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Reforming the Foreign Direct Investment Screening Mechanism of Bosnia and Herzegovina

TradeLab

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Abbreviations

BiH - Bosnia and Herzegovina

FDI - Foreign Direct Investment

e.g - Exempli gratia - for example

TFEU - Treaty of the Functioning of the European Union

SAA - Stabilization and Association Agreement

SM - Screening mechanism

EU - European Union

GDP – Gross Domestic Product

GNI - Gross National Income

UNCTAD - United Nations Conference on Trade and Development

BITs - Bilateral Trade Agreements

EFTA - European Free Trade Association

CEFTA - Central European Free Trade Agreement

IPFSD - Investment Policy Framework for Sustainable Development

CSR - Corporate Social Responsibility

IIA - International Investment Agreements

FET - Fair and Equitable Treatment

ISDS - Investor-state dispute settlement

IMS - Inspection Management System

USAID - U.S. Agency for International Development

SCM Agreement - Agreement on Subsidies and Countervailing Measures

WTO – World Trade Organization

ITA - Indirect Taxation Authority

VAT – Value added tax

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Part I
Introduction

This report was prepared for the Ministry of Foreign Trade and Economic Development of Bosnia and Herzegovina (the Ministry) based on independent research in continuous consultations with Ms. Samira Sulejmanovic, representative of Bosnia and Herzegovina (BiH), Ms. Daut and Mr. Hadžiomerović, to address the challenges concerning Screening mechanisms about Foreign Direct Investment (FDI)

The report is developed under the framework of a legal clinic organized by TradeLab[1]. It provides a detailed and non-exhaustive account of proposals to reform the BiH screening mechanism in the context of peculiarities given by the BiH legal system.A number of noteworthy points are presented; the need to reform the foreign direct investment screening mechanism in line with EU policies and BiH's accession to the EU.

The research consists of two parts: (1) to find solutions and remedies to overcome the lack of transparency and stability of foreign direct investments in BiH and (2) to find a way to align the BiH foreign direct investment policies with the EU policies.

As relations between host governments and foreign multinational companies move from conflict to cooperation, there is a strong need for a transparent, accurate and rigorous process for managing such investments.

The potential to attract significantly higher investment inflows in BiH is undeniable. However, if FDI is to play a larger role in the country's development, the key regulatory and promotional issues must be addressed. The main aim is focused on helping BiH fully exploit its investment potential and contribution to sustainable development. Development of these policies must fit within the existing political structure in BiH and consider the existing economic environment.

1 Background

This section provides a general background and overview of foreign direct investment in BiH, based on existing and historical investment patterns and in light of consultations, taking into account BiH's interest in becoming a member state of the EU.

1.1 Political history of Bosnia and Herzegovina

1.1.1 International Relation with the European Union

Today, BiH is considered an upper middle-income country, performing very well since 1995, when the conflict ended. However, the conflict destroyed much of the Bosnian economy and infrastructure, increasing unemployment, and decreasing output.

[1] https://www.tradelab.org/about - TradeLab is an NGO that connects students and experienced legal professionals with public authorities, particularly in developing countries, to develop sustainable legal capacity.

BiH joined the Council of Europe on 24 April 2002. Since then, the Bosnian authorities have been committed to fulfilling the official commitments made upon accession. To date, BiH has signed and ratified 64 Council of Europe conventions.

BiH has been committed to peacebuilding, democracy, and the transition to a market economy. Since 2003 BiH has formally entered the accession process to the EU and is working to achieve further economic integration with the regional bloc. As an extension of these approaches, BiH signed a Stabilization and Association Agreement (SAA) with the EU, which entered into force on 1 June 2015. The SAA establishes a close partnership between the EU and BiH and deepens the political, economic and trade ties between the two parties[2].

In February 2016, the country applied for EU membership and in September 2016 the European Council invited the European Commission to submit its opinion on the merits of BiH's application. The Opinion identifies 14 key priorities for BiH to fulfill to be recommended for the opening of accession negotiations, in the areas of democracy, functionality, the rule of law, fundamental rights, and public administration reform.

The Commission calls on the country to align its Constitution with the European Convention on Human Rights and to improve the functioning of its institutions in order to be able to integrate European law. Alignment with European policies is therefore a key element of these opinions.

The European Commission states that 'the conclusion of these negotiations is conditional on further progress on a number of priorities, including police reform'. This essentially includes the verification and protection of foreign direct investment destined for BiH.

In its opinion published on 29 May 2019, the Commission explains that "negotiations for accession to the EU should be opened with BiH once the country has reached the required degree of compliance with the accession criteria, and in particular with the Copenhagen political criteria requiring stable institutions and guaranteeing democracy and the rule of law".

The FDI Screening Regulation ("Screening Regulation") was adopted in March 2019[3]. The Screening Regulation established an EU-wide framework within which the European Commission and Member States can coordinate their actions on foreign investment. This

[2]eur-lex.europa.eu - EUR-LEX access to European Union Law - The decision marks the European Union's (EU's) conclusion of the Stabilization and Association Agreement (SAA) with Bosnia and Herzegovina. The aims of the agreement are to: support the efforts of Bosnia and Herzegovina to strengthen democracy and the rule of law / contribute to political, economic and institutional stability in Bosnia and Herzegovina, as well as to the stabilization of the region / provide an appropriate framework for political dialogue, allowing the development of close political relations between the EU and the Bosnia and Herzegovina / support the efforts of Bosnia and Herzegovina to develop its economic and international cooperation, including through aligning its laws more closely to those of the EU / support the efforts of Bosnia and Herzegovina to complete the transition into a functioning market economy / promote harmonious economic relations and gradually develop a free trade area between the EU and Bosnia and Herzegovina / foster regional cooperation in all the fields covered by this agreement.

[3]Ec.europa.eu – EU foreign investment screening mechanism becomes fully operational

powerful tool enables the European Commission to defend European interests. The regulation imposes a legal obligation for all Member States to notify the Commission when a transaction is being screened by national authorities. This is a major achievement in terms of access to information: whenever a transaction is screened, the regulation authorizes the Commission and EU Member States to request additional information. The Commission is finally getting on top of the big picture of problematic deals. It is anticipated that the considerable innovations brought about by this new regulation will benefit all EU Member States.

Likely, BiH will not always be able to benefit from the conduct dictated by this regulation. As a result, the challenges remain problematic; BiH cannot fully benefit from the modernity of European policies if it does not modify and reorganize its internal processes.

One set of unique challenges for BiH in adopting EU investment policies is its complex, specific, and multifaceted internal political structure.

BiH inherited a relatively developed but now obsolete economic system from the Yugoslav era. Indeed, it is highly dependent on external markets, which makes it vulnerable and therefore less prone to investment.

The Dayton Accords[4], brokered by President Clinton and signed in Paris on 14 December 1995, ended the war in BiH. Annex 4 of these agreements contains the Constitution of BiH, imposed from outside on the belligerents, but which distributes power between a weak central state and two Entities: The Serbian Republic, created during the war, and a Muslim-Croat Federation, created during the last months of the conflict, at the instigation of NATO, to allow for a geographical redistribution of the populations. This constitution only governs the appearance of power. The real power is held by a High Representative, who is only mentioned in Annex 2 of the Constitution, paragraph 1c, which only indicates that he chairs a transitional institution, the Joint Interim Commission.

It is not an overstatement to say that BiH's is a complex country which atypical internal structure can lead to confusion and blockages at several administrative levels, which can restrict direct foreign investment.

In the north and east, the Republika Srpska[5](RS), a unitary and centralized republic. In the center and west, the Federation of Bosnia and Herzegovina (FBiH), itself a decentralized federation of 10 cantons. In the north, the Brcko district belongs to both entities, but has a certain autonomy and neutrality. Thus, Brčko District has a special status as an "autonomous territorial unit", although it is part of both the Federation of BiH and the Bosnian Serb Republic. Moreover, this self-governing territorial unit has

[4]Dayton Accords, peace agreement reached on Nov. 21, 1995, by the presidents of Bosnia, Croatia, and Serbia, ending the war in Bosnia and outlining a General Framework Agreement for Peace in Bosnia and Herzegovina. It preserved Bosnia as a single state made up of two parts, the Bosniak-Croat federation and the Bosnian Serb Republic, with Sarajevo remaining as the undivided capital city.

[5]portal.cor.europa.eu - European Committee of the Regions - Bosnia and Herzegovina as a Potential Candidate

its own institutions, laws and regulations, the powers and status[6].

Nevertheless, the investment climate for foreign investors has improved, although significant challenges remain in attracting foreign investment. Foreign investors find it difficult to navigate the complex legal and regulatory system, although some progress has been made in this area. At the entity level, the RS has established district commercial courts to improve the enforcement of local contracts. The RS has also streamlined business registration procedures, reducing the time required from 23 days to 3 and the number of procedures from 11 to 5, as well as the cost. State and entity level institutions have targeted foreign investors through proactive campaigns. Efforts have also been made to encourage green growth investments, such as the adoption of the State-level Renewable Energy and Efficient Co-generation Act in 2014, which encourages private investment in power generation.

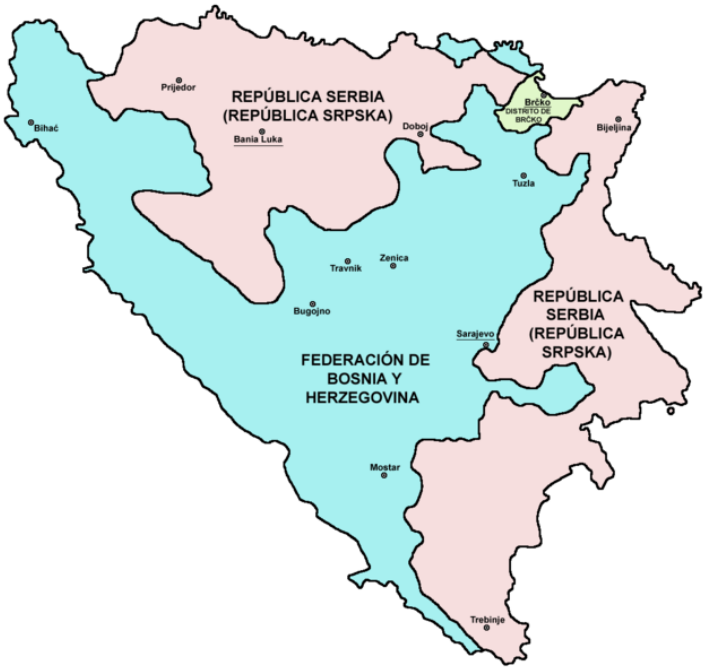

Figure 1: Political and administrative division in Bosnia and Herzegovina[7]

The mobilisation in favour of investment is a priority declared at the highest level of the State. The hearings carried out showed that this mobilisation, effective from the central to the local level, sets in motion a galaxy of actors that it is difficult to name exhaustively. We must separate the central and local levels, but also the complexity of the administrative reality.

