Aid intended to cover the costs associated with creating new jobs

<table>
<thead>
<tr>
<th>new jobs created</th>
<th>eligible costs of the new investment</th>
<th>amount of aid</th>
</tr>
</thead>
<tbody>
<tr>
<td>automotive, electronics, aviation, biotechnology</td>
<td>250</td>
<td>PLN 40 million</td>
</tr>
<tr>
<td>modern services (i.e. business processing outsourcing (BPO) which includes, inter alia, operations of shared services centres and IT services centres)</td>
<td>250</td>
<td></td>
</tr>
<tr>
<td>R&amp;D</td>
<td>35</td>
<td>PLN 3 million</td>
</tr>
<tr>
<td>significant investments in other sectors</td>
<td>500</td>
<td>PLN 1 million</td>
</tr>
</tbody>
</table>

Table B: Aid intended to cover eligible costs of a new investment

<table>
<thead>
<tr>
<th>new jobs created</th>
<th>eligible costs of the new investment</th>
<th>amount of aid</th>
</tr>
</thead>
<tbody>
<tr>
<td>automotive, electronics, aviation, biotechnology</td>
<td>50</td>
<td>PLN 160 million</td>
</tr>
<tr>
<td>significant investments in other sectors</td>
<td>500</td>
<td>PLN 1 million</td>
</tr>
</tbody>
</table>
Before investing, a permit must be obtained from the Minister responsible for economic affairs, and this is granted if the following conditions (amongst others) are fulfilled:

- the scope of the planned activity must be compliant with the SEZ development plan;
- the SEZ administrator must have available land, structures or premises which are indispensable for the investor to run its business activity; and
- granting the permit can be justified by the degree of the intended business operations’ input into the objectives specified in the SEZ development plan.

Examples of new investments that satisfy the above criteria are, inter alia, investments in the formation of a new business, the diversification of a business's production or the acquisition of an existing business which is in receivership or would have been wound up.

The permit issued to the investor allows the activity to be carried out in that particular SEZ and also states the minimum value of investment which needs to be financed by the investor's equity (calculated on an individual basis but in any event such amount being a minimum of EUR 100,000).

The benefits for the investor include:

- income obtained from business activities conducted in the SEZ in accordance with the permit is exempt from corporation tax
- aid to support new investment projects
- aid for creating new jobs

Subject to certain exceptions (for example in relation to particularly large projects), SEZ aid benefits from the special arrangements on “existing aid” under the treaty under which Poland acceded to the EU. This means that SEZ aid does not necessarily have to be notified to the European Commission under the regular proceedings for notification of state aid, which saves both time and effort for the investor and the state.
**Cash subsidies**

Cash subsidies are granted from funds assigned from the State Budget and European Union to support businesses and innovation, with particular consideration given to the needs of small and medium-sized enterprises. Cash subsidies are granted via the Polish Enterprise Development Agency (PEDA). The procedure begins with the submission of an investment proposal. The Ministry of Economy then reviews the proposals in line with current economic policy objectives and successful investors are invited to sign an agreement with the Ministry specifying the value and timing of the investment, the number of new employees and other investment conditions.

*From a financial perspective, between 2007 and 2013, PEDA shall manage over EUR 7 billion in funds to effect various operational programmes. The largest parts of these funds are allocated to:*

- innovative economies
- human capital
- the development of eastern Poland operational programmes

**Real estate tax exemptions**

Investors can also receive support from the local authorities in the form of real estate tax exemptions. These exemptions are granted to a particular investor on the basis of a resolution of the relevant municipality.

Municipalities also have the right to fix real estate tax rates and establish exemptions. The tax rates in a municipality may vary due to the type, location, purpose and use of real estate. The amount of the real estate tax is set by a resolution of the municipal council; however annual rates cannot exceed the limits set out in the Act on Local Taxes and Charges. Under the act, the maximum annual rate for land used for business purposes cannot exceed PLN 0.62 per m² and PLN 17.31 per m² for buildings used for business purposes.
Romania

General structure of incentives

The Romanian Government has adopted a large number of state aid schemes to stimulate economic development. The general framework for state aid was originally established by means of a Government Emergency Ordinance No. 85/2008 which regulated, inter alia, types of incentives and general eligibility conditions. The legislation now in force follows EU legislation and does not add new or different ways of granting incentives. In December 2009 the Romanian Center for Promoting Trade merged with the Romanian Agency for Foreign Investments, the resulting entity is the Romanian Center for Trade and Investment (CRPCIS) whose main objective is to attract new investors and help them with the main guidelines for creating investments in Romania. Any foreign investor should request and receive from CRPCIS comprehensive and consolidated information in order to maximise its investment benefits.

Under Romanian law an “investment” means a capital contribution made for one of the following purposes:

– the purchase of tangible and/or intangible assets with respect to the incorporation of a new company, enlargement of an existing company, extending the production of a company by adding new products, fundamentally altering the production of a company as well as the acquisition of fixed assets of an inactive company or a company that may become inactive without the acquisition;

– the financing of research, development and innovation projects;

– the creation of new work places and/or the professional training of existing employees; and

– initiation of projects related to the harnessing of green energy, environmental protection and lasting development.

Moreover, the investments must contribute to the accomplishment of several objectives including: regional development and cohesion, environment protection and recovery, increase of energy efficiency and the production of green energy, employment and training of the available work force, as well as improving the process of research, development and innovation.

An “investor” is any legal person who makes an investment in Romania and fulfils the conditions required to receive incentives. Legal persons that owe outstanding debts to the state budget, have requested the payment of the due amounts for external or internal credits guaranteed by the state to the Ministry of Economy and Finance, received loans guaranteed by the state, have entered insolvency procedures or wind-up procedures, or are the subject of a decision for the recovery of a state aid, shall not receive incentives from the state authorities.

In accordance with EU legislation, for any state aid granted through an incentives scheme notification to the European Commission shall not be mandatory as long as the scheme’s provisions are observed.
Incentives schemes available in Romania

To benefit from incentives, investments must be in one of the following fields of activity:

– agro-industrial processing activities;
– high-level manufacturing industry;
– production and supply of electrical and thermo energy or production of equipment for the increase in the efficiency of energy and the level of usage of green energy resources;
– protection and improvement of the environment;
– water distribution, sanitation and waste management;
– information technology and communication;
– research, development (including new products) and innovation activities; and
– employment services.

With respect to the incentives which may be granted by the state authorities, investors may receive financial contributions for the acquisition of tangible and intangible assets, financial contributions from the state budget for newly created work places, or interest facilities for obtaining credit. What follows are some of the schemes available.

<table>
<thead>
<tr>
<th>Year</th>
<th>Total (EUR)</th>
<th>From European regional development fund (ERDF) (EUR)</th>
<th>From state budget (EUR)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011</td>
<td>165.71 million</td>
<td>133.06 million</td>
<td>32.65 million</td>
</tr>
<tr>
<td>2012</td>
<td>55.23 million</td>
<td>44.35 million</td>
<td>10.88 million</td>
</tr>
<tr>
<td>2013</td>
<td>55.23 million</td>
<td>44.35 million</td>
<td>10.88 million</td>
</tr>
</tbody>
</table>

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Incentives scheme ensuring sustainable economic development

This scheme’s objective is to improve regional development by stimulating investment and creating new jobs. Initial investments creating the following number of jobs will be eligible for incentives:

<table>
<thead>
<tr>
<th>Value of initial investment</th>
<th>Minimum number of jobs</th>
</tr>
</thead>
<tbody>
<tr>
<td>between EUR 5 million and 10 million</td>
<td>50 new jobs</td>
</tr>
<tr>
<td>exceeding EUR 10 million</td>
<td>100 new jobs</td>
</tr>
<tr>
<td>exceeding EUR 20 million</td>
<td>200 new jobs</td>
</tr>
<tr>
<td>exceeding EUR 30 million</td>
<td>300 new jobs</td>
</tr>
</tbody>
</table>

Under Romanian legislation, “initial investment” means: any investment made in tangible or intangible assets related to the establishment or extension of a new unit.

