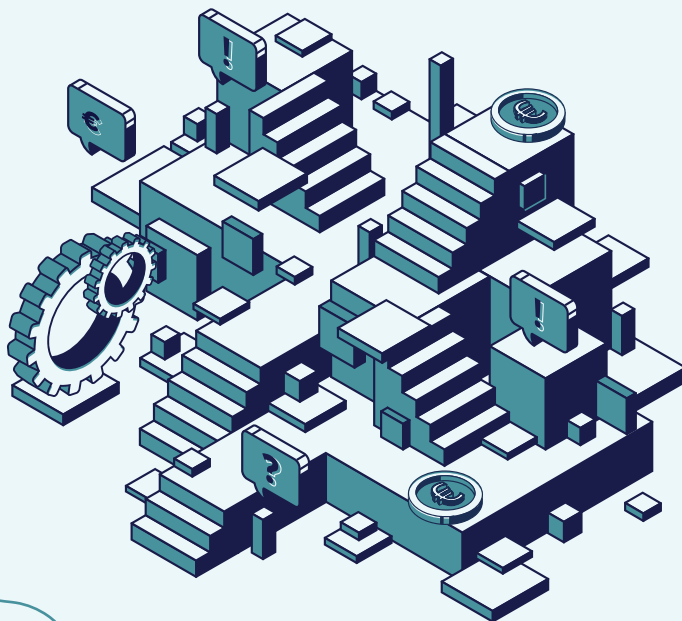


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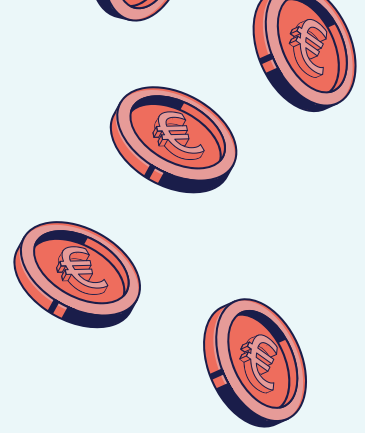
Comparative Analysis of the FDIs' Screening Mechanism Implementation in Selected EU countries: Finding a Role Model for the Macedonian Economy

Zoran Jovanovski, Viktor Mizo



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INTRODUCTION



FDI screening mechanism is a relatively new feature of the EU's economy. It is a mechanism that aims to safeguard the security and public order in the EU. Not every EU member country has such a mechanism in place, so it is a work in progress. Nevertheless, given the geopolitical changes and global economic developments taking place, having a properly designed and functioning FDI screening mechanism grows in importance and increasingly becomes a must for any country that is already a member of EU or wants to become one. At the time when legislative proposal on this matter was tabled in 2017 there were 11 member states with a national FDI screening mechanism. In the meantime, this number has substantially increased and in 2023 a total of 21 member states were effectively working on introducing such a mechanism.

Given the circumstances and the regulation gaps in terms of the FDI screening mechanism in the EU it becomes even harder for an EU candidate country to introduce such a mechanism. Nevertheless, the

process inevitably includes understanding of the overall framework and the EU coordination mechanism in this regard. A comparative analysis of selected countries is also needed in order to learn valuable lessons for designing our own mechanism.

The purpose of this policy paper is to provide information that would facilitate the process of designing an appropriate FDI screening mechanism for North Macedonia. Therefore, two key elements are taken into consideration. Firstly, the EU coordination mechanism for FDI screening is being analyzed in order to better understand "the big picture" regarding this mechanism within EU and the context of information and data sharing among EU member states and the EU Commission. Secondly, a sample of individual countries' FDI screening mechanisms and their functioning within the national and the EU-wide environment was analyzed. The sample included small and open Eastern European fast developing economies in order to mirror the key characteristics of the Macedonian economy.

IMPRESSUM

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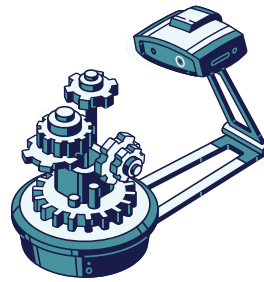
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EU COORDINATION MECHANISM FOR FDI SCREENING



For the time being, the ultimate decision related to introduction of national FDI screening process rests with individual EU member states. They decide whether they will initiate screening procedure for an FDI and decide on the outcome of that procedure. Maintaining security and public order is, nevertheless, of broader importance that goes beyond the borders of an individual country, especially when that country is a member of a group of countries such as the EU. This is because of the risk that an FDI may pose a risk for the security and public order for a number of countries within the EU. Therefore, it becomes a must for the EU to have rules in place that would eliminate such risks. Those rules are part of the so-called “cooperation mechanism” in relation to foreign direct investments, covering both situations – when FDIs are subject of screening or not.

These rules are incorporated in the Regulation (EU) 2019/452 of the European Parliament and of the Council¹. The Regulation establishes a framework for screening of FDIs in the Union. It provides details on the definitions of the main concepts covered, screening mechanisms of EU member states, the factors that may be taken into consideration by member states or the Commission in the course of the screening process, the cooperation mechanism, the information requirements, confidentiality of the process, establishing of contact points,

international cooperation with regard to the issue at hand, evaluation of the screening mechanism, etc.

Given the developments in the last few years related to COVID-19 pandemic and the war in Ukraine, the Regulation (EU) 2019/452 has been accompanied by Guidelines in 2021 and 2022 in order to strengthen the FDI screening mechanism. For the purpose of this paper we focus on the main “messages” from the source document, the Regulation (EU) 2019/452. Important to outline here is that, according to Article 15, “by 12 October 2023 and every five years thereafter, the Commission shall evaluate the functioning and effectiveness of this Regulation and present a report to the European Parliament and to the Council”. The final findings and probable changes in the Regulation are not available at the time of the preparation of this paper.

Key points from the Regulation (EU) 2019/452 that are to be taken into account by any EU member state or a candidate country such as in the case of North Macedonia when designing and implementing FDI screening mechanism are the following:

- EU regulation related to the FDI screening mechanism is for coordination purposes only. At the time the regulation was introduced it was a sole responsibility for the member states to set up a screening

¹ <https://eur-lex.europa.eu/eli/reg/2019/452/oj>

mechanism or to screen. It is still the case, i.e. there is no legal obligation for the member countries to introduce an FDI screening mechanism but at present it is expected that every member state will set up a screening mechanism.