Thus, the excessive bureaucracy involved in having 14 governments in the country is a considerable political disadvantage in reforming foreign direct investment in BiH.

[6]Definitively determined by the awards of the Arbitral Tribunal on the Entity Border Dispute in the Brčko Region
[7]commonswikimedia.org

For several years, strong political disputes between the Serb, Croat and Muslim communities have considerably limited the possibilities for national reform. Thus, the lack of coordination created significant challenges for BiH to develop sufficient power in the field of foreign direct investments and thus to have a preponderant place on the European scale.

The political challenges could only be achieved in alliance with the country's economy. For this it is necessary to develop and foresee the economic context in BiH.

1.2 Overview of the BiH legal framework and environment

The legal framework in Bosnia and Herzegovina (BiH) is quite complex due to the combination of different government systems. In addition to the State, the two Entities the Republika Srpska ("RS") and the Federation of Bosnia and Herzegovina ("FBiH"). have their own legal systems. In addition, the Brčko District has a separate legal framework. Only a small number of laws are adopted at the State level. The majority of existing laws were in force in the former Yugoslavia, and accepted as Entity laws, in most cases with no major alterations.

As the Entities have wide legislative competences, each of them may adopt completely different laws. However, with the stimulus of the Office of the High Representative (OHR), the Entities started enacting the so-called "mirror laws", i.e., laws being identical but enacted separately by the Parliaments in each Entity. As a result of the country's political structure, legal reform was very difficult to achieve during the period after the war and up until 2002. However, the situation is improving, and a number of substantial positive developments occurred under the auspices of the OHR[8].

1.2.1 The 2019/452 Regulation: the key instrument

BiH has an aspiration to be part of the EU and seeks to conform with the Regulation (2019/452)[9], the EU framework for screening foreign investment. This information makes it possible to address the question of the influence of Balkan politics at a time of Russian-Ukrainian conflict. Even if this process is going to take some time, before the acceptance, European sources are very important because they are necessary to align BiH with the EU perspective.

As of today, they are still not a part of the BiH legal system. We know that this regulation is not currently part of the BiH legal system. Nevertheless, this regulation is important because it firmly defends European interests, which BiH would like to do, but also allows an efficient communication system between the Commission and Member States, which could directly benefit BiH.

[8]Commercial Laws of Bosnia and Herzegovina – European Bank for reconstruction and Development

[9]Regulation 2019/452 entered into force on April 10, 2019, will automatically apply in EU Member States from October 11, 2020. The objective of this new Regulation is to create cooperation mechanisms between Member States on the one hand, and between Member States and the European Commission on the other hand, in order to control foreign direct investments in sensible European business sectors.

The Regulation has created a legal obligation for all Member States to inform the Commission when a transaction is examined by national authorities.

Therefore, this is a major achievement in terms of access to information[10]: whenever a transaction is examined, the Regulation allows the Commission and EU Member States to request additional information.

By being part of the European Union and adopting this regulation, BiH could, through the Commission, finally have an overview of problematic transactions.

1.2.2 The Agreement between the European Union and Bosnia and Herzegovina

Bosnia and Herzegovina has the potential to attract significant levels of foreign direct investment (FDI) across various sectors. In particular, the signing of the Visa Facilitation Agreement for Bosnian citizens on 17 September 2007[11] and the recent launch of discussions between the EU and Bosnia on the introduction of a visa-free travel system on 5 June 2008. These agreements offer new opportunities for BiH, including trade, commercial and financial benefits. It gives the country a clear European perspective for its development. These agreements represent an important step in EU-Belarus relations and pave the way for improved mobility of citizens, contributing to closer links between the EU and its Eastern Partnership neighbours.

The main objective of the EU-Belarus readmission agreement is to establish, on the basis of reciprocity, procedures for the safe and orderly return of persons who reside irregularly in the EU or Belarus, in full respect of their rights under international law[12].

The effective implementation of the agreements signed between the EU and BiH requires close and effective co-operation between the various structures and institutions at State and Entity level. Such cooperation has not yet been established, given BiH's complex political and constitutional set-up. Without genuine reform, the country will not be able to take full advantage of the benefits that European integration can bring.

1.2.3 Decentralized and fragmented FDI screening mechanism

There is a fragmented, absence, and large diversity in scope and design of FDI screening mechanisms. The EU has no single centralized FDI screening mechanism on grounds of security or public order. FDI screening is the exclusive responsibility of EU Member States under EU law, and national security exceptions under international law.10 Prior to the Commission proposal, no formal coordination among Member States and between Member States and the Commission existed in this field. FDI screening is conducted independently from merger control reviews under EU competition law at EU and Member

[10]The new landscape of investment screening in Europe – Institut Montaigne

[11]Official journal of the European Union - agreement between the European Community and Bosnia and Herzegovina on the facilitation of the issuance of visas - first concrete step towards the visa free travel regime, to facilitate people-to-people contacts as an important condition for a steady development of economic, humanitarian, cultural, scientific and other ties, by facilitating the issuing of visas to nationals of Bosnia and Herzegovina.

[12]European Commission - Visa Facilitation and Readmission: the European Union and Belarus sign agreements

State levels.11 Member States' screening mechanisms vary significantly in scope (review of intra- or extra-EU FDI; differing screening thresholds, breadth of sectors covered beyond defense) and in design (pre-authorisation vs. ex-post screening of FDI).12 A 2018 study into Member States' national rules for the protection of infrastructure relevant for security of supply in the energy sector commissioned by the European Commission provides an insight into the diversity of sector-specific rules.

1.2.4 The global protection of Bosnia and Herzegovina by the European Union

Thus, we can directly notice that a path towards a European integration of BiH is currently developing. In addition, the European Union has several times wished to speak out, supporting the sovereignty and power of BiH on the world stage.

Therefore, from March 2022, the EU Extends Travel Ban on Persons Who Threaten Sovereignty of BiH[13]. The Council of the European Union has decided to extend the current sanctions that apply to persons and entities who undermine the territorial integrity, sovereignty, constitutional order and international personality of BiH. The Council revealed that the restrictive measures will get extended until March 31, 2024.

1.3 Economic Environment

Despite the difficult political environment, BiH is now in its fourth year of stable economic performance, with GDP growth estimated at 5.5% in 2018. Inflation in the first quarter of 2007 was only 1.5% but started to rise in the second half of 2007 as food and transport prices increased, reaching 4.9% in December and rising above 7,43% in spring 2008. The geographic location and trade agreements make BiH an attractive export platform. Located in the heart of SEE, BiH is weel placed to service the regional and EU market. Moreover, BiH has been a member of the Central European Free Trade Agreement since 2006 and has preferential trade access to this market of nearly 22 million people.

Thus, the existence in BiH of large untapped opportunities to attract much larger foreign direct investment (FDI) into the country, and to diversify investment flows and sources beyond the usual sectors and investors.

The economy of BiH is in an ambivalent position and the government has launched a structural reform program for 2019-2021 to boost private investment and exports. Following a recession caused by the Covid-19 pandemic, the economy is estimated to grow by 2.8% in 2021, mainly driven by household consumption (accounting for about three-quarters of GDP). The IMF[15] forecasts GDP growth of 3.3% this year, rising to 3% in 2023, although uncertainty remains due to low vaccination deployment and political

[13]Article from the Schengen Visa News - March 22, 2022 - EU extends travel ban to those who threaten the sovereignty of Bosnia and Herzegovina

[14]Data obtained by Statista concerning % of inflation in Bosnia

[15]The IMF - The International Monetary Fund's mission is to promote financial stability, economic cooperation, produce statistics and studies, and lend money for reforms to countries in crisis.

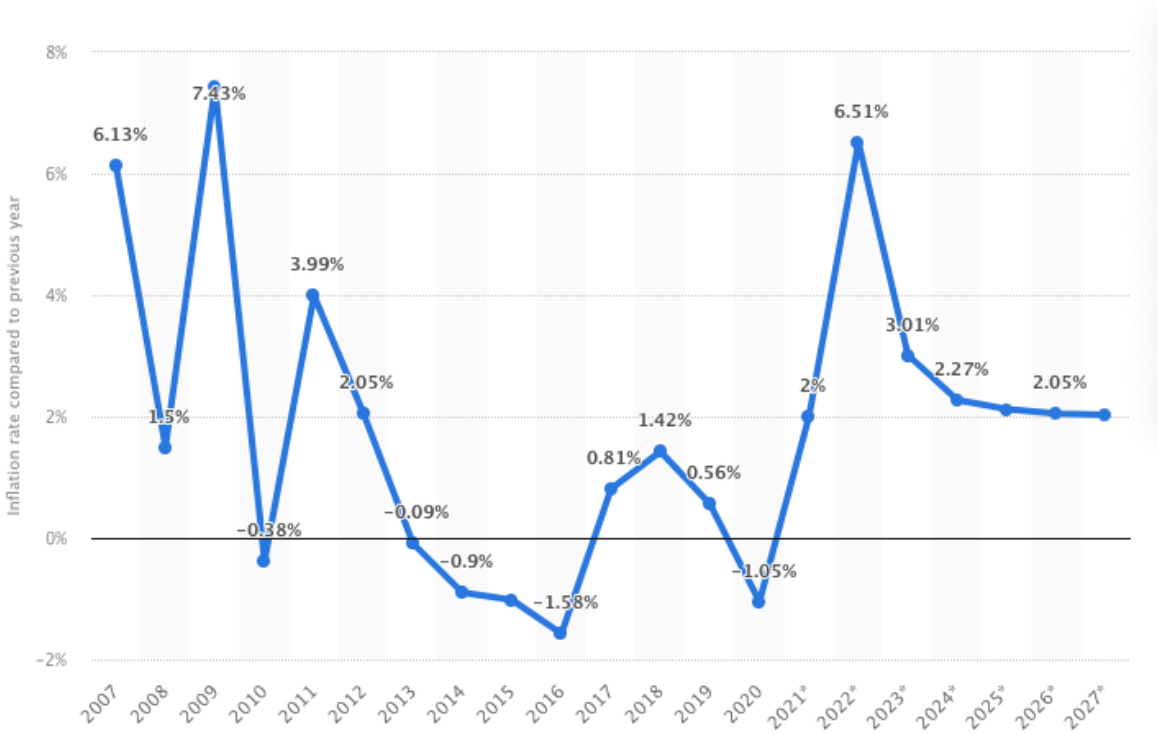

Figure 2: The inflation rate of Bosnia & Herzegovina from 2007 to 2027[14]

instability. However, little progress has been made in reforming the business environment in Bosnia, which discourages investment and keeps unemployment high, estimated at 31.1%, with 20% of the population living above the poverty line. This situation negatively affects economic recovery and widens the gap between BiH and other transition countries. The country needs to attract new foreign investment to create new jobs.

