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Slovak FDI regime: what does it mean for your M&A and banking deals?

2023

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The Slovak FDI regime applies from 1 March 2023. What are the first impressions?

The FDI Act dramatically expands the powers of certain Slovak authorities to scrutinise investments from the perspective of national security and public policy. As a result of this scrutiny, the authorities may either (i) clear (approve); (ii) clear with mitigation measures (such as divestments); or (iii) prohibit the scrutinised transactions. The FDI Act will apply to certain investments made by non-EU investors completed after 1 March 2023.

At long last, Slovakia finally adopted a comprehensive FDI scrutiny. This means yet another regulatory approval for a number of transactions. Which transactions are on the hook? What can be expected? And what are the impressions after the first few months of application? Please read on to find out more.

Which transactions are within scope?

The FDI Act brings a revolution to the Slovak transaction market. The far-reaching scope of the new regime and the resulting administrative burden and transaction risk will inevitably have a significant impact on acquirers looking to invest in Slovakia. Therefore, the key question is – which investors and transactions are within the scope of the FDI Act?

The FDI Act applies to "foreign investors" and "foreign investments".

Who is a foreign investor?

In general, any person (legal or natural) outside the EU will be considered a foreign investor – ie persons that are not EU citizens or do not have their registered seat or place of business in the EU, including:

a non-EU individual or entity (ie non-EU citizenship or seat) that has invested or is intending to invest in a Slovak target;

an EU individual: (a) with financing for the investment being provided from a third country/entity with a third-country stake; or (b) who acts in concert with a non-EU individual or entity or a third country;

an EU entity with a non-EU individual or a third country: (a) as the ultimate beneficiary owner; (b) as the controlling person; (c) as a financing party; or (d) acting in concert together; or

a trust or its trustee (depending whether the trust has legal capacity) if an investment is made on behalf of a trust with a non-EU element (ie either the beneficiary, founder or trustee is any of the persons listed above).

The FDI Act links the definition of a foreign investor to the EU. This means that investors from the U.S., Japan or the UK also qualify as foreign investors.

What is a foreign investment?

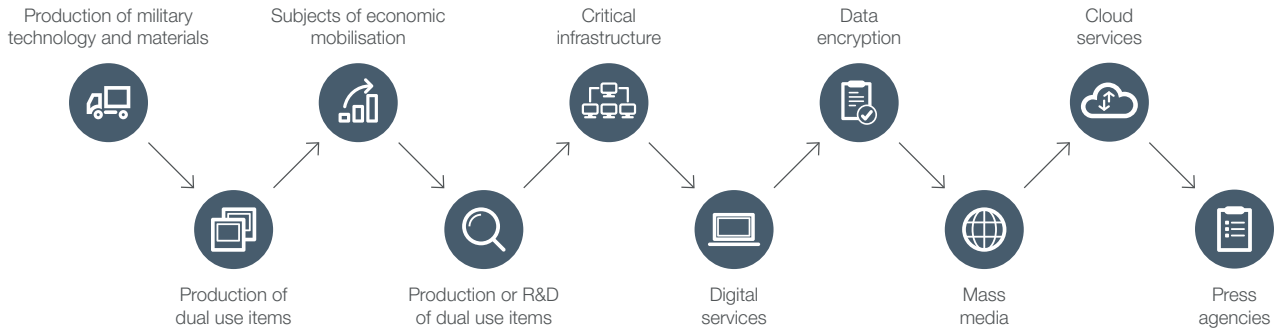
The FDI Act distinguishes two types of foreign investments with different rules on notification requirements, acquisition thresholds, scrutiny procedures and possible penalties:

Critical foreign investment

Non-critical foreign investment

1. What is the difference between a critical and non-critical foreign investment?

A **critical foreign investment** is an investment of a foreign investor in relation to a Slovak target operating in at least one of the following sectors:



A **non-critical foreign investment** is any other investment of a foreign investor in relation to a Slovak target that does not operate its business in the mentioned sectors (eg acquisition of a shopping or logistics centre).

2. What investments are covered?

Only an investment meeting the following thresholds is within the scope of FDI scrutiny:

Critical foreign investment

– acquisition of a business or part of a business (asset deal);
– acquisition of a shareholding (share deal) of at least 10%;
– increase of a shareholding to 20%, 33% or 50%;
– acquisition of control (eg by controlling the management body); or
– acquisition of substantial assets, which are key for carrying out the activities of critical infrastructure.

Non-critical foreign investment

– acquisition of a business or part of a business (asset deal);
– acquisition of a shareholding (share deal) of at least 25%;
– increase of a shareholding to 50%; or
– acquisition of control (eg by controlling the management body).