- The final decision in this screening process remains to be made by the member state.
- There is a non-exhaustive list of factors to be taken into consideration for the screening process. Thus, security and public order could be threatened when potential FDI can affect the critical infrastructure (water, health, energy, transport, communications, media, defence, financial infrastructure, etc.). In addition, critical technologies and their dual use items, freedom and pluralism of media, access to sensitive information and supply of critical inputs should be taken into consideration as well.
- Important aspect of the FDI to be assessed is the link between the foreign investor and the government of his country. This includes assessment of the share of the government (in a variety of forms) in the ownership structure of the foreign investor and/or the funding of the FDI, including through government subsidies. This should help identifying the level of control that the foreign government exercises over the foreign investor.
- As usual, the behaviour of the foreign investor should be also assessed, such as his involvement in illegal or criminal activities or prior involvement in activities that affected security and public order in an EU member state.
- In essence, the cooperation mechanism sets the rules of the interactions between the EU member state in which the FDI is taking place, the other member states and the European Commission. Key elements of these rules are the following:
 - The starting point is for each member state and the European Commission to establish a contact point for implementation of the Regulation and mutual communication. The communication between the contact points is to take place through a system that is encrypted and secure.
 - After this, two situations are identified
 - whether a member state is doing a screening of an FDI that takes place on its territory or does not plan to do it.
 - If there is a screening undergoing for an FDI, then the member state on which territory the FDI is taking place informs other member states and the European Commission about the screening or may request opinions from them, and provides, to the best of its knowledge, the information prescribed in the regulation, such as the ownership structure of the foreign investor, the value of the FDI, the products, services and business operations to which the FDI is related, the funding of the FDI and the source of funding and the date when the FDI is planned to be completed or has been completed.
 - Other member states or the European Commission may react to the information they received from the member state in which the FDI screening is taking place. They may provide comments to that member state that are relevant for the screening. The European Commission notifies other member states about the comments made. The Commission itself may issue an opinion addressed to the member state that is doing the screening procedure if it has relevant information about the FDI or assesses that the FDI may jeopardize the security and public order in more than one member state, but shall issue opinion if the security and public order in more than one third of member states may be affected.

- The cooperation mechanism sets timeframe for completion of the communication. Thus, other member states and the European Commission shall notify the member state that is doing the screening whether they will provide comments/opinion about the FDI at hand within 15 calendar days from the day they received information about such screening. If they intend to provide comments/opinion then other member states shall provide them within 35 calendar days from the day they received information about such screening. The European Commission receives the comments of other member states and has 5 additional days to provide its opinion. If other member states request additional information from the member state that is doing the screening than they should provide their comments within 20 days from the day they received the additional information.

- If there is a situation in which the member state in which particular FDI is taking place does not plan to undertake screening but other member states have relevant information that such an FDI may affect the security and public order, these member states provide comments to the member state in which the FDI is taking place. In addition, the European Commission may issue an opinion on its own or shall issue an opinion if the security and public order in more than a third of the member states might be affected by a particular FDI. Other member states may require additional information from the member state in which particular FDI is taking place to provide additional information and may send comments to this member state within 35 days from the receipt of the requested information. When there are such comments from the member states and the European Commission issues an opinion, the Commission has

additional 15 days to issue the opinion. It is important to mention that, when no screening mechanism is exercised by the member state in which the FDI has taken place, the other member states and the European Commission may provide comments and an opinion no later than 15 months after the foreign direct investment has been completed.

- Regardless of the fact whether a member country is undertaking or not screening, the European Commission is simultaneously informed about the whole communication that takes place among the member states regarding certain FDI.

- Cooperation mechanism requires that confidentiality of the information exchanged must be maintained.

- Coordination mechanism allows for international cooperation of member states and the European Commission with third countries, regarding the FDI screening related to preserving the security and public order.

The FDI screening related regulation at EU level, which is valid at the time when this paper has been drafted (January 2024), is currently being revised, following its evaluation, as stipulated in the current Regulation (EU) 2019/452. As indicated by the European Commission, cooperation mechanism does not cause delays in member states' decision-making process and high-level confidentiality within the mechanism is maintained. Nevertheless, certain weaknesses have been identified, as indicated in the OECD report assessing the efficiency and effectiveness of the EU framework for FDI screening, including that:

- The EU framework for FDI screening does not cover investments made by EU subsidiaries of foreign companies.

- There is no obligation for the member states to introduce an FDI screening mechanism.
- There is a need to streamline further both the national procedures and timeframes for screening and the scope of what is being screened in terms of infrastructure, technologies, etc.

European Commission held public consultation between June 14 and July 14, 2023 aimed at evaluating the current framework. The final outcome of the revisions in the Regulation covering FDI screening mechanism, including the coordination mechanism are expected to be publicly announced in the first half of 2024.

Review of the FDI screening mechanism regulation is also stipulated in the Joint Communication of the European Commission and the High Representative from June 20, 2023, related to the European economic security strategy. This Strategy focuses on enhancing management of risk that emerges from specific economic links in a changing geopolitical setting. Hence, the FDI screening mechanism is covered as a segment of a broader context. European economic security strategy identifies four areas of risk to the economic security:

- risks to the resilience of supply chains, including energy security;
- risks to physical and cyber security of critical infrastructure;
- risks related to technology security and technology leakage;
- risks of weaponisation of economic dependencies or economic coercion.

Apart from the relevant Regulation, important aspect of the FDI screening is the implementation itself. In this regard, the European Commission produces an annual

report on FDI screening². This report relates to 2022 and is a third edition. It indicates that the use of FDI screening in the EU continued to grow.

The Annual report of the European Commission shows that in 2022:

- Regarding the Member states
 - 55% of the FDIs are formally screened. This is an increase compared to 29% of the transactions in 2021.
 - The screening was not equally distributed among the member states. Thus, 66% of the notifications for screening were made by 4 member states.
 - The share of blocked transactions of those that have been subject to screening is rather small.
 - 86% of the screened transactions are authorised without conditions or mitigating measures
 - 9% of the screened transactions are authorised with conditions or mitigating measures
 - 4% of the transactions are withdrawn by the parties
 - 1% are blocked transactions.
- Regarding the EU cooperation mechanism
 - 17 member states submitted 423 notifications to the European Commission about FDI screenings.
 - Vast majority of these notifications, i.e. over 90 percent of them, have been submitted by 6 member states (Austria, Denmark, France, Germany, Italy, Spain).
 - Sectoral distribution of the transactions:
 - 27% in manufacturing
 - 24% in ICT
 - 12% in professional activities
 - 9% in wholesale and retail
 - 8% in financial activities
 - 7% in transport
 - 13% in other
 - For the cases for which it received notifications by the member states the

² <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM%3A2023%3A590%3AFIN&qid=1697706246222>

European Commission issued an opinion for less than 3% of the cases.