Land, the constructions and any equipment are also considered as tangible assets and hence part of the initial investment. Additionally, an acquisition of fixed assets may be considered as initial investment even though it involves acquiring the fixed assets of a company that would have been otherwise closed down and the assets are acquired by an independent investor.

The maximum level of incentives granted to a specific company without any restrictions cannot exceed EUR 28,125,000, for investments carried out and new jobs created as a result of initial investment in any of the other development regions in Romania, except Bucharest-Ilfov region where the maximum level is EUR 22.5 million. Should the above mentioned level be exceeded, such state aid must be notified to the European Commission. The state aid intensity shall be computed depending on the value of the investment. For example, the maximum level of the state aid in the case of a EUR 150 million investment is EUR 46 million.

In each case the beneficiary’s contribution must be at least 50% of the investment. Once the investment is completed, the beneficiary must maintain the initial investment for at least five years (three years in the case of SMEs).

The average annual budget for this scheme is EUR 200 million per year and the duration of the scheme is until 2013.
Incentives scheme for investments made in industrial parks

Industrial parks are well-defined areas where economic, scientific research, industrial production activities and services are carried out. This scheme’s main object is regional state aid granted to investments made in industrial parks. Any company registered under the Romanian Company Law making an investment in an industrial park in Romania may become a beneficiary. However, the present scheme is only applicable to initial investments that are not considered large investments.

The beneficiary must provide its own contribution of at least 25% of the investment, while the intensity of the state aid cannot exceed 50% of the investment (40% for the Bucharest-Ilfov region). The intensity may be raised by 20% for micro-sized and small companies and by 10% for medium-sized companies (except for aid awarded in the transport sector). In any event the investment must be maintained for at least five years (three years in the case of small and medium-sized companies).

The incentives that may be granted under this scheme are:

– building tax exemption;
– land tax exemption;
– exemption from the payment of taxes for changing the destination of the land belonging to industrial parks; and
– exemption from the payment of taxes for the withdrawal of the land belonging to the industrial park from the agricultural circuit.

Building and land tax exemptions are granted by the territorial administrative division where the industrial park is located. The incentives granted under this scheme may not be obtained at the same time as other state or community aid.

The Romanian legislation also uses the concept of scientific and technological parks as areas where education and research activities are performed. For their establishment and operation, scientific and technological parks benefit from the following incentives:

– tax reduction granted by the local authorities for the fixed assets and land given to the park for its use, as well as other incentives, which may be granted according to the law, by the public local authority;
– deferred payment of VAT for materials, equipment and connecting to the public utilities during the investment period until the opening of the park;
– development programs for infrastructure, investment and providing equipment granted by the central and local public administration, private companies and foreign financial assistance; and
– donations, concessions and structural funds for development.

The maximum annual budget for this scheme is RON 268,681,461 and the duration of the scheme is until 2013. The budget is:

<table>
<thead>
<tr>
<th>Year</th>
<th>Total budget (RON)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011</td>
<td>49,675,520.8</td>
</tr>
<tr>
<td>2012</td>
<td>69,269,131.4</td>
</tr>
<tr>
<td>2013</td>
<td>91,029,131.4</td>
</tr>
</tbody>
</table>
**Incentives scheme for supporting regional development by means of investment stimulation**

A large company is defined as any company that does not fulfil the requirements in order to be considered a small or medium-sized company. This scheme provides a specific list of industries for which state aid may be granted, such as the extraction industry, processing industry, construction industry. However, any investor should check carefully, as specific limitations are applicable to each of the above-mentioned industries.

This scheme's objective is to support regional development by encouraging investments in Romania.

Under the present scheme the beneficiaries are large companies which meet the following three conditions:

– the initial investment exceeds EUR 100 million;
– the eligible investment costs are over EUR 50 million; and
– a minimum of 500 newly created jobs as a result of the initial investment.

Any state aid exceeding EUR 30 million for Bucharest Ilfov region (EUR 37.5 million for the other regions) must be notified to the European Commission.

The annual average budget is EUR 115 million and the duration of the scheme is until 2012, with the possibility of extending this period until 2013.

**Incentives scheme harnessing renewable energy resources**

This scheme’s objective is to improve regional development by stimulating investment and harnessing renewable energy resources for the production of electric and thermal energy-renewable energy sources: sun, wind, waves, micro-hydro (systems with installed power <10 MW), biomass, biogas, geothermal etc.

The beneficiaries are large, medium sized and small enterprises.

The beneficiary must provide its own contribution of at least 30% of the investment, while the intensity of the state aid cannot exceed 50% of the investment (40% for the Bucharest-Ilfov region). The intensity may be raised by 20% for small enterprises and by 10% for medium-sized enterprises. The beneficiary’s contribution should under no circumstances be part of a public aid.

The scheme does not apply to projects with a total expenditure exceeding EUR 50 million. The duration of the scheme is until 31 December 2013. The annual budget available to this scheme shall be: €41.4 million for 2011, €35.8 million for 2012, and €31.6 million for 2013.
Incentives scheme for tourism investments

The objective of this scheme is the achievement of a sustainable local and regional development through:

– exploitation of natural resources for tourism purposes;

– diversification of touristic services; and

– creating, modernising or extending the tourism infrastructure, in order to increase the number of tourists and the length of their vacation.

This scheme is exempted from the obligation to notify the European Commission and is valid until 2013.

The beneficiaries may be companies active in the tourism industry, administrative divisions and joint ventures between administrative divisions or between administrative divisions and non-governmental organisations or small and medium sized companies active in this field.

An investment shall be considered eligible for incentives if the following criteria are met:

– it is an initial investment located in an urban area, in the countryside (in such case the investment must be of at least EUR 1.5 million) or in a spa or other tourism resort;

– the eligible investment has an expenditure between EUR 170,000 and EUR 21 million;

– the investment must be completed before 31 July 2015 and must be maintained for a period of five years (three years in the case of small and medium-sized companies); and

– the investment is fully or partially ready for public access for a period of 5 years after its finalisation.

The budget is:

<table>
<thead>
<tr>
<th>Year</th>
<th>Total (EUR)</th>
<th>From European regional development fund (ERDF) (EUR)</th>
<th>From state budget (EUR)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011</td>
<td>84.30 million</td>
<td>76.92 million</td>
<td>7.48 million</td>
</tr>
<tr>
<td>2012</td>
<td>73.02 million</td>
<td>66.60 million</td>
<td>6.42 million</td>
</tr>
<tr>
<td>2013</td>
<td>53.74 million</td>
<td>49.99 million</td>
<td>4.75 million</td>
</tr>
</tbody>
</table>
Slovakia

**General structure of incentives**

In Slovakia the rules for providing state aid to investors are governed by the Act on Investment Aid that entered into force as of 1 January 2008. The Act is a scheme under the European Commission’s General Block Exemption Regulation (the GBER). The Act on Investment Aid provides for the rules applicable to regional aid, which is the usual form of aid granted by the Slovak government to attract foreign investments. Aid that is in line with the rules set out in the Act on Investment Aid does not have to be notified to the Commission.

During the financial crisis the rules were temporarily softened, allowing investors to receive the aid even for smaller projects. In 2011 a more detailed state aid reform took place, coming into force on 1 August 2011.

With the reform, the requirements for investment projects to become eligible for aid were softened on a permanent basis and additional support for SMEs was introduced. The rules governing the aid intensity became more transparent and precise, objectively supporting particular areas with the highest unemployment rate. It remains to be seen how the new rules will be put into practice.

The Act on Investment Aid recognises four categories of investment projects:
- manufacturing;
- technology centres;
- centres of strategic services; and
- tourism.

In general, a project aimed at initial investment or creation of jobs executed in the course of three years by an undertaking having its registered seat in Slovakia is eligible for aid.

The aid may take the following forms:
- cash grant (ex post subsidy for the acquisition of long term tangible or intangible assets);
- income tax relief;
- contribution for newly created jobs; and
- transfer of real estate at a reduced price.