In addition, corruption and high unemployment are major obstacles to the country's economic development. The unemployment rate stood at 15.8% in 2021 and is expected to remain stable over the forecast horizon. Addressing the root causes of persistent long-term unemployment will be essential, including increasing participation in the formal labour market (especially for women) and reducing the skills mismatch of young people. The country's GDP per capita (PPP) is low, estimated at USD 15 935 in 2021 by the IMF.

1.3.1 European Mechanism of Foreign direct investment

Nevertheless, despite the importance of FDI, countries cannot accept FDI irrespective of certain minimal national security and public policy concerns. In order to coordinate this monitoring, the EU has set up the FDI screening Regulation. Following the formal entry into force of the FDI Screening Regulation in April 2019, the Commission and Member States have worked on putting in place the necessary operational requirements for the full application of the Regulation starting 11 October 2020. The EU is one of the worlds‘s maximum open funding locations and the primary vacation spot for overseas direct funding withinside the world.

To protect the EU's financial autonomy, combined with foreign funding, on the world stage, the EU Law of March 2019: created a cooperation mechanism for Member States and the Commission to improve statistics and if important improve worries associated with particular investments; lets in the Commission to problem critiques whilst an funding poses a hazard to the safety or public order of multiple Member State, or whilst an funding may want to undermine a venture or program of hobby to the complete EU; establishes positive middle necessities for Member States who keep or undertake a screening mechanism at country wide degree at the grounds of protection or public order; encourages global cooperation on funding screening, which include sharing of experience, pleasant practices and statistics on troubles of not unusual place worries.

On 25 March 2020, the Commission issued guidance to the Member States, calling inter alia upon all Member States to install a fully-fledged screening mechanism, and making sure a robust EU-huge method to overseas funding screening at a time of public fitness disaster and associated monetary vulnerability.

Without obliging Member States to set up a national foreign investment control system, this regulation aims to provide a framework for existing national control mechanisms and to ensure coordination at European level. It also aims to introduce a right of scrutiny by the Commission over FDI in strategic assets or companies, without, however, giving it any decision-making power. The Regulation also sets out a common minimum framework to be followed by Member States that maintain or adopt a screening mechanism at national level. Even if BiH decides to follow this regulation uniformly, it does not have the capacity to implement it effectively at the national level. Therefore, BiH needs to develop an appropriate mechanism that can fit its governmental structure, institutional framework and strategic goals to increase of foreign investors.

1.4 Legal basis and relevant definitions

Foreign direct investment is an important part of all global economies today. Indeed, in an era where capital is severely constrained by tariff barriers and high transport costs, international investment appears as a substitute for trade in goods. It also allows the movement of capital from the most developed countries to least developed.

A screening mechanism, also defined as an 'Investment Screening', refers to a procedure allowing the State to assess, investigate, authorize, condition, prohibit or unwind foreign direct investments based on a range of security and public order criteria[16].

The department in each Member State is responsible for implementing the EU Regulation "establishing a framework for screening foreign direct investment in the Union". The Foreign Direct Investment Screening Mechanism will act as the national contact point for cooperation with the European Commission and other EU Member States on investment screening.

[16]enterprise.gov.ie - Department of enterprise, Trade and deployment

Among these measures, many of which have already been commented on in the European Papers[17], the Communication adopted by the Commission on 25 March 2020 on Guidance to Member States on foreign direct investment and the free movement of capital from third countries and the protection of European strategic assets, in view of the application of Regulation (EU) 2019/452 (FDI screening Regulation) deserves attention.

With these guidelines, the European Commission intends to guide States in the application of their foreign direct investment screening mechanism, in relation to the reactions that need to be deployed to face multiple crises such as the current health and economic emergency.

Article 2 of the Regulation provides for numerous and important definitions. For the purposes of this paper, the following should be held relevant:

- *Foreign direct investment* means "an investment of any kind by a foreign investor[18] aiming to establish or to maintain lasting and direct links between the foreign investor and the entrepreneur to whom or the undertaking to which the capital is made available in order to carry on an economic activity in a Member State". For the definition of investment, though contested and not legally binding, the so-called "Salini" test[19] may be useful. As for its scope, forms of investment not implying the exercise of voting rights[20] seem to be excluded.

- *Screening mechanism* (hereinafter, if not cited, SM) means "an instrument of general application, such as a law or regulation, and accompanying administrative requirements, implementing rules or guidelines, setting out the terms, conditions and procedures to assess, investigate, authorize, condition, prohibit or unwind foreign direct investments on grounds of security or public order".

In this guidance, the Commission goes beyond the role assigned to it by Regulation 2019/452. By calling on States to use their screening mechanism to control FDI that could threaten the Union's ability to respond effectively to future health crises comparable to those of COVID-19, and by insisting on the need to carry out these controls with due regard to the Union's interests, the Commission is laying the groundwork for a genuine common investment policy, the cornerstone of which is the security of the Union.

A foreign direct investment screening mechanism will enable Member States and the Commission to exchange information and share their analyses of the issues at stake,

[17] European Papers - www.europeanpapers.eu - EU Foreign Direct Investment Screening and COVID-19: towards a common investment policy based on the security of the Union

[18] Art.2 n.2 means a *"natural person of a third country or an undertaking of a third country, intending to make or having made a foreign direct investment"*, while the undertaking of a third country is defined as *"undertaking constituted or otherwise organized under the laws of a third country"* (art.2 n.7). Please note that as a third country under EU law it is a non-EU country.

[19] See *International Center for Settlement of Investment Dispute Case no.ARB/00/4, Salini Costruttori S.P.A and Italstrade S.P.A v. Kingdom of Morocco (§52)* which interprets investment under art.25 of the ICSID Convention

[20] Such as portfolio investment, which does not entail active control over the management of a company but rather an aim to grasp its profits, and acquisitions for reselling purposes, which are nonetheless both caught by art.63 TFEU and subject to limitations under art.65 TFEU, see recital n.4, which is relevant also for restrictions of intra-EU investment. See also A. Dimopoulos, *The Constitutional Fundamentals of EU Investment Policy*, p.9 in S.W. Schill et al, *International Investment Law and Constitutional Law*, Edward Elgar, 2020.

and sometimes the risks, that certain investment projects that are to take place on European territory may present, following the example of that set up by the European Union. Screening mechanisms are now necessary for the proper functioning of the economy. This necessity has already been demonstrated during the economic crisis of 2019, when China decided to invest in the Balkan countries. Balkan Investigative Reporting Network ('BIRN'[21]) has identified 135 Chinese-linked projects in the Balkans worth more than 32 billion €[22]. These investments were not accompanied by the necessary tools for their verification (information exchanged / does the investment appear to pose a threat to the security or public order of more than one Member State / is the transaction likely to affect a project or program of interest to one of the parties), so that most of them were the center of corruption, exploitation, and environmental harm.

[21] birn.eu.com - BIRN – Balkan Investigative Reporting Network

[22] https://balkaninsight.com/ - China in the Balkans (controversy and cost)

Part II
Current situation in Bosnia and Herzegovina

Foreign direct investment benefits both home and host countries, and it is an essential component of an open and efficient international economic system, as well as a key driver of development. However, the benefits of FDI are not automatic, and they are not distributed evenly across countries, sectors, and local communities.

National policies and the international investment framework play an important role in attracting FDI and maximizing the development benefits of such investment. The primary responsibility for creating a transparent and favorable investment environment, as well as building the human and institutional capacity to exploit it, rests with host countries[23].

FDI has become an increasingly important source of economic development and modernization, income growth, and employment for developing countries such as Bosnia and Herzegovina. They have liberalized their FDI regimes and taken other steps to attract investment. They are attempting, with varying degrees of success, to determine how national policies can best contribute to maximizing the benefits of a foreign presence in the local economy.

FDI has technological spillovers, contributes to human capital formation, facilitates integration into international trade, helps create a more competitive business climate, and improves enterprise development in host countries with adequate policies and a minimum level of development. All of these factors help to accelerate economic growth, which is the most powerful tool for combating poverty in developing countries.

While many of these negative effects are likely to be related to shortcomings in host countries' domestic policies, significant problems can arise where these shortcomings are difficult to address. These include a deterioration in the balance of payments as a result of profit repatriation, a lack of positive relations with local communities and national collaboration, potential environmental damage, particularly in the extractive and heavy industries, and social disruption caused by accelerated commercialization in developing countries, particularly in terms of human rights and the effects on competition in national markets.

Furthermore, the authorities of some host countries believe that the growing reliance on multinational corporations constitutes a loss of political sovereignty. Furthermore, some of the anticipated benefits may not be realized if, for example, the host economy's current level of economic development makes it unfit to benefit from the technology or know-how transferred through FDI.

[23]OECD, 2002, Foreign Direct Investment for Development

2 Problems that arise in other developing countries where there is no review mechanism

The main impact of FDI on human capital in developing countries is primarily the result of local governments' efforts to attract FDI by improving local human capital.

The host country's labor standards are an important consideration. By taking anti-discrimination and anti-abuse measures, the authorities increase employees' chances of improving their human capital and provide them with additional reasons to do so.

A labor market in which participants have a sense of security and social recognition is more likely to have the flexibility required for successful human capital-based economic strategies. It creates an environment in which multinational corporations can operate more easily, adhering to home country standards and contributing to human capital development. The compliance of national policies with relevant ILO standards is critical in this regard. In the context of the rapid and exponential growth of foreign investment in developing countries, the treatment of human rights, particularly in the social field, is critical.

In terms of the social consequences of FDI, there is evidence that it can help reduce poverty and improve social conditions. When FDI is used to develop labor-intensive industries and multinational enterprises strictly adhere to national labor laws and internationally accepted labor standards, the poverty-reducing benefits of FDI may be greater.

There is little evidence that the presence of foreign firms in developing countries causes a general deterioration of fundamental social values such as labor standards. Labor laws may even act as a deterrent to FDI in some cases, because investors are concerned about tarnishing their reputation elsewhere in the world and fear social unrest in the host country, but if the company does not care about its reputation, a real problem may arise. However, problems may arise in specific contexts. It is argued, for example, that the significant role played by export processing zones in a number of developing countries raises concerns about the respect for fundamental social values.

The private sector (including foreign investors) is critical to economic growth and the achievement of long-term development goals. As a result, how private enterprises behave and are governed is critical for maximizing the benefits of FDI for economic development.

The particular difficulty in regulating the activities of transnational corporations stems, first and foremost, from their elusive and protected nature. These private bodies have the potential to become as powerful as, if not more powerful than, sovereign states. As a result, in the absence of an appropriate legal framework, the transnational nature of their activities, as well as their organizational structure, allow them to avoid national and international laws and regulations that they deem unfavorable to their interests or prohibitively expensive. The acquisition of rights derived from international norms by subjects not belonging to the international order but treated as objects of international

law is gradually emerging as international law evolves, particularly contemporary international economic law. Furthermore, bilateral investment treaties (BITs) enshrine the idea that an individual not only has international rights and protections, but also the ability to claim compliance with the norms established between states.