- Nine member states sent comments to a member state that notified them about the screening of a transaction. These comments were related to 7% of the screened transactions.

- The origin of the ultimate investors was:

- 23% from USA
- 7.6% from UK
- 5.4% from China
- 5% from Japan
- 4.8% from Cayman Island
- 4.6% from Canada
- 40.6% from other countries

- Regarding the time needed for decision-making, 81% of the cases are decided in Phase 1, i.e. within 15 calendar days, 11% in Phase 2, i.e. within 24 calendar days. The remaining 8% of the cases have been ongoing at the end of 2022.

Overall, an important implicit message from the third Annual Report of the European Commission is that FDI screening mechanism is not a theoretical construct but a tangible tool for protecting the security and public order in the countries with such a mechanism. This is a very encouraging message for any country interested in setting up and introducing an FDI screening mechanism.

EU considers the use of a functional FDI screening mechanism within the Union as a “hot topic”, having in mind the geopolitical tensions. There is a strong focus on this issue through the continuous efforts to improve the overall system, including both the EU coordination mechanism and the presence and functionality of the national FDI screening mechanism setups. At present the EU is predominantly looking inwards when it comes to this mechanism. Third countries’ FDI screening mechanisms are important for the EU, but of less importance compared to the status of the EU member states. The conclusions drawn from a meeting with relevant representatives from DG Trade indicate that, at present, phasing-in is not considered as a viable option for third countries, even with the EU candidate countries. This means that they would not be in a position to have access to the EU data bases with information relevant for the FDI screening mechanisms. Nevertheless, such conditions do not reduce the need for the EU candidate countries, including North Macedonia, to make their best effort to design and introduce appropriate FDI screening mechanism and fully exploit all the opportunities provided under Article 13 of the Regulation (international cooperation) as well as the encouragement it provides to the European Commission and the member states for cooperation with like-minded countries.

FDI SCREENING MECHANISMS OF SELECTED EU MEMBER STATES



The next step in the process is creating a pool of ideas that would facilitate the decision-making of how to set-up an FDI screening mechanism in a country like North Macedonia. In this context, it is very important to select relevant countries that would really enrich the pool of ideas. The comparative analysis includes several selected countries.

The rationale in selecting the countries for the analysis was to holistically take into account several factors, such as: the size of the population, GDP per capita, openness of the economy, share of FDIs in GDP (in percent) and the political setup of the country (not a federation, etc.), geographic location. As a result, the following three countries were selected: Estonia, Hungary and Czech Republic.

These are the cases of the selected countries:

Estonia

1. Brief overview of the relevant regulations

Estonia has a special law in place regarding screening of inbound FDIs. It is called Foreign Investment Reliability Assessment Act³ (hereinafter: Act). This Act is passed in January 2023 and came into force in September 2023.

The Act has 6 chapters and is well structured, concise and clear, covering all the important aspects of an FDI screening mechanism. The meaning of certain terms, such as the terms "foreign investment", "foreign investor", "target undertaking", etc. is provided for the

purposes of the Act. It is important that the meaning is linked with the definitions of those terms specified in other relevant acts, such as the Securities Market Act, Competition Act, Strategic Goods Act, National Defence Act, Weapons Act, Media Services Act, Railway Act, etc. This approach secures consistency across the board within various regulations. Additionally, EU documents such as the List of Critical Raw Materials for the EU, are used as a reference point.

When it comes to the meaning of "foreign investor" for the purpose of this Act, it should be pointed out that foreign investor is an entity, a natural person or an undertaking who come from a third country where third country means a country other than a member state of the EU. So, the natural person holds at least one citizenship of which at least one is from a third country and the undertaking is either control by such a person, regardless of the place of establishment or is established on the basis of a law of a third country.

The Act provides a description of the foreign investment authorisation procedure. It distinguishes between the application process, processing of the applications, the elements of assessment process and the possible outcomes from that process. It is important to emphasize that the assessment process distinguished three elements:

1. the foreign investor (his area of operation, his ownership structure, sources of financing for the investment, the degree of direct or indirect control of the foreign investor by a government/armed forces of a third country)

³ <https://www.riigiteataja.ee/en/eli/504042023002/consolide>

2. the economic activities of the target undertaking (the economic sector in which it operates and its relative importance for that sector, its intentions to make changes in that respect, ownership of property rights, to what degree it is financed by the EU funds or other public funds)
3. the economic sector of the target undertaking (the competition situation in the sector, availability of substitute products and services, the impact of the target undertaking entrance in the sector)

The Act defines the work of the key body in the screening process - the Foreign Investment Committee, its composition and functions. With Estonia being a member state in EU, the Act also covers the cooperation in EU on processing foreign investments. At its end the Act explains the government supervision of the compliance with the requirements stipulated in this regulation.

2. Institutional framework

From the institutional framework point of view, the institution for the FDI screening mechanism in Estonia is the **Consumer Protection and Technical Regulatory Authority**. It is a public institution that operates since 2019. It is in charge of strengthening the market and safety regulation and making the consumer environment safer. Its broad portfolio covers the regulations related to the safety of various products and services (toys, cosmetics, clothing and footwear, leisure services, gas and electrical appliances, etc.), issuance of licences for media services like television and radio, communication services, entrepreneurship (consumer protection requirements in various areas, unfair trading practices, dispute resolution, etc.). FDI screening is incorporated in the entrepreneurship segment of this institution's portfolio of activities.