3. What investments are not caught?

The following transactions do not qualify as foreign investments:

intragroup transfers (ie when no change of ultimate ownership structure takes place);

the creation of a pledge in relation to the Slovak target, but only if the pledge does not grant any rights over the business decisions of the Slovak target; or

the purchase of stock, services or products within the ordinary course of business.

4. What investments are recommended to be voluntarily notified?

The Ministry has published its first guidelines laying down scenarios in which it is advisable to make a voluntary FDI filing. The Ministry recommends filing a voluntary notification if:

the Slovak target is a supplier of goods/services to the state or to operators of critical infrastructure or to other key service providers;

the Slovak target supports R&D or innovation, especially through contracts with universities or the Slovak Academy of Sciences (mainly in the energy, semiconductor, AI and biotechnology sectors);

the Slovak target participates in projects of EU interest listed in the attachment to the EU FDI Regulation (2019/452);

any of the previous scenarios (including indirect acquisition) is already being FDI screened by another country; or

it is not clear whether a mandatory filing is required.

On top of the above, the Ministry noted that a foreign investor may carry out a voluntary FDI filing in order to confirm its credibility.

5. Critical or non-critical – why it matters

Critical and non-critical foreign investments have different rules on notification requirements, scrutiny procedures and penalties.

Critical foreign investment	**Non-critical foreign investment**
Mandatory filing	Non-mandatory filing
Ex ante screening	Ex post screening on the basis of a call-in right
Stand-still obligation	No stand-still obligation
Fine of up to 2% of the investor's group turnover for failing to notify the transaction	No fine for not notifying the transaction (but risk of call-in right)

Call-in right

The authorities can call in (even) completed transactions (if completed after 1 March 2023)

– for non-critical foreign investments, the call-in right is time-limited to **two years** after completion of the transaction; and

– for critical foreign investments, the call-in right is not time-limited.

To avoid a call-in right for non-critical foreign investments, we recommend a risk assessment of the investor and the transaction before its implementation. Common risk factors may be: (i) the presence of a non-EU state in the transaction (eg shareholder); (ii) difficulties with getting clearance in another jurisdiction EU member state; or (iii) indications that the investor is involved in any illegal activity.

If risks are identified, voluntarily notification is advisable prior to implementing the transaction.

Scrutiny procedure and timeline

The Ministry of Economy of the Slovak Republic is the key authority with respect to the FDI Act. The Ministry has broad investigative powers, such as requiring foreign investors to provide cooperation and necessary information and even conducting dawn raids similar to those well-known in the antitrust world.

As for non-critical foreign investments, the screening procedure has two phases. Within the **first phase** after filing the FDI notification, the Ministry will open consultations with other authorities. If it does not identify any risks within 45 days of the FDI filing, the transaction is deemed cleared. If it does, it opens the **second phase**. **Phase two means a full FDI screening** of the transaction.

Critical foreign investments jump directly into the full screening phase.

Within the second phase, the Ministry initiates broader consultations with other ministries, the police, secret services and also with other EU member states, and may either:

Clear (approve) the transaction

Clear (approve) the transaction with mitigation measures (such as divestment)

Propose prohibition of the transaction to the Slovak Government

While phase one should not take more than 45 days, phase two will probably drag on for several months.

Even if the Ministry clears the transaction, there is still some additional paperwork for the foreign investor to do:

– **Registration with the Slovak Register of Public Sector Partners** – the foreign investor has to register itself with the Slovak Register of Public Sector Partners. It must disclose its ownership structure and management, and identify its ultimate beneficiary owners.

– **File a report on completing the transaction with the Ministry** – within 60 days after completing the investment, the foreign investor is required to file a specific report on completing the transaction with the Ministry.

Scrutiny risk of intra-EU transfers concerning critical infrastructure

On top of the FDI procedure regarding foreign investors, the FDI Act also tweaks the existing temporary FDI screening of transactions concerning critical infrastructure (relevant only for the energy and industry sectors). Under the amended rules, the Ministry might also screen transactions, in which an intra-EU investor wishes to acquire at least a 10% stake in a Slovak company owning an element of critical infrastructure within the sectors of energy (mining, electro energy, oil and gas) and industry (pharma, metallurgical and chemical).

In practice, the Slovak target company will make a prior notification to the Ministry of the intent to carry out the transaction and the Ministry will decide whether to screen or not.