The Ministry of the Economy grants the incentives under the first bullet point above, the Ministry of Finance grants those under the second, the Ministry of Labour those under the third, and the public body which owns or administers the relevant real estate handles those under the fourth. For projects in the tourism sector, the aid is provided by the Ministry of Transport.
Conditions for the granting of aid

The following conditions must be met in each respective sector if the project is to be eligible for aid:

Manufacturing
– setting-up of a new production facility, extending an existing facility or diversifying its output or fundamentally changing the overall production process; and
– making an investment of at least EUR 14 million into the acquisition of long term tangible or intangible assets. This figure is reduced to EUR 7 million if the investment is directed at regions with an unemployment rate higher than the Slovak average, and to EUR 3.5 million if the unemployment rate is at least 50% higher than the national average. If the investment is made by an SME, the minimum investment amounts are reduced to 50% of the above. More than half of the invested amount must come from the investor’s own sources.

Centres for strategic services
– the development of a new centre for strategic services or expansion of an existing centre;
– eligible costs of at least EUR 400,000, of which at least 50% must come from the investor’s own sources; and
– at least 30% of employees having a university degree.

Technology centres
– the development of a new technology centre or the expansion of an existing one;
– eligible costs of at least EUR 500,000 (at least 50% coming from the investor’s own sources); and
– at least 60% of employees having a university degree.

Tourism
– the development of a new complex tourism centre, or the expansion of an existing one;
– the acquisition of new technology equipment designated for the provision of services with a value of at least 40% of the total eligible costs; and
– eligible costs of at least EUR 10 million, reduced to EUR 5 million in regions where the unemployment rate is higher than the Slovak average, and to EUR 3 million in those regions where the rate of unemployment is at least 50% higher than Slovak average.

Obligations of the investor
The investor, as the beneficiary of investment aid, must retain the assets that were acquired through the investment aid throughout the period during which the investment aid is applied, but in any case for at least five fiscal years following completion of the project. This corresponds to the general rule of the GBER that the investment must be maintained in the recipient region for at least five years.

At least 25% of the investor’s eligible costs must be financed from sources other than state aid, e.g. from the investor’s equity or debt.

An applicant may apply for investment aid for a new project only after its current project, which received state aid, has been completed.
Other available support

Industrial parks

In Slovakia, a number of industrial parks have been developed by various municipalities using subsidies from the Slovak Ministry of the Economy. The relevant criteria for receiving the state subsidies are:

- **Manufacturing**: At least one investor must intend to carry out manufacturing business on the site.
- **Industrial**: The applicable land planning resolutions predetermine the site to be an industrial park.
- **Municipality**: The municipality is responsible for at least 15% of the development costs (whether by means of its own funds, debt or co-funding).
- **Consent**: The municipality has secured the consent of the Slovak land fund if its properties are involved.
- **Agreement**: The municipality has an “agreement on future agreement” with the relevant investors outlining their intentions concerning their business in the park.

The state may subsidise up to 85% of the costs for improving the infrastructure of the park and the costs of acquiring the necessary land, provided that the total investment by the state does not exceed 50% of the total investment cost.

This type of support by the state is distinguished from incentives granted to individual investors, as it is the municipality which applies for funding and this may take the investment outside the scrutiny of the EU rules on state aid. It is therefore worth an investor considering whether the project could be structured so as to benefit from the provisions on industrial parks. However, once again, it is crucial for a full analysis of the facts to be undertaken before this is agreed with the state. In particular, where only one investor is planning to invest in the industrial park, there is a serious danger that the subsidies granted could be regarded as state aid to that particular investor. Alternatively, actions by the municipality itself, rather than by the Ministry of the Economy, could put the municipality in the position of being a provider of state aid, when notification, and perhaps clearance, would be required.
Part 5

Focus on incentives III: process for receiving incentives in CEE

Given the different legislative structures in the various CEE countries, the application process for receiving incentives also differs significantly. This can also be a key issue for an investor, as it will want to know what it has to do to actually be able to receive and utilise incentives. Obviously there is a good chance that an investor might be considering a number of different sites in a number of different countries simultaneously, with the initial stages of the various procedures described below being undertaken at the same time. It is therefore especially important to appreciate at what stage in each process steps must be taken in order to qualify for incentives (it may be earlier in one country than in another), and at what point the investor becomes effectively committed to investing in the relevant country.

Investment agreements

As will be seen, in the majority of cases of investment in the five CEE countries, most incentives are granted without the investor and the relevant state body negotiating a detailed investment agreement. Having said that, it may be the case (especially where proposed projects are particularly large) that an investor could find itself negotiating an investment agreement in any of the five countries, although we understand from CzechInvest that it does not envisage that, in practice, investment agreements will ever really be used in the Czech Republic. However, we have set out below the key clauses an investor might expect to see in such an agreement.
**Description of project**

The investment agreement should usually include a detailed description of the project, including, for example:

- the product(s) to be manufactured or the technology to be developed
- the amount, timing and nature of the investment by the investor
- the number and types of jobs to be created each year
- the structure of the project, for example which companies within the investor’s group will be involved and what their roles will be

It is easy for an investor to underestimate the importance of getting the description of the project right, but it really is key. The state will want to ensure that the actual payment of incentives depends on the actual investment made by the investor compared with the investment it commits to make in the investment agreement. If the project description and forecasted investment by the investor prove to be wrong, the investor could face a situation where it has made a huge investment in a new site but cannot get any of the incentives it needs from the state.

**Conditions, targets and the calculation of incentives**

It will not be enough for the investment agreement to set out what incentives the state will grant and when the grant of any incentives is to depend on the investor meeting the investment or other agreed targets (for example, for job creation). The mechanism for calculating whether any targets have been met is likely to be rather complex and will require negotiation.

One typical approach (where the state will agree to grant incentives over a period of time) involves calculations at each stage that incentives are payable. On the relevant date, the level of investment made by the investor in the period up to that date is compared to the level of investment the investor had agreed to make during that period. If the investor has made investment equal to or more than the amount it promised, then the incentives become payable.

Any investor will appreciate that there may be much room for negotiation within such a structure. For example, if the investor has only invested a proportion of what it agreed, will it receive a corresponding proportion of the incentives (this was a very hotly debated topic during the financial crisis)? If the investor fails to meet its target for one particular period but invests much more than it agreed during the next period, is it entitled to receive the incentives it did not get before? How often and when exactly will the calculations be made? When dealing with all these issues, it is a good idea for an investor to seek as much flexibility as possible in how it may meet its targets, but this is unlikely to be a popular approach with the state.

One possible way to deal with these issues, especially if the investor knows it will invest heavily in the project, but perhaps not at the times agreed with the state, is to include a final adjustment mechanism. This will compare the total investments made by the investor and the state with what they each agreed to make at the start of the project and will require the state to pay additional incentives or the investor to pay back extra incentives received, as necessary. An investor may be able to get the state to agree that it can have all of the offered incentives even if it meets less than 100% of its investment targets but should also beware that it could end up being liable to make a large cash payment at a time when cash is at a premium (for example, when production is about to start) if the incentives it is entitled to receive are adjusted downwards.
**Provision of information by the investor**

The state will require the investor to provide regular and detailed information about the project, its proposed investment (based on the project description), the actual investment made and the use of the incentives.

While any investor understandably may not want the administrative burden of preparing “investment plans” and “investment reports” for the state, they should not ignore this issue. As soon as the state’s obligation to give money becomes dependent on the information provided by the investor, the investor should ensure it has a clear obligation defining the information it must provide. Providing the investor fulfils its obligation, this should hopefully preclude any refusal by the state to make a payment on the basis that the investor has not provided enough or the right information.

The parties will also have to agree what information the investor will provide and how often. The state may want quarterly, six-monthly or annual updates and will almost certainly want the timing of information to reflect the timing of incentives being granted. It may be a good idea for the investor to try to agree the timing for the provision of information to the state so that it coincides with the preparation of its own accounts, to ease the administrative burden.

It is also very sensible to determine how any objections of the state to the information provided by the investor will be dealt with. The investor should seek to limit the grounds on which the state can object (for example, because the expenditure incurred (or part of it) does not relate to the project at all or the evidence submitted does not prove that the investor incurred the expenditure) and the time it has to do so, to avoid protracted arguments and delays in receiving incentives.