The key body for investment screening that operates within the Consumer Protection and Technical Regulatory Authority is the **Foreign Investment Committee**. The composition of this Committee includes representatives from a wide range of institutions that may contribute in making a proper assessments about the threats for the security and public order coming from a foreign investment. The Committee has representatives from the Ministry of Defence, Ministry of the Interior, Estonian Internal Security Service, Police and Norder Guard Board, Financial Intelligence Unit, Estonian Foreign Intelligence Service, Ministry of Economic Affairs and Communications, Ministry of Finance, Ministry of Foreign Affairs, Consumer Protection and Technical Regulatory Authority and Government Office. Notably, there is no representative from the Estonian Central Bank.

3. How the mechanism works

The screening mechanism is rather clear, simple and straightforward. It starts with a clarification and advice that the foreign investor/target undertaking may ask from the relevant institution (Consumer Protection and Technical Regulatory Authority) in order to clarify whether the foreign investment is subject to an authorisation obligation. The foreign investments that are subject to authorisation can not be completed before obtaining authorisation.

The screening starts with an application and additional documents being sent electronically by the investor to the Consumer Protection and Technical Regulatory Authority. The application provides information such as data about the foreign investor and target undertaking, including the ownership structure and economic activities, description of the

foreign investment, including information about its value, source of financing and time schedule. The application is processed by the Consumer Protection and Technical Regulatory Authority and Foreign Investment Committee, which may request additional information, if deemed necessary.

Processing of the application and making a decision take place within a predetermined time limits. Once the assessment whether the particular foreign investment bears risk for the security and public order in the country is done, a decision is made. The Consumer Protection and Technical Regulatory Authority grants a foreign investment authorisation, refuses to grant it or notifies that the foreign investment is not subject to authorisation obligation based on the Act. This is done within 30 calendar days from the date when the complete application was submitted. This time limit may be extended once for additional 90 days, if needed, or if notification is received from another EU member state or the European Commission that they intend to send comments or opinion regarding the particular foreign investment. On the top of this, the time limit may be extended once for up to 60 days if negotiations have to take place with the foreign investor regarding secondary conditions that require measures to be taken by the investor.

4. The role of each involved entity

There are two entities in charge of the FDI screening process in Estonia: **Consumer Protection and Technical Regulatory Authority and Foreign Investment Committee**. The Foreign Investment Committee approves the granting of a foreign investment authorisation. Based on that, the Consumer Protection and Technical Regulatory Authority grants a foreign investment authorisation. It can be said that

the Foreign Investment Committee is the decision-making body, while the Consumer Protection and Technical Regulatory Authority is the operational body of the screening process.

Consumer Protection and Technical Regulatory Authority is the institution responsible for a number of operational elements within the screening process. It receives the application, communicates with the foreign investor, forwards the information to the Foreign Investment Committee, etc. Consumer Protection and Technical Regulatory Authority is also in charge of the state supervision of compliance with the requirements of the Act. If there is non-compliance it is authorized to impose penalties. It may also revoke a previously given foreign investment authorisation based on foreign investor non-compliance with the secondary condition or because the foreign investor provided information (data, documents) that were important for the assessment but were not correct. In such a case the foreign investor is required to restore, as much as possible, the initial situation as before the investment.

Consumer Protection and Technical Regulatory Authority also plays the role of national point of contact for cooperation on FDI screening prescribed within the EU, collecting and forwarding data to the European Commission, communicating with other EU member states to exchange information, providing/obtaining comments for foreign investments under screening in other EU member states, etc.

Foreign Investment Committee operates within the Consumer Protection and Technical Regulatory Authority. It has a diverse representation of relevant ministries and government institutions. The Committee

operates in line with the rules prescribed by a regulation from the Estonian Government. Foreign Investment Committee is the key element in the screening mechanism because it makes the decisions. Based on its assessment about the risk for the security and public order, the Committee approves or refuses to grant of a foreign investment authorisation. If deemed necessary, the Committee proposes to impose a secondary condition for a foreign investment authorisation. In making the assessment the committee may obtain the information needed and also cooperate with relevant authorities from other countries, the European Commission and international organisations. If the granting of foreign investment authorisation is refused, the reasons for such a decision are not publicly disclosed and are not shared with the applicant. If there is a foreign investment in another member state of the EU for which Estonia wants to provide comments within the prescribed procedure of the EU foreign investment screening, the comments are prepared by the Foreign Investment Committee.

5. Criteria set for evaluation of cases and the decision-making process (based on countries, economic sectors, company specific, etc.)

The FDI screening mechanism in Estonia covers only investments coming from a third country, in accordance with the meaning of that term provided in the Act.

The Act identifies a long list of target undertakings that are of distinctive importance for the security and public order, including: those that are providers of a vital services, undertakings that are related to the defence (those who own a permanent national defence object, those that produce military goods or dual-use items), undertakings

that are related to important infrastructure (operator of airport or heliport, Estonian maritime port, public railway), undertaking related to the media (national television or radio broadcaster, provider of on-demand audiovisual media service, and publishers of news, newspapers and magazines in print media with annual turnover in Estonia in the previous calendar year exceeding three million euros), companies in which the government has a qualifying holding, etc.

6. Results from the work of the mechanism (good and bad practices)

Having in mind that the Act came into force in September 2023 it is too early to make assessment about the results from the implementation of the Act. Nevertheless, the effort made by the authorities produced a well structured screening mechanism so it is reasonable to expect that the overall setting of the FDIs' screening mechanism will produce the expected outcome. Such expectations are based on:

- a. The solid legal ground for implementation of the mechanism, which has entered into force recently thus supposedly building on the experiences gained regarding the screening mechanism within the EU.
- b. The clear and detailed definition of various elements included in the mechanism. This applies to what is intended to protect with the mechanism, the data to be requested from the investor, the elements that serve as a basis for assessment of the investor's application.
- c. The clear definition of the roles and responsibilities of the players within the process.
- d. The efficiency of the screening process setup. Adding the screening mechanism to a public institution that is responsible for strengthening market and safety

regulation and making the consumer environment safer in a number of other areas is a logical step. Additionally, it makes the institution a multiple point of contact regarding specific EU regulations, including for the FDI screening mechanisms. Such a setting is a rational solution for countries with relatively limited resources that have to be used for fulfilling multiple obligations.

- e. The favorable timeframe for decision-making within the mechanism. The regular time limit of 30 days and maximum time limit of 180 days, if needed, represent a reasonable amount of time for ultimate decision to be made by the relevant authorities. Such a timeframe also seems reasonable for the investors, too.