Implications for M&A and banking deals

Like the merger clearance proceedings, FDI rules will have an indisputable impact on M&A and banking deals. Generally, the FDI rules will result in further advisory costs and delays to the transaction. More specifically, FDI may have the following implications:

- **FDI analysis** – investors need to check whether their transaction is caught by the rules in order to eliminate the risk of any fines or scrutiny.
- **Conditions precedent** – especially for critical foreign investments in which a stand-still obligation applies, transaction documents will need to include conditions precedent for obtaining the FDI approval.
- **Security** – when securing financing with a pledge, the banks should make sure that the pledge agreements do not give them any specific rights in business decisions (eg veto rights), otherwise establishing or registering such pledge might be considered a foreign investment.
- **Modification/prohibition of the transaction** – think of the possibility that the FDI rules may result in significantly altering the transaction (eg allowing the purchase of a smaller portion of shares or a divestment obligation) or even prohibiting it completely. This might affect break fees and other fees under the transaction documents.

FDI on the rise

FDI is a clear trend within the EU market. As far asthe CEE is concerned, the Czech Republic introduced its FDI screening mechanism in 2021, Hungary in 2018, and Poland in 2015 (and in various forms afterwards) with Slovakia following with the FDI Act in 2022.

FDI has been showing its teeth in the EU, especially towards the end of 2022. In November 2022, the German Government blocked prospective Chinese investment in two domestic semiconductor producers after the moves raised concerns over national security and the flow of sensitive technological know-how to Beijing.[1]

Similarly, in November 2022 the UK Government ordered Nexperia (reportedly backed by the Chinese Communist Party) to divest its 86% stake in Newport Wafer Fab, Britain's largest chip plant, over national security concerns.[2]

Consequently, investors contemplating investment in the EU market must pay closer attention to the FDI rules. Otherwise, they risk incurring monetary fines, modifications to the transaction or even its prohibition or unwinding.

Our first impressions

A&O Bratislava was involved not only in commenting on the FDI Act during its legislative journey, but also in one of the first (if not the first) FDI proceedings. The Ministry had clearly stated that its job is to support and approve transactions and not to prohibit or prevent them from completing. It adhered to all relevant statutory periods and requested only the necessary documents (ie no nice-to-have requests).

It was very quick and responsive in communication and open to pre-discussing the transaction during pre-notification talks, as well as to clarifying and discussing interpretation of the FDI Act. Overall, the Ministry seems to have adopted a very pro-active and pro-investment approach.

1 https://www.reuters.com/markets/deals/germany-block-chinese-takeover-semiconductor-firm-ers-electronic-handelsblatt-2022-11-09/
2 https://www.ft.com/content/cdaddf62-72f7-4789-890c-69f1ce196748

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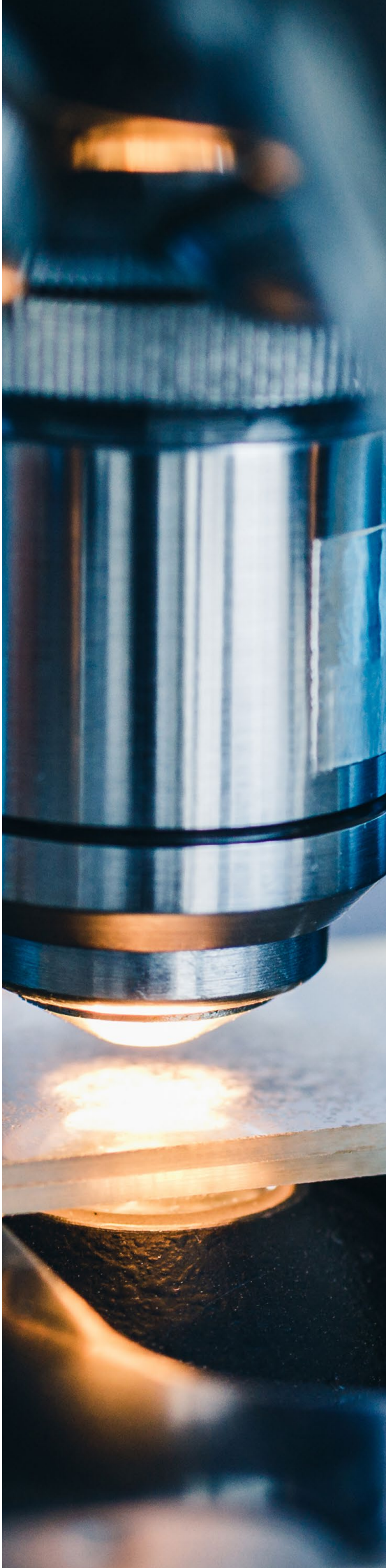

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