In terms of sanctions, subjects of domestic law cannot be held liable for international wrongful acts. Only at the national level can liability be sought. If it is civil, it is the result of the national legal system to which the harmful acts are linked. International instruments, such as environmental conventions, can serve as a framework for these liability regimes. However, liability remains a matter of domestic law, and these regimes are conditioned by the instruments' transposition and application in domestic law by the State.

The goals of international investment and trade law appear to be at odds with the need to give real priority to the protection of human rights in developing countries and to strengthen control over multinational corporations' practices. International economic law promotes international trade facilitation. Its main goal is to support the overall policy of reducing and eliminating national protectionist measures and trade barriers. Historically, states have had little leeway in enforcing protective public interest rules that contradict or oppose the economic interests of foreign investors or WTO rules[24]. Human rights and environmental concerns, by definition, can stymie trade and slow economic growth[25].

Through the dissemination of good practices used by multinational corporations and the subsequent spill-over effects on local businesses, FDI can bring environmental and social benefits to host economies. There is a risk, however, that foreign-owned companies will use FDI to export products that are no longer approved in their home country. In such cases, regulatory standards may be lowered or frozen, especially if the host country authorities are eager to attract FDI.

The presence of natural resources in the host countries (exemplified by investment in the oil industries in Nigeria and Angola) and, to a lesser extent, the size of the local economy appear to have been the main factors driving FDI in Africa, for example, in comparison to a continent where many countries are developing, in recent decades[26].

The Ogoni case, involving the Shell company in Nigeria, exemplifies the lack of review mechanisms. In this case, a complaint was lodged with the African Commission

[24]Examples are numerous, we will cite a few, ICSID, SPP v. Egypt, no. ARB/84/3, award 20 May 1992; Permanent Court of Arbitration (PCA) Tribunal, Philip Morris Asia Limited v. Government of the Commonwealth of Australia, No. 2012-12, December 2015

[25]These rights are expressed through the rights and obligations contained in eight fundamental ILO Conventions. Freedom of Association and Protection of the Right to Organise Convention, 1948 (No. 87) Right to Organise and Collective Bargaining Convention, 1949 (No. 98) Forced Labour Convention, 1930 (No. 105) Abolition of Forced Labour Convention, 1957 (No. 138) Minimum Age Convention, 1973 (No. 182) Worst Forms of Child Labour Convention, 1999 (No. 100) Equal Remuneration Convention, 1951 (No. 111) Discrimination (Employment and Occupation) Convention, 1958

[26]E. Hernández-Catá (2002, ≪ Raising Growth and Investment in Sub-Saharan Africa : What Can Be Done? ≫, IMF Policy Discussion Paper, PDP/00/4.

on Human Rights against the Nigerian government[27], which is the majority shareholder in a Nigerian subsidiary of the Dutch company Shell[28].The consortium was accused of causing significant environmental damage and health issues among the Ogoni people as a result of environmental contamination[29]. Following that, the Nigerian government was accused of facilitating and condoning these violations by handing over the state's judicial and military powers to the oil companies. In response to the continued nefarious activities of the Dutch multinational's subsidiary with the complicity of the state, a protest movement formed and conducted a nonviolent campaign.The government placed its military forces at the disposal of the transnational company to ensure the protection of the oil drilling, its investment, and its profits. According to the communiqué, Nigerian security forces attacked, burned, and destroyed several Ogoni villages and homes, displacing thousands of civilians. Nigeria has been found guilty of violating several articles of the African Charter on Human and Peoples' Rights by the African Commission.

Foreign-domiciled investors may be discouraged by the loss of assets due to breach of contract because they are typically excluded from informal networks that develop in the absence of a transparent judicial system[30].

Chinese investment is one example. Most Chinese firms routinely violate the most basic workers' rights, particularly where states lack the means and will to enforce them. Chinese entrepreneurs avoid local social legislation as well as close collaboration between Chinese firms and public authorities (local and/or national). This can also be seen in the context of large infrastructure projects funded by China[31].

These projects, such as the Meroe Dam, are also designed with no regard for their social and environmental costs in mind. Chinese companies exploit legal loopholes, loopholes in national legislation, and the weakness of control bodies, where they exist, to increase their profit margins, with little regard for working conditions or the social, environmental, and health impact of their activities[32].

The working conditions and working relationships in Chinese companies operating in a dozen African countries are appalling: insignificant remuneration, excessively long, back-breaking working days without breaks, widespread use of temporary contracts or no contracts at all, appalling housing conditions for workers, failure to comply with

[27]African Commission on Human and Peoples' Rights, case Social and Economic Rights Action Center, Center for Economic and Social Rights v. Nigeria, Communication 155/96, 30th Ordinary Session, Banjul, Gambia, 13 October 2001

[28]The Nigerian government participated through a state-owned company, the National Petroleum Company (NNPC) in a consortium with Shell Pretoleum Development Corporation (SPDC)

[29]African Commission on Human and Peoples' Rights, Social and Economic Rights Action Center, Center for Economic and Social Rights v. Nigeria, §1. Furthermore, the communication also alleges that the oil consortium has exploited the Ogoni reserves without regard to the health or environment of local communities, dumping toxic waste into the air and local waterways, in violation of applicable international environmental rules. The consortium also neglected and/or failed to maintain its infrastructure, causing many foreseeable accidents near villages. Ibid. §2

[30]Voir, par exemple, D. Dollar et W. Easterly (1998), ≪ The Search for the Key : Aid, Investment and Policies in Africa ≫, World Bank Working Paper

[31]The construction of the Meroe Dam in Sudan (2003-2008), financed by China and involving Chinese construction companies, was accompanied by the forced displacement of thousands of people (mostly peasants, relocated in precarious conditions on poorly fertile land), and the murder of dozens of protesters (Askouri, 2007)

[32]Yaw Baah A. and Jauch H. (2009), Chinese Investments in Africa. A Labour Perspective, African Labour Research Network

minimum safety standards, hostility towards trade unions, increasing threats and pressure on workers, coercive measures These forms of exploitation are particularly linked to China's application of labor standards in its contacts[33].

Beijing has long justified its companies' behavior by citing the principle of non-interference in the internal affairs of states or citing its inability to monitor private actors' activities. This non-interventionist rhetoric, however, has not always been true. The People's Republic of Zambia, for example, threatened to withdraw aid if Michel Sata, the opposition candidate in the 2006 presidential elections, won and announced that he would challenge contracts signed with China. This example demonstrates China's political and electoral reach in Africa through its investments[34].

These various examples highlight the dangers posed by the legal vacuum and lack of oversight of foreign investments in developing countries. This demonstrates not only the risks that this can pose in terms of fundamental rights respect, but also in terms of the country's political stability[35].

Several countries, however, have been successful in attracting FDI, owing to the quality of the local business environment. Countries such as Mozambique, Namibia, Senegal, and Mali were discovered to have a relatively favorable investment climate in the late 1990s, apparently due, first and foremost, to government efforts to encourage trade liberalisation, the launch of privatisation programs, the modernization of investment codes and the adoption of international FDI agreements, the development of a small number of priority projects with broad economic impact, and finally, the high profile of FDI[36].

3 Difficulties in implementing review mechanisms

3.1 Political: locally agreed-upon political investments

Measures taken by host countries to attract FDI and benefit from the presence of foreign firms are largely equivalent to measures taken by host countries to mobilize domestic resources for productive investment. In most cases, local resources serve as the foundation for self-sustaining development. A hospitable business climate is critical not only for mobilizing domestic resources, but also for attracting and effectively utilizing international investment.

Every aspect of a host country's administrative practices should be assumed to have an impact on the investment climate. Policymakers' overarching goal should thus be to ensure maximum institutional predictability.

The general conditions for FDI are the same as those needed to create a dynamic

[33] L. Serván (1996), ≪ Irreversibility, Uncertainty and Private Investment : Analyticial Issues and Some Lessons for Africa ≫ , World Bank Working Paper

[34] Love Hate: Michael Sata's Complex Relationship with China, A China in Africa , Podcast, November 6, 2014

[35] N. Odenthal (2001), ≪ FDI in Sub-Saharan Africa ≫, Technical Paper no 173, OECD Development Centre

[36] J. Morisset (2000), ≪ Foreign Direct Investment in Africa : Policies Also Matter ≫, World Bank Working Paper

and competitive environment for domestic businesses. The rule of law, transparency principles (both in host country regulatory action and corporate sector practices), and non-discrimination all help to attract foreign companies and leverage their presence in the local economy. If investors do not have a reasonable understanding of the environment in which they will operate, FDI is unlikely to enter the country. Furthermore, a lack of transparency can lead to illegal and unethical practices, weakening the conditions under which companies operate in the host country.

The Dayton Peace Agreement of 1995 established a complex system of governance, which based the country's post-war territorial and administrative reorganisation on the division of the country into two entities: Republika Srpska and the Federation of Bosnia and Herzegovina.

Bosnia and Herzegovina's Constitution established a multi-ethnic government with an asymmetric and complex governance structure. The collegiate Presidency is made up of three members, one from each of the constituent nations: one Bosniak and one Croat from the Federation of Bosnia and Herzegovina, and one Serb from the Republika Srpska. The Chairman of the Presidency is the Head of State, and the Chairman of the Council of Ministers is the Head of Government. The Parliament is divided into two chambers: the House of Peoples (Dom Naroda) and the House of Representatives (Predstavnicki Dom)[37].

Bosnia and Herzegovina ratified the European Charter of Local Self-Government in 2002, which means that it applies to all levels of local self-government in Bosnia and Herzegovina, including cantons, according to Article 13 of the Charter. Bosnia and Herzegovina ratified the Charter on November 1, 2002. Thus, the country has committed to enshrining the principle of local self-government in its domestic law in order to ensure its effective implementation, transferring competences to local governments with corresponding financial resources, and ensuring the full implementation of the principle of subsidiarity in order to guarantee the exercise of local self-government in accordance with the provisions of the Charter. Due to the State's structures and the competences of the Entities, the Charter is not expressly recognized in the BiH Constitution. However, the Entities' constitutions and legislation protect the principle of local self-government.

Although the two Entities of BiH have distinct and very different local government systems, necessitating a separate examination of their situation, they face serious common challenges. They face the following difficulties: secondary city decline and a growing urban-rural divide; the fragmented and often costly nature of local government administration; the burdens of servicing external debt; controversies over horizontal resource allocation (particularly in the Federation of Bosnia and Herzegovina); the often inefficient management and sharing of natural resources (which cannot become an important source of funding for local governments); the lack of scope for increasing accountability. Both local government systems suffer from serious problems and need fundamental re-

[37]Report CG37(2019)18final 31 October 2019 Local and regional democracy in Bosnia and Herzegovina

forms, a view shared by a large majority of local government leaders[38].

Bosnia and Herzegovina's local government system is extremely complex and disparate, particularly in terms of the division of responsibilities between municipal and cantonal or Entity levels. Furthermore, the administrative and financial autonomy of municipalities, particularly the smallest ones, appears to be severely limited. Local decision-making procedures are as inefficient as local administration, which frequently lacks competence.