The assessment of the FDI screening mechanism of Estonia would be complete if details about the rules of procedures of the Foreign Investment Committee were available for review. Nevertheless, these rules of procedures are established by a regulation of the government and are not available. Another potential weakness of the screening mechanism may be that it covers only foreign investments that come from a third country.

Czech Republic

1. Brief overview of the relevant regulations

Czech policy on foreign investments has been very liberal in the past. It is one of five most open economies in the world⁴ providing many benefits for attracting foreign Investments. Investments have been regulated only in specific business sectors such as ammunition manufacturing, pyrotechnic industry, electronic communication industry, banking and energy.

In February 2021, the new Act No. 34/2021 Coll., on the Screening of Foreign

Investments⁵ (the “FDI Act”) was enacted. It has been in effect since 1 May 2021, it is not retroactive and therefore cannot be applied to investments made before this date, as is the case in some other EU Member states.

The FDI Act aims to strengthen the control of foreign investments by introducing a mechanism of foreign investment screening that includes both a preliminary mandatory application for permission and screening proceedings initiated by the Ministry of Industry and Trade (“the Ministry”). For this purpose, the Act No.2/1969 on establishment of ministries and other state control administrative bodies was also supplemented. The main aim of the FDI Act is to enable assessment whether the particular foreign direct investment might have a negative effect on the security of the state or its internal or public order, including impact on critical infrastructure, key technologies, and other important entries, which are key for its national security.

2. Institutional framework

The Department for Trade Policy and International Economic Organizations, within the Ministry is responsible for screening foreign investments, conducting consultations and negotiations on conditions, decides on foreign investments and inspects compliance with the obligations laid down by the FDI Act. The Department is headed by Director who should remain impartial and independent in his/her work. The Ministry also devotes a significant part of its analytical capacity to assessing the impact of investments notified by other Member States on security and public order. It also cooperates with relevant international organizations and institutions.

Opinions of other authorities and institutions are required throughout the process, such as those of Ministry of Interior, Ministry of

⁴ <https://data.oecd.org/fdi/fdi-restrictiveness.htm#indicator-chart>.

⁵ <https://www.mpo.cz/en/foreign-trade/investment-screening/legislation/legislation-261340/>

Defense, Ministry of Foreign Affairs, Police and the intelligence services, and, if foreign investments concern their competences, National Cyber and Information Security Agency, Czech National Bank and other state bodies. These bodies should provide the Ministry with their opinion, which must include a reasoning within 30 days from the date of delivery of the Ministry's request submitted to them.

In case of involvement of a Czech company in projects of European interest, if European Commission identifies the acquisition of a company as risky, the Ministry must take into utmost account of the Commission's opinion.

3. How the mechanism works

The investment screening mechanism combines two regimes: sectoral and cross-sectoral. The first regime (*ex ante*) defines a narrow group of the most sensitive areas, *inter alia*, production and development of military material or dual-use goods or the operation of critical infrastructure elements. The second regime (*ex officio*) is cross-sectoral i.e. applying in all other sectors that have the potential to endanger the state security or its internal and public order. In this case, the Ministry may initiate screening within 5 years from the completion of the foreign investment if no consultation procedure was completed before.

Pursuant to the FDI Act, a review may be initiated in respect of any foreign investment, which might endanger the security of the Czech Republic or its internal or public order. Sectors under the strictest review are the following:

- target entities engaging in the production, research, development, or innovation of the life cycle of military equipment pursuant to legislation governing foreign trade with military equipment;

- target entities operating a critical infrastructure elements identified by a relevant central administrative authority (e.g. water supply, power plants or hospitals);
- target entities that are the administrator of an information system of critical information infrastructure, the administrator of a communication system of critical information infrastructure, the administrator of an information system of a basic service, or the operator of a basic service; and
- target entities that develop or produce the goods listed in Annex IV to Council Regulation (EC) 428/2009, setting up a Community regime for the control of exports, transfer, brokering and transit of dual-use items, as amended, or in target property through which such items are developed or produced (specified industries).

Screening of investments in media is also regulated in the FDI Act: "If the target person holds a license for nation-wide radio or television broadcasting or publisher of periodical press, the aggregate minimum average print run of which amounts to 100,000 copies per day in the past calendar year, the foreign investor must, before completing the investment, file to the Ministry a proposal for consultation on whether the foreign investment can threaten the security of the Czech Republic or internal or public order".

Under the FDI Act, a foreign investor is defined as a natural or legal person who has made or intends to make a foreign investment in the Czech Republic and is:

- not a Czech citizen or citizen of another Member State of the EU;
- not a legal person with its seat inside the EU;
- a legal person directly or indirectly controlled by a person who fulfils the above conditions.

As foreign investor is considered also a trustee of a trust fund (in Czech: "svěřenský správce svěřenského fond") if a founder or trustee of the trust fund, the person in whose interest the fund is established or another person able to control those persons fulfils the above conditions. The term "trust fund" also applies to any comparable establishment under foreign law (this also applies to the term "trustee").

"Foreign investment" means an investment of any kind by a foreign investor to pursue an economic activity in the Czech Republic if it enables the foreign investor to effectively control that economic activity.

"Effective control of an economic activity" is defined as a control in which:

- the foreign investor enjoys at least 10% of the voting rights or corresponding influence in an entity conducting the economic activity (including the voting rights of persons who are subject to joint management or practices in concert with the foreign investor);
- the foreign investor or a person closely related to him or her is a member of an elected body (e.g. a director) of an entity conducting the economic activity;
- the foreign investor holds the ownership rights to property through which the economic activity is conducted; or
- the foreign investor has another level of control that would enable him or her to gain access to information, systems or technologies that are important for the protection of the security of the Czech Republic or for its internal or public order.

The FDI Act applies only to non-EU foreign investors, including investors from Great Britain, Liechtenstein, Norway and Switzerland. However, the FDI Act does not

distinguish between non-WTO and WTO investors, between OECD and non-OECD countries, or state-owned enterprises and private companies. Therefore, the same FDI rules are applicable for all non-EU investors.

4. The role of entities involved

The FDI Act provides for three types of filings: (i) mandatory application for permission in respect of foreign investments in a specified industry; (ii) mandatory proposal for consultation in respect of foreign investments in media; and (iii) voluntary proposal for consultation in respect of other foreign investments. Depending on the procedure type, different entities are involved.