**Management of ongoing relationship**

Unlike in many transactions, the investor and the state are likely to be working together over a period of years. It is therefore crucial that some thought is given to the way in which future co-operation will work and to the appropriate undertakings given.

Typical undertakings which the investor may want from the state could include a commitment to support the project and procure any necessary assistance from other public bodies, including in relation to the grant of permits and approvals.

The inclusion of such undertakings can help to focus the minds of the parties; however, the investor should be aware that such undertakings may in practice be difficult to enforce or be unenforceable.
Other assistance from the state

If it is anticipated that, as part of the package offered by the state, the state will spend money on improvements to the region which will benefit the project but which do not constitute specific incentives, the investor should require that provisions on these measures are included in the investment agreement, for example in relation to the amount to be spent, the work to be carried out and the timing agreed. Without such provisions the investor may have difficulty requiring the state to fulfil the agreed commitment.

Timing

For the investor, it will almost certainly be crucial that the involvement of the state does not have the effect of hindering progress with the project, especially where the state is involved in the acquisition of the land, preparation of the site etc. We therefore would always recommend that the parties include a detailed timescale in the investment agreement, setting out the deadlines for completion of the key stages of the project. This helps to focus the minds of the parties on the structure of the project, helps to agree an achievable timetable and gives the investor a basis on which to approach the state should the project not proceed as agreed.

Termination

As with any commercial agreement, the transaction may not proceed as anticipated. It is therefore sensible for the parties to determine at the outset the circumstances in which either party will be entitled to terminate the agreement. The investor may want to be able to terminate the agreement, for example, in the event that EU approval is not received or if it does not receive necessary permits or approvals from governmental bodies by the deadlines agreed. It is also likely that the state will want to be able to terminate the agreement if the investor fails to make a specific proportion of the investment it committed to making.

The parties should agree what the exact mechanism for and consequences of termination will be. For example, will there be a remedy period for any breach? If the state terminates because the investor is in default, will the investor be obliged to repay the incentives it has received? Will interest be payable on any repayable sum?
Czech Republic

As was explained in Part 4, if an investor negotiates terms of investment aid with the state that go further than those under the currently available investment incentives schemes, the investment aid will first have to be notified and cleared by the European Commission. For more information, please refer to Part 3 where general rules on the notification and clearance of state aid by the Commission are described. However, the state prefers to stay within the boundaries of the currently available investment incentives schemes, especially since any aid going further than that is likely to be prohibited by the Commission.

In terms of investment incentives in the narrow sense (as was explained in Part 4), in the Czech Republic there is currently one main sector where incentives are granted, namely the manufacturing sector. The process of application for incentives is explained below.

Even though a number of state institutions participate in the process of granting incentives, CzechInvest, the Investment and Business Development Agency, plays the central role in the application process.

CzechInvest’s contact details are as follows:

Štěpánská 15
120 00 Prague 2
Czech Republic

Tel: +420 296 342 500
Fax: +420 296 342 502
E-mail: incentives@czechinvest.org
Website: www.czechinvest.org
Application for incentives

Application and assessment

The process of applying for the incentives begins when the investor (the applicant) submits a completed application for investment incentives to CzechInvest. The applicant, who may be either a Czech or foreign legal entity or an individual, files an application in the form set out by CzechInvest. This is currently in the form of a booklet, and the scope of information required to be stated in the application is provided by Czech law. Investors are particularly required to provide constitutional and incorporation documents, audited financial statements, group structure charts, details of the planned project, etc.

CzechInvest will then prepare an assessment of the application to evaluate whether the investment will be able to meet all the requirements set by the legislation and will then present it to the Ministry of Trade and Industry within a maximum of 30 days of receipt of the application. The Ministry of Trade and Industry then requests approval of the individual incentives from the relevant ministries, for example the Ministry of Finance for tax relief aid and the Ministry of Labour and Social Affairs for any job creation support programme and training grants. Approval from the Ministry of the Environment is also required to determine whether the investment programme complies with Czech environmental regulations and whether it will be environmentally friendly.

Upon the assessment of the application and the prior approval of other ministries, the Ministry of Trade and Industry will then decide on the total amount of investment incentives available for the applicant’s project.

The offer

Upon receiving the comments from the ministries, the Ministry of Trade and Industry will, within two months, provide the applicant (through CzechInvest) with an offer of investment incentives. The offer contains all incentives available for the project and sets out the conditions under which the incentives are granted. It should be noted by any potential investor that one of the conditions will be that the actual recipient of the incentives must be a Czech subsidiary. Again, this may require the investor to set up a new Czech company to receive the incentives, and advice on doing this is available from our Prague office.

Decision

Based on the offer, the applicant or the recipient of the incentives (if the company already exists in the Czech Republic) may submit an application for the grant of incentives to the Ministry of Trade and Industry through CzechInvest within a maximum of three months from the date on which the offer was delivered to the investor.

Ongoing relationship

Having provided the incentives, the Government monitors the investor to ensure that it continues to fulfil the criteria through which it qualified for the incentives. For example, investors which benefit from tax incentives fill in a special tax return and thus specify particular information regarding their continued qualification for the incentives. As with any tax payer, the tax authorities may audit the investor to verify the information provided in the tax return. Similarly, there may be audits to confirm that other grants have been properly granted, for example an audit team may arrive at a factory to check that the jobs for which the investor received an incentive have been created, as specified by the investor.

In the event that the investor fails to meet the ongoing criteria for the incentives, the authorities may not only stop incentives in the future but also, in certain circumstances, demand that the incentives be repaid. So, for example, the investor may have to pay the tax from which it was exempted, together with charges and interest.
Hungary

In Hungary, not only is the system for determining what incentives are available very complicated, so is the process which must be followed to actually receive those incentives. It is, rather unsurprisingly, standard practice for foreign investors to engage specialist advisers to analyse the application process for obtaining incentives for a particular project.

Who to contact

In order to provide information to investors more efficiently and to accelerate the complex administrative procedures, a so-called “one-stop shop” has been created in Hungary. The contact institution is the governmental Hungarian Investment and Trade Agency (the Agency, Nemzeti Külgazdasági Hivatal in Hungarian), which is also responsible for, and can be contacted to provide, information on the Hungarian investment environment. The Agency assists investors through its extensive network of contacts in both the private sector and government offices.

The contact details of the Agency are as follows:

1055 Budapest
Hungary
Honvéd utca 20

Tel: +36 1 872 6520
Fax: +36 1 872 6699

Email: info@hita.hu
Website: www.hita.hu
Application process for a major investment project

The procedure for large investments is different to applications under individual incentive programmes. The two key differences, which can be crucial for an investor, are firstly, that there is no tender process and secondly, that there is no application deadline.

Application and evaluation

The first step to be taken by the investor is to write a letter of intent addressed to the Agency in which the investor describes the planned project, including the overall cost of the investment, the number of newly created jobs, the length of the investment period, the location of the investment, and the industry in which the project operates.

After the Ministry of National Development receives an investor’s letter through the Agency, the investor will be asked to fill out a form about the details of the project. Based on the information the investor provides, the project will be evaluated and a written offer will be made by the Ministry of National Development.

Negotiations and framework contract

The offer may be followed by further negotiations, and finally a framework agreement will be signed between the state and the investor. It may be possible for an investor to agree with the Government that it will receive all of the incentives offered by the Government even if it does not quite meet the conditions set out in the framework agreement.

Before signing the framework agreement the investor can, at any time, withdraw from the planned project. The framework agreement must regulate the schedule for the granting of the incentives and the legal consequences of a delay in the use of incentives. In case of material delay, the state is entitled to withdraw from the agreement.

Grant of incentives

Once the framework agreement has been signed, the Ministry of National Development will need to seek clearance from the European Commission for the incentives to be granted. It may be necessary for the investor to assist with the preparation of the application and it will need to ensure it has provided all the information which the Government must include in the application form.

After signing the framework agreement and providing clearance has been received from the Commission, the investor will receive the incentives.
The application

The relevant guidebook will set out exactly what information the investor must provide in the application. The required information will include the investor’s business plan, which must show that the investor intends to continuously operate and/or maintain the production capacities and new jobs created by the investment for which the incentives are granted for at least five business years.