This complex and fragmented institutional structure is an impediment to local development and municipal autonomy. Far from being functional and efficient, fragmentation stifles cooperation, particularly between communes belonging to different Entities or cantons, highlighting the lack of an overall framework or, at the very least, coordination between the two Entities, as well as the state's weakness: "one country, two systems and Entities".

A good example of the difficulties associated with institutional fragmentation and complexity is an EBRD loan for water supply, bridge construction, and other infrastructure, which requires the approval of too many institutions (the BiH Presidency, the BiH Council of Ministers, both Houses of the BiH Parliament, the Republika Srpska Government, the Republika Srpska National Assembly and, last but not least, the local government)[39].

Furthermore, Bosnia and Herzegovina's politics are characterized by a constant climate of election campaigns: elections (general or local) are held every two years, and the formation of governments frequently takes several months. It is difficult to focus on the concrete medium- and long-term action of the numerous executive bodies due to the constant divisive discourse and controversies between nationalist parties[40].

The ability of local institutions to provide efficient services is an important source of legitimacy. This capacity is determined by the local situation and the people involved, but it is also influenced by the larger context and larger processes, such as the allocation of competencies and financial resources. This correlation with the state situation is especially visible in Bosnia and Herzegovina. It severely limits local governments' potential and the positive contribution they could make to the country's development.

Transparency is likely to be the most important element of a favorable investment environment that can be influenced by government action. Companies, for example, may wish to invest in countries where the legal and regulatory frameworks are not otherwise regarded as investor-friendly, if they can obtain reasonable clarity about the conditions under which they will be able to operate. In contrast, there would be a certain level of transparency below which the conditions in which companies operate become so opaque

[38]These "common challenges" were identified in a recent study conducted by the EU-funded Local Governance Initiative. See: Local Governance Initiative, Local Governance in Bosnia and Herzegovina, Report on the Consultations of a Joint Commission on Local Governance, June 2018, p. 8: (https://europa.ba/wp- content/uploads/2018/06/Master-LGI-report-04062018-web-eng.pdf).

[39]Document of the European Bank for reconstruction and development, Approved by the Board of Directors on 2 September 20201 BOSNIA AND HERZEGOVINA GrCF2 W2 - Banja Luka Water - Phase

[40]Report CG37(2019)18final 31 October 2019 Local and regional democracy in Bosnia and Herzegovina

that virtually no investor would want to enter the market, regardless of the incentives offered. Another important factor related to transparency is the host country's level of social cohesion and stability.Investors' perceived risks are significantly increased by a lack of cohesion and stability, which can lead to concerns that foreign companies' reputations may be jeopardized.

Transparency is required in both the actions of the authorities and the more general conditions under which businesses operate in the host country. Given the relative irreversibility of FDI, uncertainties about legislative action and rule enforcement are significant impediments, resulting in risk premiums and fears of discriminatory treatment. Transparency about the conditions under which companies operate in the host country raises information costs, diverts energies to rent-seeking activities, and can lead to completely illegal activities such as corruption. If host-country firms face this situation, it is likely that outside investors who are unaware of locally available information will be even more discouraged.

Foreign direct investment frequently contributes to a more transparent environment. In some cases, the presence of foreign companies encourages governments to adopt more transparent practices, increases corporate transparency, and aids in the fight against corruption.

3.2 Economic difficulties: what are you avoiding? in order to stifle or discourage investment

Twenty-six years after the Dayton Agreement, which ended the Bosnian war, several actors are attempting to destabilize the Western-installed order. Foreign actors' perceptions of investment are also influenced by geopolitical perceptions as well as the country's political and military stability. With the outbreak of war in Ukraine, it is necessary to examine the options available to Bosnia and Herzegovina, as well as the implications for current and future FDI. Today, NATO and the EU, along with Russia and China, are vying for influence in the region. North Macedonia's accession to NATO could be the last, with Russia urging Serbia and Bosnia and Herzegovina not to follow suit.The region's general decline in democratic standards over the last decade has slowed its integration into the EU, handing the initiative to China's growing economic influence in the short term[41].

The Western Balkans is a complex region in which many external actors seek to exert influence by gaining the support of various ethnic and religious communities. Saudi Arabia and Turkey have ties to Muslim-majority countries (Albania, Kosovo and Bosnia). But it is Russia's ties with Serbian Orthodox ethnic groups, as well as China's growing economic footprint, that are stymieing the region's integration into the EU and NATO.The economic downturn expected as a result of the coronavirus pandemic may cause the EU accession processes to be further delayed, prompting the poorest countries to turn to China for desperately needed investment and loans. In addition to the security impasse,

[41]Larsen, Henrik (2021) 'NATO's Strategic Concept Should Initiate a New Partnership Policy', Internationale Politik Quarterly.

the region's democratic standards have declined since around 2008, slowing its integration into the EU. While the EU accession process continues to be the primary driver of economic and political reform, the road to EU integration is long and difficult. Bosnia and Herzegovina is still in the process of democratic transition and has significant governance deficits. As a result, state-building remains on the agenda, which is a matter of values as well as economic growth. The country is failing to achieve growth rates that are comparable to the average in the EU.

Although European Commission President Ursula von der Leyen has stated that it is in the EU's geostrategic interest to get as close to the Western Balkans as possible, Brussels is well aware of the destabilizing effects that enlargement could have. Premature accession risks causing a setback that could erode the EU's consensus on basic rule of law standards. Domestic issues have become even more pronounced, particularly in terms of corruption and organized crime. Given the enormous challenges of sustaining a neutral rule of law and public administration system over time, the new methodology prioritizes the fundamental aspects of state-building[42].

Despite its recent arrival, China is rapidly establishing its power in the Western Balkans. Unlike Russia, China cannot incite ethno-nationalist sentiments through history or culture. It is, however, making inroads with an economic footprint and investment potential that complicates accession processes for candidate countries and widens the economic gap in the Balkan region between EU and non-EU countries.

Since the Belt and Road Initiative's inception in 2013, China has funded a number of major infrastructure projects, including the Peljesac Bridge, which connects Croatia to its southern enclave around Dubrovnik, a high-speed rail link between Belgrade and Budapest, and highways in Montenegro, Northern Macedonia, Serbia, and Bosnia. China has loaned the Western Balkans more than €6 billion, primarily for energy and transportation. On the economic front, the Belt and Road Initiative provides new opportunities for trade development, which could assist the Western Balkans in breaking free from the middle-income trap. Upgrading energy capacity and filling critical infrastructure gaps could aid the region's economic recovery.[42]

The new economic and financial reliance on China, on the other hand, has two major implications for the EU enlargement process in the region. The first is a slowing or reversal of the overall reforms required for eventual EU membership. Tendering criteria for individual projects are highly opaque in China. In North Macedonia, a major political scandal erupted in 2015, when it was revealed that the government was about to award a major highway construction contract to a large Chinese state-owned company willing to pay bribes. With such practices, China not only makes it difficult to promote EU standards requiring transparency in public tenders, but it also exacerbates the region's widespread corruption problems.The same is true for Chinese loans, which can be more appealing than loans or grants from Western countries, which often come with strings attached. Compliance with EU environmental standards is also hampered

[42]Larsen, Henrik (2020) 'No. 263: The Western Balkans between the EU, NATO, Russia and China', CSS Analyses in Security Policy

by Chinese financing of power plants and factories.[42]

The second ramification is geopolitical. The fact that Chinese investments are purposefully focused on critical infrastructure and that the region's financially weak states accept Beijing's loans has long been a source of concern.If a borrowing country fails to meet its obligations, a Chinese state-owned company, and thus the Chinese government, could take over the infrastructure. China's heavy reliance on loans is just one aspect of the country's overall geoeconomic dependence. China's winning strategy of promoting the "17+1" cooperation format with 17 Eastern European countries implicitly makes the Western Balkans a group less likely to criticize Beijing on economic and other global issues on which the EU and NATO are attempting to reach agreement (including human rights, 5G providers and the coronavirus pandemic). Serbia has stronger security ties with China than any other country. Belgrade has used Chinese facial recognition technology, which may violate EU privacy laws. In the midst of a coronavirus pandemic, Belgrade also rejected the concept of European solidarity.[42]

Russia appears to have taken on the important role of opposing Western interests in the region. Obstacles to membership in NATO and the EU are viewed as opportunities to be capitalized on. While Russia does not regard the Western Balkans as a sphere of privileged interests comparable to Ukraine or the South Caucasus, it does have specific geopolitical interests in the region, which are bolstered by historical ties with Orthodox Serbs. The Western Balkans are fragile countries on Europe's outskirts, where Russia can project power by federating local opposition to the region's further integration into NATO and the EU.

The continuation of the conflict, according to Moscow, is the most effective way to stymie NATO integration and slow EU accession processes. Russia has maintained a close relationship with the Republika Srpska (Bosnian Serb Republic) and its president, Milorad Dodik, who is attempting to foster ethnic identity in opposition to the Bosnian state, which is eager to join NATO. Russia is also using public diplomacy to bolster its pan-Slavic/Orthodox identity with Serbia and the Republic of Srpska.

Unlike the EU and NATO, Russia has the advantage of being unencumbered by values in its relations with the region's leaders in the short term. Nonetheless, it is critical to recognize Moscow's influence limits, particularly in the economic sphere. While Russia is an appealing prospect for politicians seeking to strengthen their power through identity politics, it is not a replacement for the EU's soft power. Even in the Republika Srpska, leaders and citizens see EU membership as a positive goal. Aside from its obstructive and acquisitive tactics in strategic sectors (energy, heavy industry, and banking), Russia does not provide a long-term solution for the region. It has been successful in its endeavor to support local opposition to NATO enlargement in Serbia and Bosnia.[42]

The conflict between the various external actors has demonstrated to local elites the importance of enlisting Russian and Chinese assistance in softening the conditions imposed by NATO and the EU. NATO can do without the missing puzzle pieces of Serbia, Bosnia, and Kosovo, even if this is largely due to Russia's obstructionist policy and ne-

cessitates the presence of stability-keeping forces, which have been harmed by Ukraine's declaration of war. The question is whether the EU is willing to accept that the country may not meet EU membership criteria while still contributing to local stability through economic and financial instruments.[42]

The EU continues to benefit from its geographical location as well as the allure of the European way of life. As a result, it is impossible for the local elites to be officially opposed to Union integration. The issue with the EU is that low expectations and slow reforms undermine the candidate country, creating a vicious circle. At this rate, it will take several decades for the region's states to meet the criteria for effective membership. This issue is addressed by the EU's new accession methodology, which is divided into six thematic clusters.Drawing public attention to situations in which a lack of political will is impeding the achievement of medium-term goals may help to generate the necessary political momentum. This is especially true for the rule of law, which is constantly threatened by undue interference and will necessitate constant monitoring until accession.