Both the application for permission and the proposal for consultation must be filed using the specific filing form in Czech language provided by Government Regulation No. 178/2021 Coll. on the application form for a foreign investment permission and a proposal for consultation.

Documents containing trade and other secrets are kept separately from the subject filed and any person who gains such information in connection with the review procedure or the consultation is required to maintain confidentiality.

5. Criteria set for evaluation of cases and decision-making process (based on countries, economic sectors, company specific, etc.)

The Ministry has not published any guidelines and there are no criteria other than those described above, and no detailed description is given of those criteria. Nevertheless, the Ministry published a FAQ section answering the most frequently asked questions in its first annual FDI report issued on 1 August 2022 .

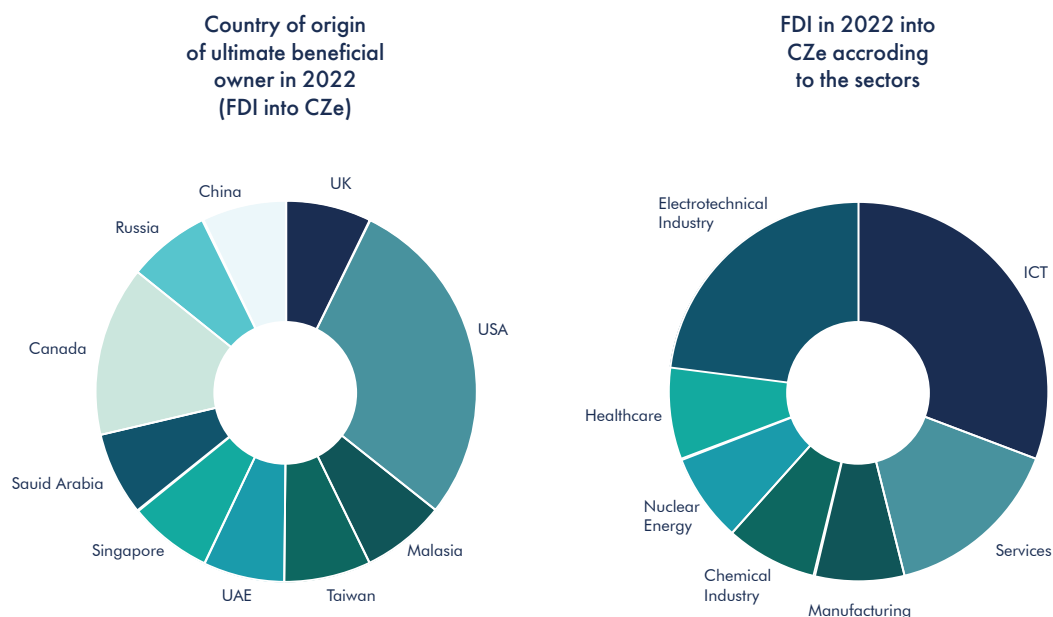
The Ministry has published recommendations to strengthen investment security in emerging technologies. The use of emerging and disruptive technologies (EDTs) such as artificial intelligence, biotechnology, space technology or quantum computing brings enormous opportunities and challenges for the society and economy. However, their strategic importance also calls for responsibility of their developers and state institutions. Decisions of approval or prohibition are not publicly available.

6. Results from the work of the mechanism (good and bad practices)

Given that the FDI Act has been in force and in effect only for two and a half years, there is very limited relevant practice of the authorities and no cases yet that might be mentioned. Accordingly, no proposals to change the law or policy have emerged yet. The very first insight was offered by the first annual report on the investment screening mechanism published by the Ministry in August 2022⁷. According to the first report, 12 cases were investigated during the first year of the

mechanism. Of those cases investigated, no transaction has been prohibited, but in two cases investors withdrew their filings and the investments were not implemented. According to the second report for 2022 solely, 5 cases in 2022 were approved and 5 cases had not been closed by the end of the year. Their closure is expected to be presented in the report for 2023. In 2022, the Czech environment reflects European trends where most frequently notified cases were from US, followed by investments from the UK and China. The investments reviewed cases mostly related to the information and communication technology sector. The second largest sector represented was the electro technical industry. Investments in healthcare, manufacturing, nuclear energy, chemical industry and services were reviewed each in one case.

The Czech Republic itself saw a 38% decline in FDI in 2021 compared to 2020. In general, the FDI Act introduced a system, which acts as a preventive measure against potentially risky investors, while at the same time being the least stringent for non-risky investors.



Source: [Annual Report – screening of foreign investments in the Czech Republic for the year 2022](#)

⁷ <https://www.mpo.cz/assets/cz/zahranicni-obchod/proverovani-zahranicnich-investic/2022/8/FIRST-ANNUAL-REPORT-FDI-Screening-in-the-CZ-2021-2022.pdf>

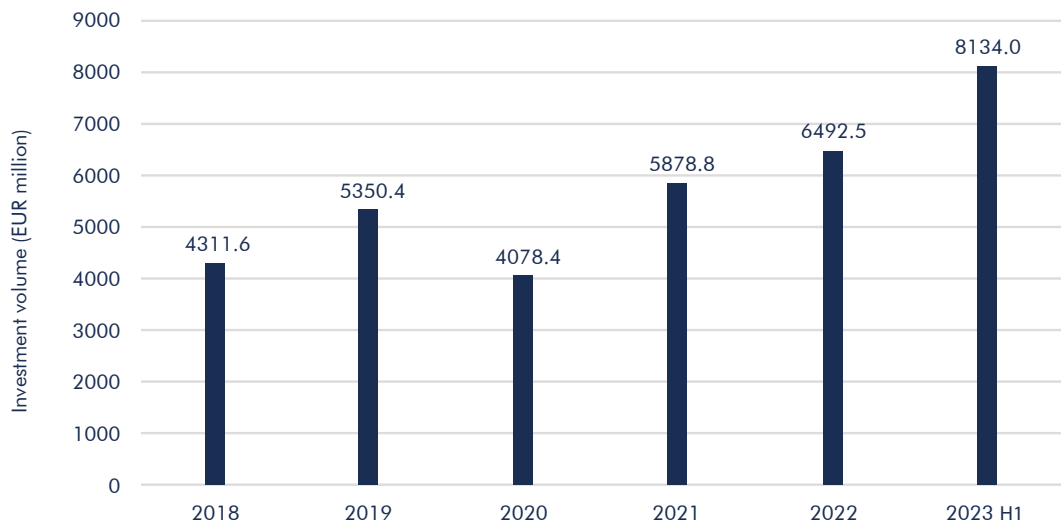
Hungary

1. Brief overview of the relevant regulations

Hungary is one of the CEE EU Member state with significant results in attracting foreign direct investments especially in advanced automotive sectors. It is one of the few EU states that can show balanced

results for investments coming from the western countries and those from the Far East (Japan, South Korea, China etc.). The proximity to EU market, the sufficient infrastructure, the still favorable wage level and the consistently good level of education established Hungary as a favorable investment location. The volume of the investment has doubled in the last four years.