Other information which the investor is usually expected to provide will include the total value of the investment required by the project, the gross value added by the investment, the jobs created and maintained as a result of the investment and the direct private investment in the business receiving the incentives.

It is very important to make sure that all the required information is included and is correct for a number of reasons. Firstly, there is always a deadline for the submission of applications, and corrections to applications may only ever be made if there is a formal deficiency in the application and within the original deadline specified in the guidebook. Secondly, if all the formal requirements listed in the guidebook are not met, the potential investor’s application may be disqualified without its merits being considered, which would be disastrous especially when a lot of time, effort and money have been spent on the application. Thirdly and finally, the information provided by the investor will relate to the criteria being used by the Government to select successful bidders and will be used as the benchmark against which allocated incentives are measured. It is for these reasons that we would always recommend a foreign investor to seek local legal advice as early in the application process as possible.

As soon as an application has been made, the investor may start the investment; however, it should be noted that the start of the investment will not have any effect on the evaluation of the application or represent any advantage in the evaluation process, and will not guarantee that the incentives applied for will be granted.

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Application process under an individual incentive programme continued

The evaluation
Following receipt of the application, the designated participating organisation responsible for the application programme will verify that the application complies with the criteria, as defined in the terms of the application.

If the application meets the criteria of submission, eligibility and completeness, the participating organisation will perform an evaluation of the submitted project according to a predefined set of evaluation criteria and the assigned scoring system. Based on the score given to the application, the participating organisation will then make a recommendation to the Selection Committee on granting aid. The guidebook will describe the evaluation process and the scoring system in detail.

The aid agreement
The head of the managing authority will decide whether and to whom to grant the incentives, based on the recommendation of the Selection Committee; the decision will be communicated to the investor in a letter of approval or refusal.

If successful, the investor must then sign an aid agreement with the grantor of the incentives for the approved project, setting out the terms and conditions of the incentives and drawn up in accordance with applicable legislation. In exchange for the incentives, the investor must undertake considerable long term obligations towards the state and, if the investor fails to meet any of its key obligations or a part thereof, or a breach of contract occurs for any other reason, the investor will be required to repay the incentives together with the interest charged thereon.

Grant of incentives
As mentioned in Part 4, incentives granted through a tender process are granted under aid schemes which have been pre-cleared by the European Commission. Therefore, once the aid agreement has been signed, there is no need to go through a lengthy process to receive individual clearance from the Commission before the incentives are granted.
An investor who receives incentives in Hungary will be required to comply with the rules on the monitoring of incentives, which comprise the collecting, processing and transfer of information regarding state aid granted, in particular relating to the types, forms and amounts of such aid.

The investor can expect that the state will monitor the implementation and operation of the project for at least five years after the framework contract or aid agreement is signed, and it will be obliged to submit reports on a six-monthly basis on the advancement of the project for which the incentives were granted to the designated participating organisation.

The investor will have to submit the reports in electronic format and, if the framework agreement or aid contract provides, in physical form. It should also be noted by an investor that Hungarian law imposes an obligation to return any incentives received (principal amount plus interest) if those incentives have been granted in accordance with any legal acts inconsistent with the Constitution of the Republic of Hungary or any law or international agreements ratified by the Republic of Hungary.

The investor will also be required to pay interest on those incentives, so it is crucial for an investor to seek legal advice on the validity of any incentives offered before they are accepted.
Poland

The investor application process in Poland depends on:

(i) the body which is granting the incentives;
(ii) the type of incentive requested; and
(iii) whether the incentive is an aid scheme or individual aid.

As an example, below is the application process for the Multi Annual Support Programmes, mentioned in Part 4.

Negotiations with the Ministry of the Economy and PAIIZ

Firstly, the investor applies to PIFIA to commence negotiations of an individually tailored aid package. The negotiations usually take several months and require several rounds to reach an agreement. On the side of the state the Ministry of the Economy leads the negotiations with the support of PIFIA, which plays an intermediary role between the two parties. As the final aid package can include various aid measures, the Ministry also represents the local authorities, other governmental bodies and SEZ's governing body in the negotiations.

Signing a contract

If successful, the investor is invited to sign a contractual agreement with the Ministry and PIFIA. The agreement defines the obligations of the investor and the location and size of the investment. It contains a schedule on the investment process, the number of employees involved and, if applicable, any circumstances in which the investor may be obliged to return the financial support. The agreement between PIFIA, Ministry and the investor is then adopted by the Polish Government and only once this has occurred can the investment begin.

Receiving funds

Once the necessary documentation has been provided to the relevant Ministry (see below), the funds are transferred to the investor. The Ministry is responsible for deciding whether the investor has fulfilled the obligations in any agreement previously concluded between the investor and the Ministry concerning an investment or any other state aid, including any conditions attached to any state aid previously granted.

“The top of the top.”

Chambers Global 2010

www.allenover.com
Since Poland’s accession to the EU, the European Commission has sole competence for clearing any grant of incentives in Poland. However, the President of the Office of Competition and Consumer Protection (the OCCP), which is responsible for monitoring the grant of incentives in Poland, still issues opinions on grants of individual aid to investors before they are sent to Brussels. Such an opinion may be required before an investor can be granted incentives under a particular legislative scheme. A positive opinion of the OCCP opens up the possibility of incentives being granted while a negative appraisal inevitably reduces the chances of an application for incentives being successful.

The general process is as follows:

- a draft of the proposed incentives is notified to the OCCP by the authority proposing to grant such incentives (it will provide detailed information on the investor and on the types, amounts, purposes and effectiveness of incentives to be offered, including all information required by the EU);
- the President of the OCCP will issue an opinion on the compliance of the incentives in question with the common market within 60 days of receiving the application together with the attached information and documents;
- the President of the OCCP will submit an opinion without undue delay to the entity which applied for the opinion and to the authority proposing to grant the incentives;
- the President of the OCCP, through the Permanent Representative of the Republic of Poland at the EU in Brussels, will notify the European Commission of its opinion; and
- the President will receive the decision of the European Commission and will then inform the appropriate entity immediately, providing a copy of the decision at the same time.

The contact details of the OCCP are as follows:

Barbara Mroczek
International Relations and Communication Department
Office of Competition and Consumer Protection
Pl. Powstańców Warszawy 1
00-950 Warsaw
Poland
Tel.: (+48 22) 826 37 59
Fax.: (+48 22) 826 11 86
Email: dzk@uokik.gov.pl

Piotr Pelka
Competition Protection and State Aid
Pl. Powstańców Warszawy 1
00-950 Warsaw
Poland
Tel.: (+48 22) 826 05 13, 556 01 02
Fax: (+48 22) 826 10 32
Email: ddo@uokik.gov.pl
Following the OCCP opinion, the aid package under the Multi Annual Support Programme must be notified to the European Commission for approval. This procedure takes a further four months.

Monitoring of granted incentives

An investor who receives incentives in Poland will be required to comply with the rules on the monitoring of incentives, which includes the collection, processing and transfer of information regarding the state aid granted, in particular about its types, forms and amounts. The authority which monitors incentives is the President of the OCCP.

The investor will be obliged to submit information regarding the granted incentives to the President of the OCCP or to the authority which granted the incentive if so requested, in the scope and the timeframes specified in the request. The timeframe must not be shorter than 30 days. The investor will have to submit periodical reports for the incentives received to the President of the OCCP or to the authority granting the incentives in electronic format on a form taken from the public IT network.

The Ministry will evaluate the performance of the investor’s obligations by comparing its actions with what was agreed at the start of the project. In the case of non-performance of any obligations which were conditions for the grant of the incentives, the incentives granted will have to be repaid with the interest accrued from the date of grant.

An investor should also note that Polish law also imposes an obligation to return any incentives received (principal amount plus interest) if those incentives have been granted in accordance with any legal acts inconsistent with the Constitution of the Republic of Poland, or any law or international agreements ratified by the Republic of Poland. The investor will also be required to pay interest on those incentives so it is crucial for an investor to seek legal advice on the validity of any incentives offered before they are accepted.