The presence of China in the region is forcing the EU to consider how to remain appealing to unconditional investment. The coronavirus-caused recession may encourage poorer countries to accept more Chinese investment.Indeed, Beijing finds it easier to implement infrastructure projects in these countries than in EU Member States, which receive more funding from EU institutions and are required to follow EU legislation on public tenders. When loans are not compatible with EU debt ceilings, EU regulations impose bottlenecks on Chinese investment. Non-member countries have fewer resources available to them from the EU. In short, the EU has more funding available for the country, but this funding is spread across a wide range of public and private sectors. China, on the other hand, has the ability to disburse funds more quickly and focuses on critical infrastructure. Furthermore, the new accession methodology improves support for candidate countries.[42]

The EU will now be able to reward them for the reforms they have implemented by providing additional funding and gradually integrating them into the European market.

In some ways, the competition in the Western Balkans between the EU and China is more intense than the more static competition between NATO and Russia. The EU's attempt to discourage new economic reliance blurs the distinction between accession and pre-accession. If the EU does not compromise on the criteria for closer integration, this strategy may be viable.

Part III
Current Investment Climate

4 Current FDI in Bosnia

In the context of FDI, Bosnia and Herzegovina possesses many comparative advantages. For example, one could name openness to FDI, a well-educated workforce, competitive labour costs, easy access to and affordability of energy, well-developed industrial banking sector, strategic location, low levels of taxation on businesses and preferential trade access to major European consumer markets.

Through its reforms Bosnia and Herzegovina has achieved progress in improving its business environment and creating a favorable legislative and institutional environment to support more efficient economic and financial activities. Nevertheless, investments in the country remain low mainly due to complex legal/regulatory frameworks, dual government structure and non-transparent business procedures[43].

The multiple layers of Bosnia and Herzegovina's political and institutional structure is a core challenge to the investment environment in the light of complex regulatory frameworks, in particular the lack of harmonization between national and entity laws. Bosnia and Herzegovina enacted the Law on Policy of Foreign Direct Investment which lacks clearness and preciseness, so it leaves a lot of room for interpretation.

The main investment partner countries are Austria, Croatia, Serbia, Slovenia, Germany, Netherlands, Italy, United Kingdom, Russia, Switzerland and other. They have strong historical and economic ties to Bosnia and Herzegovina, since they have come to learn how to navigate the domestic administrative hurdles that stem in large part from the country's highly decentralized government and public administration. However, investors face significant regulatory obstacles related to business registration, licensing and permitting which, if modernized, would provide incentives for investment. Another weaker field related to foreign direct investment is the promotion of benefits of Bosnia and Herzegovina, particularly in terms of domestic manufacturing and employment. Currently, what is impeding promotion of this type is the absence of strategic guidelines, including clear FDI objectives, as well as policy guidance to the investment promotion authorities of Bosnia and Herzegovina[44].

To promote FDI, Bosnia is working on various policy reforms that address key regulatory and promotional efforts, harmonization of business procedures are essential for Bosnia and Herzegovina to unlock its untapped potential to attract foreign direct investment (FDI) and help the country to achieve its development goals.

[43] Bosnia and Herzegovina - United States Department of State. (n.d.). Retrieved April 19, 2022, from https://preview.state.gov/reports/2021-investment-climate-statements/bosnia-and-herzegovina/

[44] Hodzic , S. (2013). Foreign Direct Investment Regulations: Comparison between Bosnia and Herzegovina and India (thesis). Retrieved from: https://www.etd.ceu.edu/2013/hodzic_seid.pdf

4.1 Investment Statistics

Foreign direct investment in Bosnia and Herzegovina has been growing despite the COVID-19 pandemic. The stable amount of foreign direct investment in 2020 stimulated by reinvestment and a significant increase in the first nine months of 2021 confirm the expected increase of FDI in Bosnia and Herzegovina. BiH's FDI registered a growth equal to 3.0 % of the country's Nominal GDP in Sep 2021, compared with a growth equal to 4.7 % in the previous quarter. According to UNCTAD's 2021 World Investment Report, FDI inflows amounted to USD 371 million in 2020, down from USD 400 million in the previous year. The total stock of FDI was estimated at USD 9.4 billion in 2020[45].

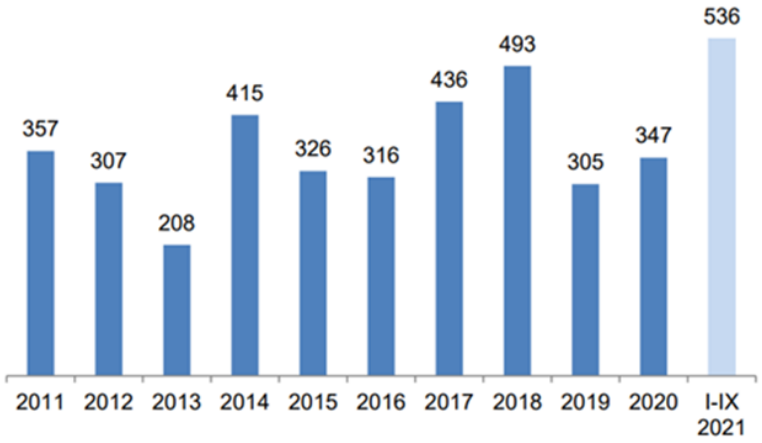

Figure 3: Flow of FDI in Bosnia and Herzegovina, million EUR[46]

In 2007 BH attracted 1.3 billion EUR that is the highest amount recorded until nowadays, mainly due to the privatization of certain large state-owned enterprises. In 2008 FDI inflow (684 million EUR), could be considered as satisfying, especially if we consider its positive nature (Investment in production sector and high contribution of Greenfield investments).

Later, the global economic crisis led to a significant decrease of foreign investments in 2009. In the period from 2010 to 2020, the trend of FDI inflows is variable and unequal. The annual average inflow of FDI for the previous five years was 379 million EUR and the largest annual amount of FDI in the mentioned period was registered in 2018.

After the decline in 2019, there was a positive increase in 2020 by 13.7%. According to the Central Bank of BiH, investment inflows at that time could be considered

[45]Bosnia and Herzegovina foreign direct investment: % of GDP. Bosnia and Herzegovina Foreign Direct Investment: % of GDP, 2008 – 2022 — CEIC Data. (2021). Retrieved from https://www.ceicdata.com/en/indicator/bosnia-and-herzegovina/foreign-direct-investment–of-nominal-gdp

[46]Central Bank of BH (CBBH), January 2022

as positive, given the deep global recession that affected the ability of foreign investors. However, most investments were reinvested earnings from existing companies with foreign investment, while investments in the form of ownership shares were much lower.

According to the primary data from the Central Bank of BiH within FDI flows, with estimated reinvested earnings, for the period January - September 2021, foreign direct investments amounted to 536.1 million EUR (or 1,048.7 million BAM). FDI increased by 65% compared to the same period last year and the amount is also higher than the annual amounts in the previous ten years[47].

4.2 Largest Investors

The largest investors in Bosnia and Herzegovina are Austria, Croatia, Serbia, Slovenia, Germany, and the Netherlands. Top investor countries in BiH for the period of May 1994 - December 2020 (Total amount 7.7 billion EUR) are displayed below:

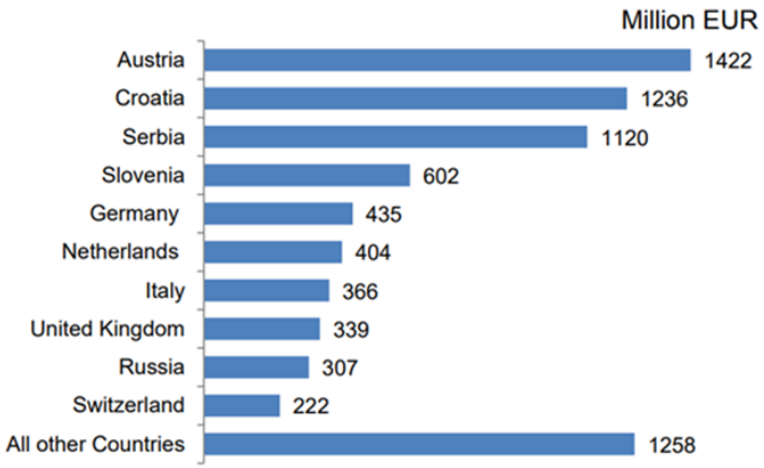

Figure 4: Top investor countries in B&H, May 1994 - December 2019[48]

Later, the main investor countries in BH in 2020 were Croatia (76.4 million EUR) and Serbia (69.2 million EUR). The following countries also registered significant capital increases: Germany (39.6 million EUR), United Kingdom (38.5 million EUR), Austria (36.5), Slovenia (36.5), Turkey (28.1) and Italy (19.0 million EUR).

In the first nine months of 2021, the countries with the largest registered amounts of capital in Bosnia and Herzegovina were: Croatia (142.5 million EUR), Austria (85.9 million EUR), Russia (67.7 million EUR) and Slovenia (67.5 million EUR)[49].

[47] FIPA - Foreign Investment Promotion Agency of Bosnia and Herzegovina. (2022, January). FDI position and performance - FIPA.GOV.BA. FDI Position and Performance. Retrieved from http://www.fipa.gov.ba/informacije/statistike/investicije/FDI%20Position%20and%20Performance_January%202022_E.pdf

[48] Central Bank of BH (CBBH), January 2021

[49] Žíla, O. (2018, July 29). "Arabic" ilidža: The only "multicultural" quarter of Sarajevo? Domů. Retrieved from https://ims.fsv.cuni.cz/arabic-ilidza-only-multicultural-quarter-sarajevo

Along with that, Bosnia and Herzegovina has become a favored destination for Arab tourists and investors as well. Almost 50 % of Arab visitors come from Kuwait, the rest arrive to Bosnia from other Arab countries (the United Arab Emirates, Qatar, Oman, Bahrain, Saudi Arabia, etc.)[50]. However, apart from the beautiful and untouched landscape, the fresh mountain air and clean water which attract Arab investors, some say that the reasons for some of these investments are far less innocent. Firstly, it is not clear where these finances are coming from. Secondly, the state is not capable of thoroughly controlling all the financial influx connected to Arab investors. Thirdly, since Bosnian law does not allow foreigners to buy directly, large companies registered in Bosnia purchase real estate and then officially rent them out for a lengthy period, or small companies are set up with the only purpose being that of buying real estate. The Bosnian public heavily criticizes the uncontrolled selling off land that is in possession of the municipality and the financial machinations. According to the latest inspection, 700 companies, 300 of which were found not to exist, and 16 tourist resorts across all of Bosnia[51].