Investment volume
between 2018 and H1 2023



Source: https://www.linkedin.com/posts/istv%C3%A1n-jo%C3%B3-11469734_hungarian-investment-promotion-activity-7096767158826733568-qm7A?trk=public_profile_like_view

Two parallel FDI screening mechanisms are now used in Hungary and are based on the following:

- Approval of the Ministry of the Interior (MI) - "MI FDI Screening" or the First regime
- Act No. LVII of 2018 on the Control of Investments Detrimental to the Interests of Hungarian National Security (the "Act").
- Government Decree No. 246/2018 (XII. 17.) on the execution of Act No. LVII of 2018 ("Decree 246/2018").
- Government Decree No. 532/2020. (XI. 28.) on economic measures during the pandemic ("Decree 532/2020")
- Approval of the Ministry of National Economy (MNE) - "MNE FDI Screening" or the Second mechanism
- Act No LVIII of 2020 on "the transitional rules connected to the termination of the emergency situation and pandemic alert" effective until 30 June 2021 ("Act 2020") and Government Decree No 289 of 2020 (VI.17.) on the definition of strategic

companies. The Temporary FDI Regime was to expire at the end of 2021, but its validity had been extended indefinitely and there are currently no signs that it will become inapplicable in the near future

- Government Decree under no. 561/2022, which extended the scope of the notifiable transactions under the New FDI regime
- EU FDI Screening Regulation (Regulation (EU) 2019/452), OJ L 79I, 21 March 2019.

The First mechanism has a relatively narrow scope regarding the covered sectors (national security, public utility services, and certain financial services) while the Second mechanism covers more sectors and activities and foresees significant exceptions such as those for indirect transactions. Both regimes focus on the origin of the investor and the activities of the domestic target companies.

Both the FDI Act as well as the Temporary FDI Regime have been under constant revision and amendments by the Hungarian lawmakers during the COVID-19 pandemic. Some changes were obviously required to tighten the applicable material as well as procedural rules, while others appear to carry a connotation of the changing shift in the Hungarian review policy (for instance, bringing under the scope of the FDI screening regime sectors that have not been included since the outset, such as higher education or insurance).

2. Institutional framework

In respect of the FDI screening regime under the FDI Act, the Minister overseeing the civil secret services (which is currently the Minister of the Interior) is responsible for conducting the review.

Regarding the screening rules applicable under the Temporary FDI Regime, the Minister responsible for domestic economic affairs (which is currently the Minister of National Economy) is responsible for

conducting the relevant review.

3. How the mechanism works

Under both FDI screening regimes, the foreign investor is required to make the relevant filing and seek prior acknowledgment of the transaction from the competent Minister. At the Ministry of Interior the proceeding takes 60 days, but can be extended for additional 60 days.

The proceeding before the Ministry of National Economy takes 30 days, which may be extended once by an additional 15 days. If the foreign investor breaches the regulation, he could be subject to:

- Criminal sanctions;
- Fines under Act 2020, prohibition of the transaction; and
- Invalidity of the underlying agreement(s) and corporate actions.

Furthermore, breach of the filing obligations can trigger administrative sanctions, as the acting Minister can impose administrative sanctions of:

- Up to 25,000 EUR; or
- At least 1% of the entity's annual net turnover in the preceding year.

4. The role of entities involved

Ministry of interior FDI Screening

MI FDI Screening applies to (i) investors from outside the EU, Switzerland and European economic Area ("EEA"), and to (ii) any subsidiary of such an investor if the subsidiary is established in the EU, Switzerland or an EEA member state and the investor holds a majority of the voting rights in the subsidiary or has a decisive influence in it. The foreign investor must obtain the prior approval of the Ministry of the Interior if he intends to:

- directly or indirectly acquire more than a 25% interest (in the case of a publicly listed

company - 10 % interest) in an existing or yet to be established company with its registered seat in Hungary, provided this company pursues activities that are deemed to be sensitive for national security (“Hungarian Company”);

- acquire decisive influence in a Hungarian Company;
- establish a branch office in Hungary; or
- acquire a right to operate or use sensitive infrastructure or assets in Hungary.

All transactions that result in a foreign investor acquiring more than a 25% interest in a Hungarian Company are subject to foreign investment screening. Moreover, prior approval is required when a foreign investor acquires an interest of less than 25% but this acquisition results in more than a 25% interest in the respective Hungarian Company being held by (several) foreign investors.

Ministry of National Economy FDI Screening

Under Act 2020, investments by foreign investors acquiring an interest exceeding (i) 10% and a value of HUF 350 M (approx. EUR 1 M), (ii) 15%, 20% or 50% irrespective of its value, or (iii) 25% if acquired by more than one foreign investor, require the approval of the Ministry. The foreign investor must notify the Ministry if he intends to acquire the right to use or operate infrastructure necessary for pursuing activities in strategic sectors (including using such strategic infrastructure as collateral).

A “foreign investor” is (a) a company or organization domiciled in, or a citizen of, a state outside of the EU, the EEA or Switzerland, or (b) a company or organization whose majority owner is domiciled in, or a citizen of, a state outside of the EU, the EEA or Switzerland. However, certain acquisitions of a majority interest require the Ministry’s approval if the foreign investor is a company or other organization domiciled

in the EU, the EEA or Switzerland. Act 2020 applies to investments in companies that have their seat in Hungary and:

1. are a limited liability or private limited or public (listed) company; and
2. operate in specified “strategic” sector

However, Act 2020 is not applicable if a transaction affects the foreign company directly, if that foreign company has a Hungarian subsidiary that qualifies as a strategic company. Therefore, transactions over the level of a Hungarian subsidiary (qualifying as a strategic company), may not be approved by the Ministry. This exemption applies to asset deals as well. Moreover, Act 2020 is also not applicable in case of intra-group transactions.