Further agreements

An investor who enters into an investment agreement with the relevant Ministry may also have to conclude further agreements related to the investment. Firstly, the total value of the state aid which is provided by different sources and under separate agreements is limited. Secondly, there are only two months in the year when applications can be submitted, January and June, and therefore investors must apply at regular intervals for further aid.
“They did a great job, offering solutions not problems. They’re absolutely excellent at providing all the services that a client could need.”

Chambers Europe 2011
Romania

Before Romania’s accession to the EU, incentives were granted based on laws applicable to a specific industry or specific list of companies. An ambiguous procedure applied to privatisations of former state owned companies. For these companies the incentives were granted following direct negotiation between the state body in charge of privatisation and the interested buyer.

Currently, the procedure for receiving incentives depends mainly on the type of investment requested, and if an investor requests an incentive that falls under a particular scheme, then the granting process shall be governed by the respective scheme. Should the requested state aid be considered as individual aid, then the process takes longer and requires more formalities to be completed.

Initial discussions with CRPCIS

The Romanian Center for Trade and Investment’s (CRPCIS) main objective is to attract and assist interested foreign investors. However, CRPCIS’s role is limited to finding investors, advising them, providing them with all the relevant information and putting them in contact with the competent authorities, which then conduct the relevant negotiations. Moreover, CRPCIS may provide information related to local business opportunities and detailed analyses regarding business opportunities. If the investment involves buying a state owned company, then the authorities in charge are the Authority for State Assets Recovery and the Ministry of the Economy and Finance.

The contact details of CRPCIS are as follows:

17 Apolodor Street
Sector 5 Bucharest
Romania

Tel.: +40 21 318 50 50
Fax: +40 21 311 14 91

Email: office@traderom.ro
Website: www.traderom.ro

www.allenovery.com
Procedures for granting individual incentives

After negotiations with the competent authorities, if individual incentives are granted, then the respective incentives plan elaborated by the competent authority shall be notified to the Romanian Competition Council. Such notice must at least mention the objective of the state aid, the basis of the granting and the total amount of the incentives granted.

Competition Council’s consent

The consent of the Council is the first step in obtaining the incentives. The Council gives only a formal consent related to the conformity with, and correctness and fulfilment of, EU legislation. The Council must issue the consent within 30 days of receiving notification. If the consent does not contain any changes to the initial notification, then the notification shall be sent to the Commission after it is communicated to the applicant.

If the Council, through the consent transmitted to the applicant, proposes changes to the initial form and content of the notification, then the applicant must respond within 10 days. If the applicant approves the changes proposed by the Council, it shall send to the Council a new notification amended accordingly. Subsequently, the Council shall send the new notification to the Commission in order to obtain its approval. If the applicant does not agree with the Council’s changes, it must request that Council send the notification to the Commission in its original form within 10 days of receiving the proposed changes. However, the Council will not send the notification to the Commission without the prior request of the applicant.

If the Commission does not approve the state aid or partially approves it, the beneficiary must repay the amount provided by the decision of the Commission.
**Procedures under the incentives schemes**

Under EU regulations, each incentives scheme for which notification to the Commission is not mandatory must mention the applicable procedure for obtaining the incentives. However, the procedure is generally similar for all the available schemes.

For each of the eight development regions, special regional development agencies were created in order to assist in the better application of the incentives schemes.

In order to obtain the incentives, an application must be submitted to the regional development agency for the region where the investment is to be located. The incentives may be granted only if the application was submitted before the works requested by the investment have started.

The agency shall perform administrative verifications with respect to the application after it is submitted. The details in the application, together with technical and financial figures, are the main criteria used for granting the incentives. Each available scheme has its own guidelines established through the “applicant guideline” available at the relevant regional development agency.

**Monitoring of granted incentives**

Any beneficiary of state aid must comply with the rules related to monitoring the incentives, which includes the collection, processing and transfer of information regarding the state aid granted, in particular information on its type, forms and amounts.

The authorities entitled to monitor the incentives are the provider of the incentives and the Council. The beneficiary must comply strictly with the terms and conditions of the incentives received.

State aid for which the Council granted its consent, state aid excepted from the notification request, state aid granted for removing damages resulting from natural disasters, and damages or social state aid are all subject to the above monitoring rules.

It should also be noted that apart from state aid to be repaid based on the decision of the Commission as mentioned above, any state aid received based on a law which does not observe the Romanian Constitution or any binding treaty to which Romania is a party also must be repaid. Moreover, the investor will be required to pay interest on those incentives, so it is crucial for an investor to seek legal advice on the validity of any incentives offered before they are accepted.
Slovakia

The Act on Investment Aid lays down a fairly clear procedure on how the investor should apply for aid as well as how each project is evaluated.

Initial discussions with SARIO

The Slovak Investment and Trade Development Agency (SARIO) is the first point of contact for investors. Its task is to provide investors with initial information and assistance with their investment. In the currently applicable procedure for awarding incentives under the Act on Investment Aid, however, SARIO’s role is limited to acting as an expert adviser and consultant to the investor. This includes helping with the search for the best locations, real estate and subcontractors, assistance with the application for incentives and helping with the creation of new job opportunities and employee retraining programmes. SARIO offers a comprehensive database of land and property available to investors, a comprehensive database of investment opportunities and detailed regional analyses and studies. In practice, this is usually a supplement to the investigations that the investor will make on its own account with private sector advisers.

SARIO’s contact details are as follows:

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<thead>
<tr>
<th>Martinčekova 17</th>
<th>Tel.: +421 2 58 260 100</th>
<th>Email: <a href="mailto:sario@sario.sk">sario@sario.sk</a></th>
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Application and assessment

During the process of application for investment aid under the Act on Investment Aid, the Ministry of Economy (MoE) is the main point of contact for the investor (the applicant). The applicant must file the investment plan (the plan) with the MoE. The plan contains detailed information on the project as well as the proposed form and amount of the investment aid. The MoE will procure an expert opinion on the plan (produced by SARIO). If the opinion is positive, the MoE will preliminarily confirm to the applicant that the investment project has the potential to be eligible for the aid and will produce a proposal for the grant of investment aid (the proposal). The proposal will be submitted to the entities that should eventually grant the aid (described in Part 4). They will then provide the MoE with their opinion on the award of the aid.
The offer

If all opinions are positive, the MoE will provide the investor with an offer for investment aid, which will contain the forms of aid to be granted together with their amounts, as well as conditions of granting the aid.

The final application

After receiving the offer, the applicant may apply to the MoE for the award of investment aid in formal administrative proceedings.

Approval by the Government

If the applicant meets the criteria for the award of investment aid, the MoE will submit the proposal for the award of investment aid to the Slovak Government. The Government will take into account, in particular, the significance of the investment for the national economy and the impact of the aid on competition in the relevant market. If the Government approves the aid, the MoE will adopt a resolution on the approval of investment aid for the applicant (the resolution). The resolution is issued in formal administrative proceedings and provides for detailed conditions under which the aid is provided.

If the investment aid is subject to prior notification to the European Commission pursuant to Article 6 of the General Block Exemption Regulation, the MoE will notify the investment aid to the European Commission and will only adopt the resolution on approval if the Commission decides that the aid is compatible with the common market.

If the investment aid is to be granted in a form other than tax relief, the investor must enter into a contract with the entity granting the aid (for more details on the forms of investment aid and the entities granting aid see Part 4).