Notably, a Dubai-based property developer sees the area of Trnovo - home to part of the 1984 Sarajevo Winter Olympics - as a prime location to realize Bosnia's biggest ever foreign investment: Buroj Ozone City. The planned holiday city of 40,000 people will include private villas, luxury hotels, a shopping mall, and a hospital. Its construction will cost a reported 4.5 billion Bosnian Marks (BAM) ($2.5bn; £2bn) and it should be completed by 2025. But the gigantic size of the project – equating to 15% of Bosnia's GDP- is triggering some concerns among locals. The builders of the property expect the project to help increase tourism and investment in Bosnia, create thousands of jobs, and result in "a full city with full facilities for everything". They claim that properties will be accessible to Bosnians as well, with prices for private villas starting at BAM 2,300 ($1,300) per square meter. However, as the monthly wages in BiH are on average $475 (837 BAM), it is quite abstract to imagine many locals being able to afford those properties.[49]

In addition, Sarajevo's Ilidža is known for being an important transport hub, a spa district with an Austro-Hungarian atmosphere and a beautiful promenade leading to the springs of the river Bosna. These are the most common associations among Bosnians when it comes to this quarter, located at the outskirts of the capital city. Yet recently, any reference to or debate about Ilidža in Bosnia has been almost exclusively concerned with newcomers from the Arab world and their foreign investments.[49] Bosnians say their concerns are mainly economic. They fear that Arab buyers will dominate the property market and drive-up prices for Bosnians and that a big number of Bosnians will be working for wealthy Arabs. For example, Bosnians see Ilidza as an Arab enclave. Street signs now offer all sorts of business services in Arabic language: real

[50] Gulf nations investment in Bosnia raises radicalism concerns. Gulf nations investment in Bosnia raises radicalism concerns - Bosnia Herzegovina - ANSAMed.it. (n.d.). from https://www.ansamed.info/ansamed/en/news/nations/bosniaherzegovina/2016/12/06/gulf-nations-investment-in-bosnia-raises-radicalism-concerns$_{e}$c29ad0a − 97a9 − 4261 − b3e3 − 9e6a3dab2514.htmlhttps : //d.docs.live.net/c1cf6d220564e247/Documents/Newest%20version.docx$_{f}$tn5

[51] Brunwasser, M. (2016, September 22). Bosnia's biggest foreign investment: Bonanza or threat? BBC News. Retrieved from https://www.bbc.com/news/business-37429682

estate, restaurants, dentists, travel agencies and souvenir shops[52].

4.3 Sectors

These include traditional industries where the country retains know-how from the Yugoslavian era, including metal and wood processing, but also other sectors such as agro-processing, textiles, and services. Indeed, several factors make the country an attractive destination for investment. For the period of May 1994 - December 2020, out of total foreign direct investments, 35% were invested within the production (primary, industrial and electricity production), followed by the banking sector with 24%, trade 14% and telecommunications 12% as presented by the graph below:

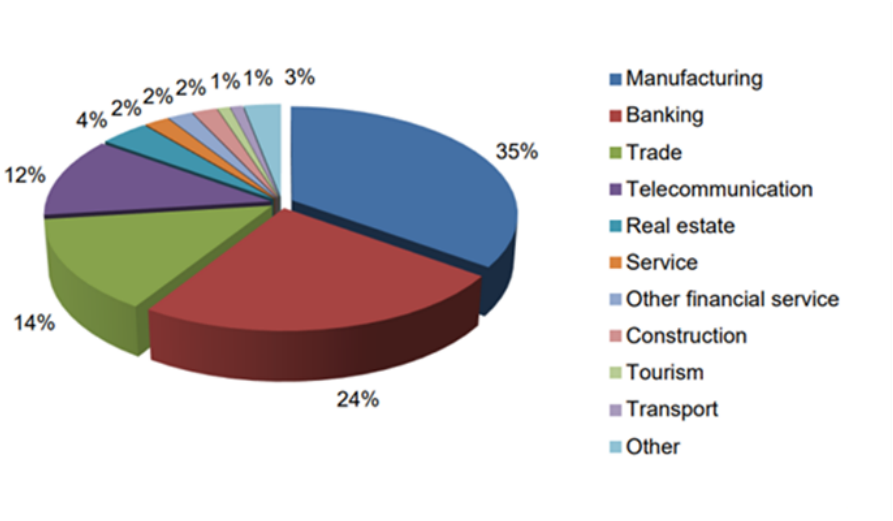

Figure 5: FDI Stocks by Industry (%), May 1994 - December 2020[53]

Later, the biggest shares of FDI in 2020 were distributed as follows: Financial service activities – banking (80.3 million EUR) and followed by: Wholesale trade (48.0), Electricity, gas, steam, and air conditioning supply (45.3). Significant capital increases has been registered also for: Retail trade (21.9), Real Estate (21.4), Manufacture of chemicals and chemical products (19.3), Mining of metal ores (16.4), manufacture of motor vehicles, trailers, and semi-trailers (15.7) and Manufacture of food products (14.1 million EUR).

For the first nine months of 2021 the most attractive investment areas were: Financial service activities, except insurance and pension funding (158.9 million EUR), Retail trade, except of motor vehicles and motorcycles (85.2), Manufacture of coke and refined petroleum products (67.7 million EUR) and Wholesale trade, except of motor vehicles and motorcycles (52.0 million EUR)[54].

[52]FIPA - Foreign Investment Promotion Agency of Bosnia and Herzegovina. (2022, January). FDI position and performance - FIPA.GOV.BA. FDI Position and Performance. Retrieved from http://www.fipa.gov.ba/informacije/statistike/investicije/FDI%20Position%20and%20Performance_january%202022_E.pdf

[53]Central Bank of BH (CBBH), January 2021

[54]empty

5 Legislative Framework for FDI

5.1 Domestic Investment Legislation

The domestic legal framework in Bosnia and Herzegovina, particularly the Law on Policy of Foreign Direct Investment, does not pose restrictions to FDI entry, except investments in some sectors such as defense industry, some areas of publishing and media and electric power transmission. Besides them, foreign investors are entitled to invest in any sector of the economy in the same form and under the same conditions as those defined for residents.

Further, under the Law on Policy of Foreign Direct Investment foreign investors have the rights to be treated "in the same form and under the same conditions" (Article 3) and have the "same rights and obligations as the residents" of Bosnia and Herzegovina and businesses "shall not be discriminated in any form" (Article 8). Moreover, foreign investors have the right to open foreign currency accounts in any bank in Bosnia and Herzegovina and make transfers abroad freely.

There is an obstacle passed in the following provision. Article 15 states that "rights and benefits of foreign investors granted, and obligations imposed, by this law cannot be terminated or eliminated by the laws and regulations passed later." The article continues by stating that investors "shall have the right to choose under which regime the respective investment will be governed". However, this choice is not provided to domestic investors, therefore creating a discriminatory dual regulatory regime[55].

5.2 International Investment Agreements

Bosnia and Herzegovina has signed 39 Bilateral Investment Treaties which cover most of its network of investors. Excluding six BITs, the treaties clarify that investments must be regulated in accordance with local legislation[56]. Further, a large part of those treaties also includes individuals who qualify as permanent citizens of the other contracting party under its domestic laws. Moreover, the majority of BITs provide national, fair and equitable treatment, and protection from expropriation.

Besides BITs Bosnia and Herzegovina has signed five other international agreements:

a. the preferential trade agreement with EFTA

b. the Stabilization and Association agreement with the European Union

c. the CEFTA

d. the Energy Charter Treaty

[55]Bosnia and Vina - UNCTAD. (n.d.). page.10, Retrieved from https://unctad.org/system/files/official-document/diaepcb2015d1_en.pdf

[56]Towards a new generation of investment policies: UNCTAD'S investment policy framework for sustainable development. Investment Treaty News. (2019, June 27). Retrieved from https://www.iisd.org/itn/es/2012/10/30/towards-a-new-generation-of-investment-policies-unctads-investment-policy-framework-for-sustainable-development/

e. the bilateral preferential trade agreement with Turkey

Some provisions in the abovementioned agreements could be added to strengthen their sustainable development scope. Such provisions could be in the light of a) more detailed obligation clauses and b) stronger investment promotion provisions. A model BIT can serve as an example for reviewing the provisions. For example, the following framework:

Investment Policy Framework for Sustainable Development (IPFSD) launched by UNCTAD on 12 June 2012, provides policymakers with concrete options for placing inclusive growth and sustainable development at the heart of efforts to attract and benefit from foreign investment. In so doing, the framework aims at creating synergies between investment policies and wider economic development goals; promoting the integration of investment policies into development strategies; fostering responsible investment and incorporating principles of Corporate Social Responsibility (CSR); and ensuring policy effectiveness in the design and implementation of investment policies. Bosnia and Herzegovina could use the framework as a key point of reference in formulating national investment policies and in negotiating or reviewing IIAs[57].

6 Business Regulation

6.1 Business registration process

Business registration is arduous in Bosnia and Herzegovina but there are already reforms taking place to facilitate the procedure. BiH still ranked 184th out of 190 countries in the "starting a business" sub-index of the World Bank's 2020 Doing Business report. It takes 13 procedures and 80 days, and costs 13.7% of GNI per capita with starting capital of 10.2% of GNI per capita to start a business[58].

The business registration is regulated in accordance with the Framework Law on Registration of Business Entities in Bosnia and Herzegovina.[58] Another positive act is the creation of a centralized business registry, which ensures transparency and access to public information.[58]

Certain procedures still need to be simplified to reduce time and cost of business registration. For example, information sharing between public administrations can be streamlined to improve the procedures. Another example of a necessary step when applying for registration is providing a certificate of zero outstanding debts. This required the participants to obtain a document from the Registry of Fines which can take up to seven days. Furthermore, company stamps are still used in BiH. As they are not mandatory in most of the countries in the European Union, electronic signatures could be better adopted instead. In addition, the involvement of notaries in the registration processes could be reduced. Republika Srpska has already implemented changes in the number of procedures and documents required for verification from a notary. Allowing for investors

[57]BTI 2022 Bosnia and herzegovina country report. BTI 2022. (n.d.). Retrieved - https://bti-project.org/en/reports/country-report/BIHpos0

[58]Framework law on registration of Business Entities of bih. (n.d.). Retrieved from https://advokat-prnjavorac.com/legislation/Framework-Law-on-Registration-of-Business-Entities-of-BiH.pdf

to choose whether to need a notary in the process of their business registration is usually considered a good practice[59].

6.2 Licenses and permits

Due to its peculiar administrative division, the procedures for obtaining business licenses and permits requires involvement of more than one level of government. Such complex structure leading to confusion and overlap of responsibilities. Depending on the type of license, it could be issued by the entity, the canton, or the municipality and sometimes a consent from all three would be required. The efficiency in terms of regulating those licenses can vary across the different levels. As local administration has discretionary power, it can leverage the complexity of the system and delay licensing for certain investment projects.

Construction permits are still a great obstacle in the country especially in the light of time and cost it takes to obtain one. For example, to start a construction, the applicant must obtain the approval of the municipality, the cadaster, the land registry, local utility services, the Institute for Protection of Monuments. This process could take months. No entity has a supervision over the entire process and therefore the completion of a construction project depends on the cooperation of the institutions[60].