5. Criteria set for evaluation of cases and decision-making process (based on countries, economic sectors, company specific, etc.)

According to the First Regime, the Minister reviews whether the triggering event “harms Hungary’s security interests” (room for discretion). The Minister evaluates the following criteria:

- Whether the proposed transaction endangers or threatens to endanger the national interest, public order or public security with particular attention to the security of supply relating to the basic needs of the society, in accordance with the relevant articles of the Treaty (TFEU Art. 36, 52 (1) and 65 (1), which invoke, among others, public policy, public security or public health issues);
- Whether the foreign investor is directly or indirectly under the control of any administrative agency of any non-EU state (including its ownership structure or financing);
- Whether the foreign investor is or was involved in any activity relating to public

security or public order in any other EU member state

- Whether there is substantial risk that the applicant will commit any crime or illegal activity

The competent ministers under the relevant FDI screening regimes enjoy reasonably wide discretion and powers to approve or reject transactions on national security and public order grounds.

Under the Temporary FDI Regime, the competent Minister is required to provide reasons for his/her prohibition decision, indicating, in particular, the public interest that is believed to be violated or endangered. On the other hand, the FDI Act allows the competent Minister to issue its prohibition decision containing only simplified summary reasoning, which in any case is not permitted to contain any classified information.

None of the competent Ministries have made available any official guidelines on their evaluation criteria of the relevant FDI laws. Decisions of approval or prohibition are not public.

6. Results from the work of the mechanism (good and bad practices)

Practice has already shown that the competent Ministers are prepared to step up in the name of protecting Hungarian national interests and issue prohibition decisions under the relevant FDI regimes, even in respect of the Hungarian components of significant international transactions. Some of those blocking decisions have recently received controversial commentary from the business community as well as European policymakers, as the decisions have been perceived by some as not genuinely falling within the domain of the prevailing and publicly asserted policies.

In 2021 the Ministry of Interior blocked the Austria's Vienna Insurance Group from buying Dutch insurer Aegon's Hungarian subsidiary, dashing a four-country acquisition. The Government granted the specific power to block this type of sale to the Ministry in November 2020, just one day before the parties agreed to the sale.

CONCLUSION

Attracting FDI is one of the main pillars of an economic development strategy for small and open economies and provides good springboard if executed properly together with other economic measures and reforms, helping to propel a country into a middle-income status. This has been the case with many Eastern European ex-communist countries, especially after their EU accession. The three countries that were analyzed as part of this paper are good examples of small and open economies with significant focus on FDI attraction over the last 30+ year period that have experienced substantial economic growth and improvement in the quality of life. North Macedonia aspires to, but is not “there” yet, in terms of economic development, level of FDI and middle-income status. The key challenge for North Macedonia is how to achieve the afore-mentioned status while introducing an FDI screening mechanism and securing it is not an impediment to its economic growth and development.

EU only provides guidelines and framework, rather than imposing implementation of an investment screening mechanism with strict uniform regulations on its member state. Nevertheless, Estonia, Czech Republic and Hungary have implemented and already upgraded such mechanisms adapted to their own individual needs, with unique institutional setup and based on internal administrative capabilities. For example, the case of Estonia may serve as a guideline for setting up an FDI screening mechanism when it comes to a country with a very small

population and relatively limited resources available. Given such circumstances their case indicates implementation of an efficient FDI screening mechanism setup. In general, the FDI Act introduced a system, which acts as a preventive measure against potentially risky investors, while at the same time being the least stringent for non-risky investors.

The still “young” mechanism in Czech played vital role in deterring potentially risky investments in a country widely known for its openness for FDI but also for transparency in the process. The frequency of the public reports with its Q&A sections is a unique approach which should, ultimately, increase the resilience of the international trading system and the security of Czech supply chains.

The complexity of the Hungarian FDI screening mechanism may, at first glance, create an ambient of arbitration, subjectivity and legal uncertainty. The regulatory dualism may negatively affect the attraction of the country for investors while providing space for discretion power for the authorities. In reality, it had more supportive rather than corrective relevance in the growth of the FDI inflows in the country.

Applicable particularities of their individual approaches should be considered as best-case examples when defining and designing the legal, institutional and implementation framework for investment screening mechanism in North Macedonia. Even though

the country is not an EU member state, as part of the pre-accession process and as a NATO member, alignment of the screening process, close cooperation and information sharing can only bring North Macedonia closer to its EU membership goals, while also creating an image of a 'clean' and secure investment destination for FDI devoid of any national and economic security risks. Early implementation of such mechanism will

also provide sufficient space for its further development and reaching excellence in the forthcoming period of the negotiations for EU accession. The global geo-political developments of the last several years (the war in Ukraine, economic tensions with China, the turmoil in the Middle East, etc.) are only emphasizing the need for sharpened focus and impetus to a speedier implementation of an investment screening mechanism.

INFORMATION ABOUT THE AUTHORS

Zoran Jovanovski is an economist and banker with 25 years of professional experience in senior management positions in central and commercial banking. He holds an M.A. in Economics from the University of Arkansas, USA. He has been a recipient of the Ron Brown full scholarship. Currently, he is Vice President of the Economic Chamber of North Macedonia. He is a member of Euromoney's global panel of experts on country risk and co-owner of "Ekonomija i Biznis", the oldest business magazine in North Macedonia.

Viktor Mizo is the Managing Director of Kostal Macedonia, part of the German family-owned Kostal Group – global leader in design and manufacturing of advanced electronics and mechatronics products for the automotive industry. He is also President of the Association of foreign companies with technologically advanced manufacturing within the auspices of the Economic Chamber of Macedonia and an outside expert for McKinsey on various economic development, FDI and free zones projects around the World. Mr. Mizo received his B.S. and M.S. in Mechanical Engineering at the Rochester Institute of Technology, graduating summa cum laude. An alumnus of Harvard University, he holds an MBA from the Harvard Business School.

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**Comparative Analysis of the FDI's Screening
Mechanism Implementation in Selected EU countries:
Finding a Role Model for the Macedonian Economy**

Zoran Jovanovski, Viktor Mizo