Ongoing relationship

The entities granting the aid will continue to monitor the use of the investment aid by the investor as well as whether the investor continues to meet the criteria for granting investment aid and its obligations under the Act on Investment Aid. If the monitoring shows that the investor has failed to meet the criteria or perform its obligations, the aid already received would have to be repaid.
Part 6
Focus on real estate issues

A further key issue for any FDI investor will be how it actually gets ownership of the investment site. Although the purpose of this brochure is not to go into a detailed explanation of all general real estate issues (separate publications are available on these topics from the various Allen & Overy offices – please contact us for copies), we will look at some specific issues which may arise for large scale investors in each jurisdiction. First though, there are a few general issues which an investor in any country should consider:

Legal due diligence

When considering potential investment sites, based on the key factors for the particular type of project discussed in Part 2, we would always recommend that the investor, as a potential purchaser of real estate with a considerable value, carries out quite extensive due diligence on the proposed site. This may include (depending on the type of land and the jurisdiction) an examination of:

- an extract from the relevant land register showing ownership of the land;
- any possible leases which are not registered in the land register;
- claims of former owners, litigation and administrative proceedings concerning the property;
- claims for easements (perhaps created by prescription) and unregistered mortgages;
- preliminary injunctions and pending execution;
- bankruptcy proceedings;
- appropriate zoning and building permits or occupancy certificates;
- the designation of the land for a specific purpose (for example agriculture) as this may need to be changed (which can take time); and
- property, liability and other relevant insurance policies.

Of course, legal due diligence is not the only type of investigation that may be necessary in relation to the land. For example, an investor may want to consider having an environmental audit of the site, especially where there could be ongoing liability for environmental damage caused by previous owners.
Consider who owns the land

Imagine an investor which finds the perfect investment site and sets about purchasing the land. After quite some time, it discovers that a piece of land right in the centre of the project site belongs to a private owner who is unwilling to sell, making it impossible to start construction of the necessary buildings according to its schedule. It is because of this type of scenario that an investor should consider the fact that, while for every other reason a site may be perfect, it could become a nightmare if owned by 200 (or 10,000) different private owners, each of whom has to be approached and negotiated with.

Certificates, approvals and permits

Whenever construction and use of land are intended, there will be a number of certificates, permits and approvals which the investor will need to get. Failure to do so can lead to very large fines or worse, for example the refusal of permission to occupy or use a building which has been constructed, and appropriate local legal advice should always be sought. Some examples of the types of permits which might be necessary are as follows:

Zoning permit – this states that the type of building envisaged may be built on the site with generally defined parameters.

Building/construction permit – this allows the investor to construct the specific building, road, conduit etc. as set out in the detailed plans submitted to the relevant authority. There may be conditions, for example planting trees to replace any cut down for the construction. An investor must beware of any changes to the design of the construction after the permit has been issued as an amended permit may be necessary.

Occupancy/use certificate – this sets out the purposes for which the building may be used and a building may not be used without the certificate or for any purpose not included in it. It is therefore key to ensure that the permit applied for covers all the potential uses to which the buildings may be put.

Approval of environmental agency – this may be needed, for example, if the construction site is near a water source and the construction would have to comply with any rules set down by the environmental agency.
Czech Republic

Generally in the Czech Republic, the real estate issues which an investor must consider are the same as those for other purchasers of land. However, one aspect of the purchase of land which may differ for an investor is the potential to acquire land at a discount.

**Acquisition of land at a discount**

As well as the centralised, legislation-based system of incentives described in Part 4, an investor may also be able to take advantage of local benefits which may be provided by municipalities seeking, for example, to increase employment in their region. This will often take the form of the sale of land at an undervalue to an investor. The municipality will typically require a number of criteria to be satisfied by the investor to ensure, for example, that the investor does not acquire the land for speculative purposes, does in fact build the planned factory, continues to use the land for the planned purpose for a fixed number of years and invests in certain infrastructure on the land.

These requirements will typically be tested at various intervals after the sale (for example after two and four years), with the municipality having the authority to reclaim the land from the investor if it is not meeting the criteria.

As they are not centrally regulated, these sales at an undervalue, can apply differently in different areas, and there is no single framework of requirements that investors should fulfil, nor is there a fixed level of discount or fixed conditions on sales. However, it is important to note that, while these sales at an undervalue fall outside the incentives system from a legislative point of view, the benefit to the investor must be taken into account when considering the total incentives which that particular investor has received for the purpose of the EU restrictions on state aid. Typically, the value ascribed to a sale will be the difference between the market value of the land involved and the actual purchase price paid by the investor.

**Help acquiring land**

In order to sell large areas of land to investors, municipalities may need to purchase the land from private individuals. The municipalities do not do this under any special statutory powers. The Government does have the power to order the compulsory purchase of land from individuals; however, this power does not come from any legislation related to incentives but is a power of general public interest. To date, the Government’s policy has been that this power is not appropriate for use in acquiring land for the purpose of incentives.

However, municipalities have in the past negotiated with private individuals to buy land in situations where the potential sale to an investor as part of an incentives scheme is already in place. In this case, the municipality is effectively acting to buy the land on behalf of the investor, although legally this may not be the case.
As a general rule, foreign nationals or legal entities may not acquire the proprietary rights to any agricultural land or protected natural areas. Except for cases when they are held by inheritance, which is, of course, very unlikely for an FDI investor. The property rights to properties that do not qualify as agricultural land may be acquired by foreign individuals or legal entities if such acquisitions are authorised by the head of the Budapest or county government administrative office (Kormányhivatal in Hungarian) with jurisdiction over the locality of the properties. Citizens of the EU and legal entities registered in EEA countries, with which Hungary has international treaties in this regard, do not need such authorisation. The acquisition of property by foreign natural persons establishing themselves as independent entrepreneurs in Hungary must also be authorised if such properties are directly required for the performance of the economic activities they are establishing.

As for the Czech Republic, the main issues facing an FDI investor when seeking to acquire real estate in Hungary are the same as those for any other purchaser of land. However, any potential investor should be aware that there are some general restrictions on foreign entities purchasing land which may affect the choice of site or require the setting up of a Hungarian company.

As for the Czech Republic, it may be possible for an investor to negotiate a preferential price for land owned by the Hungarian Government or by a local municipality, and any reduction in the price of the land below market value could well constitute state aid and so must be taken into account when considering the total incentives that the investor has received for the purpose of the EU restrictions on the intensity of aid discussed in Part 3.

Where an investor is investing in Hungary, it can expect that the Government will assist it to try to simplify the acquisition process for the investment site. However, it should also be noted that, while the Government does have the power to order the compulsory purchase of land from individuals, this power is only used in very limited circumstances. In case of compulsory purchase usually the Government acquires the ownership of the land, however in certain cases (e.g. in relation to energy or telecommunication investments) it is possible for investors to acquire the ownership of real properties directly through compulsory sale and purchase.
Poland

Title to real estate

Under Polish law there is generally little difference between public and private ownership of real estate. However, where the acquisition of state-owned land is being considered, there are special regimes regarding the transfer of title to the land set out in the Polish Real Estate Law. In such cases, a tender procedure is usually undertaken, and it is only in exceptional cases that state-owned land will be sold on the open market. This is obviously a key distinction for an FDI investor, as a tender offer process may provide the potential investor with an opportunity to present terms to the seller which reflect the value of its overall investment, rather than merely negotiating on price alone.

Real estate located in an SEZ is generally state-owned, with the exception of cases where the land is owned by a managing entity, which is a special company set up for the purpose of managing the SEZ (in which the state owns a majority of the votes at shareholder meetings and is entitled to appoint and dismiss a majority of the members of the board). However, a private owner may agree to its land comprising part of an SEZ so that it is subject to the rules of the SEZ. This may be a key issue for an investor and, when considering land within an SEZ, it is important that at the earliest possible stage it is established whether the land is privately owned or state-owned, because if the land is privately owned the tender process described above will not be available.

Apart from the ownership title, the real estate may be the subject of a perpetual usufruct, which is a legal concept similar to a leasehold agreement and is specific to Polish law. A perpetual usufruct refers only to property which is owned by the state.

Benefit of acquiring land from the state

The investor will need to negotiate a land purchase agreement or a preliminary land purchase agreement with the owner of the real estate in question, whether it is the state or a private individual. However, one benefit of buying state-owned land is the removal of the risk of re-characterisation or termination of the land purchase agreement by a fickle private seller. Another benefit is that in most cases the price of state-owned real estate sold for investment purposes will be preferential when compared with equivalent market prices. This applies to land located both within and outside an SEZ. However, it should always be noted that the general rule is that the price of the land is established by the owner, and this determination is not dependent on the land being either publicly or privately owned.

Help acquiring land

If the project includes a significant investment, in our opinion it may be possible to expropriate the land from its owner under additional proceedings which override the owner's refusal. The local government authority (Starosta) may be entitled to expropriate the land from the owner if the expropriation is in the public interest and adequate compensation is provided and reflects the market price of the real estate.
Romania

Ownership principles

Under Romanian law, foreign nationals and stateless persons are allowed to acquire land in Romania in accordance with the conditions set forth under the treaty regulating Romania’s accession to the European Union or pursuant to other international treaties to which Romania is a party, based on reciprocity and in compliance with the conditions provided under organic law(s), as well as through legal inheritance.

However, due to difficulties in applying the new regulations, it is preferable that foreign nationals establish Romanian companies for acquiring land.

Publicity requirements; evidence of ownership

Title over real property is deemed to be transferred between the parties upon the execution of the transfer agreement or at a later stage agreed by the parties. However, the ownership of the acquirer becomes enforceable against third parties, meaning that the acquirer can use its title to prove its ownership, only if it is duly registered in the relevant public land registry. The enforcement of real estate property rights against third parties is achieved through cadastral surveys and public notices issued by immovable property offices (Land Registry Offices).

The Land Registry Offices issue excerpts evidencing the registered owner of the immovable property and any encumbrances registered over the immovable property.
Acquiring land from the state; concession of state owned land

Under Romanian law, there are two types of state owned properties: public property of the state and private property of the state. It is noteworthy that while there is no significant difference between the private property of the state and general private property, public property of the state has a separate regime. Thus, land representing public property cannot be sold to third parties, and can be granted in concession only for erecting constructions of public use and/or in the public interest.

The land representing private property of the local authorities may be sold or granted in concession by the relevant local authority only based on decisions of the relevant county council or local council and only following a public tender organised for this purpose. The law provides very limited exceptions to this rule (e.g. if a local authority decides to sell land, the owner of a construction erected on that land will have a pre-emption right). It is worth noting that the concession agreements may be concluded for a maximum period of 49 years, with the possibility of extending by at most half of the initial duration.

Expropriation

Romanian legislation provides for an expropriation regime for reasons of public interest. The public interest may be declared for works of national or local interest. Such works are expressly provided for in the law and relate, amongst others, to: geological prospects; the extraction and processing of minerals; electricity production; transport networks; telecommunications; gas, heat, water and sewerage networks; infrastructure for environmental protection; and dams. The Government may declare works of national interest, while the local authorities may declare work of local interest. In addition, in cases of expropriation which are not listed in the law regarding expropriation, a separate law is required to establish the public interest of specific works. It seems likely that the authorities would not be able to expropriate land in order to sell it to an investor, even a strategic one, as it would be very difficult to prove the public interest of such a transaction, irrespective of the activity to be performed by the investor. On the other hand, the expropriation of land to create industrial parks is, for example, possible, but only subject to the issuance of a special law establishing the public interest of such industrial park.

Given that, as a general rule, the sale or concession of land must be made through public tenders, such transactions are usually concluded at a fair market price. However, the authorities may decide on a case-by-case basis to sell or grant concessions over land at an undervalued price, as a form of state aid, though there is no express law in this respect.
Help acquiring land

The Slovak Government has recognised that, especially where the investment site is not owned by the state or the relevant municipality, actually acquiring land can be logistically difficult and very time-consuming for the investor. The municipality where the site is located may, therefore, agree to set up a special purpose vehicle (SPV) funded by the state to acquire ownership of all the land. The SPV will then be sold to the investor for the price of the land. This can save the investor from negotiating many land purchase agreements and, therefore, from expending a huge amount of time and legal costs. Remember, though, that if the municipality does agree to purchase the land, the investor and the municipality should include provisions about this and agree a strict timeframe for this to be completed in the investment agreement; otherwise, the project may be seriously delayed, with construction unable to start and without the investor really having any legal basis to speed up the process.

Further benefits for large investment projects

If the project proposed by the investor is granted the status of a “significant investment” by the Ministry of the Economy, there will be three further benefits the investor can take advantage of when acquiring the land on the investment site, all discussed below: Large investment status may be granted (following an application by the investor) where:

- the construction costs needed for the production project are not less than approximately EUR 33 million, or not less than approximately EUR 16.5 million if the investment is to be made in a region where the unemployment rate exceeds 15%;
- the contemplated production volumes and the impact on employment are regarded as material to the national economy;
- the beneficiary of the grant is a legal person incorporated in Slovakia; and
- the Slovak Government has decided that the investment is in the public interest.
The three benefits are as follows:

**Simplified acquisition procedure of state-owned land**

When working on a project with large investment status, the municipality is entitled to follow a simplified acquisition procedure if the state or the Slovak Land Fund is the owner of the site. Obviously, this assists in transferring the investment site to the investor more quickly.

**Expropriation**

As mentioned in the introduction to this Part, the worst possible scenario for an investor would be to own virtually the entire investment site only to find that one or more private owners refuse to sell. How can this be dealt with?

If the project has large investment status, the municipality may be entitled to expropriate the land from that owner under proceedings before the Building Office. Beware also, that any of the decisions of the Building Office may be appealed and/or judicially reviewed, potentially creating huge delays and legal costs.

Also, the Building Office may fully or partially revoke its expropriation decision if the expropriated land is not used for the purpose for which it was expropriated within the time limit provided in the expropriation decision (this time limit may be up to two years).

**Restriction of other rights**

As in many jurisdictions, there is a possibility in Slovakia that a third party of whom the purchaser was not even aware may claim that it owns the title to land purchased from the apparent owner. If this occurs, there can be a number of adverse consequences for the purchaser, including a successful claim by the third party that ownership of the land never validly transferred to the purchaser.

The advantage of having large investment status is that no third party can be authorised to claim title to the land forming part of the site of the large investment. However, it must be recognised that a third party’s right to receive damages is not affected and, in such circumstances, the investor should contract with the transferor of the land for specific indemnities or other suitable risk allocation provisions to avoid or reduce the investor’s exposure to liability.
Other issues

There are many issues that a purchaser of real estate in Slovakia must always consider, for example ensuring that the description of the land in the purchase agreement complies with the law, translating the agreement into Slovak and arranging for the legalisation of the signature of the seller, and these are dealt with in a separate publication entitled “Real Issues in Real Estate”, which is available from our Bratislava office. However, one issue to note is that where any parts of the land required by the investor are state- or municipality-owned, it may be possible for an investor to agree to purchase that land at a reduced price. Again, it must be remembered that this could constitute state aid.

Conclusion

In conclusion, it can be seen that the CEE countries covered by this publication have spent a great deal of time and effort developing legislation, rules, agencies and procedures designed to attract foreign investment and that these efforts have been highly successful and rewarded by a huge influx of inward investment.

The governments of each of these countries have above and beyond their efforts to close the “chapters” allowing them to progress to EU accession, taken great strides in trying to create an environment which can stimulate investment and sustain it in the long term. These have included not only macroeconomic policies such as combating inflation, aiming to join the eurozone, and setting competitive but sustainable tax rates, but also getting down to the fundamentals of creating a better and more efficient legal system for setting up companies, acquiring real estate, applying for permits and liberalising the labour market - all this at the same time as privatising the entire financial, utilities and telecommunications sectors, and building roads and airports. The effort required has been staggering.

On the other hand, in devising the relevant rules and procedures, each of the governments has had to take into account differing circumstances and, of course, changes in policy, and will need to be revised frequently.

Each of the countries therefore, in making itself attractive to investors and finding distinct ways of doing so, has inevitably developed widely differing laws and procedures. Common threads are nonetheless evident, and the overarching framework of EU legislation allows some examination of the relevant issues to take place under a common system. However, the procedures involved in physically deciding upon an investment location and agreeing all the necessary elements to make your project a reality are complex, and different, in each of the countries. Planning and seeking advice are essential.

As we said at the beginning, this publication was never going to be an encyclopaedia of all that you need to know about FDI and the related rules. That would be impossible. However, we hope that it has served as a useful introduction to the issues to consider when contemplating your investment. We wish you the best of luck on your project.
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ICS110_CDD-245_04.11.11

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