6.3 Inspection

There were some significant improvements in terms of consolidation of inspection bodies. The Federal Administration for Inspections was established in 2007 and is responsible for coordinating the work of 10 units. Likewise, Republika Srpska's inspection body was established in 2006 and is responsible for the coordination of 13 inspection units. In both entities, fiscal inspection bodies remain separate. Funded by USAID, the administrations introduced standardized inspection checklists and automated Inspection Management System (IMS) that collects data, thus facilitating inspection coordination. As a result, business inspections have been reduced by half or more as well as overlaps and duplications of jurisdictions were clarified as well as better detailed rules were established.

However, it still happens that investors are subject to repetitive inspections from different levels of the government. The division of labor among inspectors is not always clear and not entirely properly communicated to the businesses either. Furthermore, instead of mainly focusing on confronting and imposing fines on businesses which have failed to comply with the laws and regulations, the government could provide better coordinated guidance to help investors to avoid infringements and comply with the law[61]. One way would be to introduce a Business Ombudsman Institution with the aim to defend businesses and entrepreneurs with legitimate claims against state or sub-state entities that

[59] Registar poslovnih Subjekata. (n.d.). Retrieved from https://bizreg.osbd.ba/

[60] Bosnia and Vina - UNCTAD. (n.d.). page.11, Retrieved from https://unctad.org/system/files/official-document/diaepcb2015d1$_e$*n.pdf*

[61] Bosnia and Vina - UNCTAD. (n.d.). page.14, Retrieved from https://unctad.org/system/files/official-document/diaepcb2015d1$_e$*n.pdf*

infringe on their rights[61].

6.4 Taxation

Bosnia and Herzegovina has implemented attractive corporate income taxes. The general rate is 10 percent across the country. Although tax rates are attractive and incentive schemes are in place, Bosnia and Herzegovina's tax administration appears to be quite complex due to the different provisions and interpretations of entity law. For example, in the Federation of Bosnia and Herzegovina and Brcko District, the taxable base is determined by the International Accounting Standards (IAS), while in Replublika Srpska it is not.

VAT refund in Bosnia and Herzegovina is standard. Taxpayers can claim a refund or a tax credit if the amount of input tax is paid (VAT) than the amount of output tax liability. However, there are some discrepancies and difficulties understanding the provisions related to non-residents eligible for a VAT refund. The concerns are mainly raised in the private sector claiming that the definition of non-residents is not precise enough therefore leaving the ITA to rely on a non-exhaustive list of legal entities to refunds that excludes individuals[62].

Furthermore, there is some confusion between taxpayers in terms of how these issues are addressed by the Indirect Taxation Authority (ITA) as they appear inconsistent and lack transparency. Apart from being lengthy, these opinions are also not made publicly available which prevents taxpayers from referring to precedence established in previous cases.

Bosnia and Herzegovina provides access to free trade zones where any commercial, industrial, or service activity which does not endanger the environment, public health, property, or national security are allowed. There are only four FZs, all in the Federation of Bosnia and Herzegovina, Vogošća (Sarajevo), Holc (Lukavac), Herzegovine (Mostar) and Visokov (Visoko). Exemption from VAT is one of the benefits that is offered to companies in the Free Trade Zone. Despite the attractiveness of the free zones, FDI in them remains low. There are several reasons for this. Due to the interim trade agreement with the European Union, tariff rates on most imports are minimized and the incentive to operate under FZs has declined. Some investors also claim that the customs and tax exemptions are not honored in practice, including the exemption from VAT. In particular, companies which export more than 30 percent of their annual turnover are exempted from tax which contradicts with the idea of the free zone. Finally, given that the country is in the process of accession to the WTO it will have to abolish this tax on export in order not to violate the SCM Agreement of the WTO[63].

[62]Business Ombudsman Initiatives. European Bank for Reconstruction and Development (EBRD). (n.d.). Retrieved from https://www.ebrd.com/what-we-do/sectors-and-topics/business-ombudsman-initiatives.html

[63]IMF country report no. 15/299 Bosnia and Herzegovina. (n.d.). Retrieved from https://www.imf.org/external/pubs/ft/scr/2015/cr15299.pdf

6.5 Labour regulations

Although the Labour Code of Bosnia and Herzegovina and Republika Srpska contain a big part of the principles established under Yugoslavian law, they have evolved and changed ever since.[63] Discrepancies in labour legislation and its implementation occurs even only in one entity, as in the Federation of Bosnia and Herzegovina there is no inventory of the labour and employment legislation enacted by the cantons, therefore making it difficult to measure the compliance with entity-level regulation. As a result, this hampers investors from abiding correctly to the labour legislation, especially if they operate in more than one canton[64].

Contradictory Labour regulations can also be a heavy obstacle for FDI. There are different laws between the different entities in Bosnia and Herzegovina which need to be harmonized to avoid discrepancies and disputes. For example, this concerns businesses which operate in more than one entity and need to comply with all the regulations. Moreover, the informal sector (estimated to account for 30% – 50% of GDP) provides a vast number of unregistered jobs and heavily distorts market-based competition as well as official unemployment data. Overall, the extensive state intervention in the economy and the semi-formal/informal control that political elites exert via the huge informal sector means that only a very limited segment of the private sector (mostly in the Federation of BiH) functions primarily on a market-economic basis. Further, labour disputes which are later settled in courts which is often a lengthy and costly process, creating legal uncertainty which tends to be seen as negative for businesses when evaluating worker's protection[65].

7 Impact of Russian Aggression

The war in Ukraine started in February 2022 adds major uncertainties to foreign direct investment (FDI), presenting new challenges for Bosnia and Herzegovina just as it rebounded from the Covid-19 crisis. Prospects for economic activity are further affected by domestic tensions and lack of consensus on reforms to enhance the integration of the economy internally and with international markets[66].

Additional political tensions are created by the Bosnian Serb entity which wanted to "maintain neutrality" when it came to Russia and Ukraine and was against sanctions against Russia. Republika Srpska representatives in Bosnian institutions should vote against the imposition of sanctions against Russia, according to another of the parliament's conclusions at the June 6, 2022, session.

The outlook is highly uncertain as most of the consequences will depend on the position Republika Srbpska decides to maintain and the severity of the potential sanctions

[64]The labour law - ilo.org. (n.d.). Retrieved from https://www.ilo.org/dyn/natlex/docs/ELECTRONIC/54990/94734/F1498928730/BIH

[65]Employment Policy Review - Bosnia and Herzegovina. (2008). Retrieved from http://www.oit.org/wcmsp5/groups/public/—europe/—ro-geneva/—sro-budapest/documents/publication/wcms$_1$68761.*pdf*

[66]Bosnia and Vina - UNCTAD. (n.d.). page.16, Retrieved from https://unctad.org/system/files/official-document/diaepcb2015d1$_e$*n.pdf*

and countersanctions. For years, Bosnian Serb leader Milorad Dodik has spoken of the independence and secession of Republika Srpska, territorially half of the Republic of Bosnia and Herzegovina. It is in Republika Srpska that the 'Ukrainian scenario' is most likely, where Bosnian Serbs can declare independence and be helped by Serbia or Russia itself, seeing the area as an opportunity to open a front against the West. In the case of Bosnia and Herzegovina, Russia has considerable influence in Republika Srpska[67].

Nonetheless, the most immediate economic impact of the war is the large increase in food and fuel prices, which is already hitting many households and firms and will last for some time. Although direct economic ties with Russia and Ukraine are limited, BiH's economy is vulnerable to rising commodity prices, slower economic growth in Europe, and tighter financial conditions because of the war. Domestically, political tensions, including regarding the role of state-level institutions, have paralyzed reforms, and weighed on investor sentiment. With high uncertainty, the International Monetary Fund expects growth to moderate to $2\frac{1}{2}$ percent this year and average annual inflation to accelerate to 6.5 percent. Delays in government formation after the October general elections could further affect economic prospects, while the potential emergence of new Covid variants poses another risk[68].

On a positive note, the expansion saw Slovenia-based poultry producer Perutnina Ptuj, a subsidiary of Ukraine-based agricultural produce company Mironivsky Hliboproduct, announce that it was investing $2.3m in new production capacities in 2020 in its operations in Bosnia-Herzegovina, in a bid to boost its exports. Additionally, the UK ranked as the top country for attracting greenfield Foreign Direct Investment projects from Ukraine in 2019 and 2020, with three projects. Right behind are Germany and Bosnia-Herzegovina that attracted two projects each. The industries attracting the two projects in Bosnia and Herzegovina are meat products and water collection, treatment, and supply[69].

[67]Service, R. F. E. R. L. B. (2022, June 7). Bosnian Serb leader says secession plan delayed by war in Ukraine. RadioFreeEurope/RadioLiberty. Retrieved from https://www.rferl.org/a/31886186.html

[68]Bosnia and Herzegovina: Staff concluding statement of the 2022 Article IV Mission. IMF. (2022, March 25). Retrieved from https://www.imf.org/en/News/Articles/2022/03/25/bosnia-and-herzegovina-staff-concluding-statement-of-the-2022-article-iv-mission

[69]Karadima, S., Sofia Karadima. In which countries and sectors has Ukraine's FDI activity been directed? Investment Monitor. Retrieved from https://www.investmentmonitor.ai/special-focus/ukraine-crisis/ukraine-fdi-activity-conflict-invasion-investment

Part IV
Survey of Existing SMs Options

In the light of art.70 of the SAA with Bosnia and Herzegovina, pursuant to which *"Bosnia and Herzegovina shall endeavour to ensure that its existing laws and future legislation will be gradually made compatible with the Community acquis"*, the EU framework on SMs will be analyzed. Moreover, in the second subsection the SM laws of some select EU and non-EU countries will be looked into in order to highlight some specificities which may help the Bosnian legislator in setting up a SM.

8 European Standards for FDI Screening Mechanism

After the wave of foreign acquisitions in the EU market taking place in 2016, many MSs were worried about the lack of reciprocity and possible sell-out of European expertise[70]. This concern prompted to build on failed negotiations on an European framework on SMs of FDI back in 2013 and led to the adoption of the SM Regulation. The European Commission (hereinafter, either "EC" or "Commission") in its first report[71] on the application of the SM Regulation pursuant to art.15 thereof, noted that following its entry into force only 3 MSs did not, at least, engage in a public debate over adopting a SM. Furthermore, the Commission also recognised that 80% of the screened investments were cleared without conditions and 80% of the notified screenings were closed by the EC itself in the Phase 1 of the cooperation mechanism[72]. These data explain the attractiveness of the EU for FDIs.

8.1 Overview

Under art.207(1) of the TFEU, the common commercial policy, included within the exclusive competences of the EU pursuant to art.3(1)(e) TFEU[73], shall extend to *"foreign direct investment"*. On this basis,, the SM Regulation was enacted[74].

Notwithstanding the EU exclusive competence, several provisions in the founding Treaties of the EU[75], as recognized by art.1(2) of the Regulation, allow for Member States (hereinafter, if not cited, MSs) to adopt measures *"which they retain necessary to defend essential interests of its security"* and *"maintenance of public order"*. Therefore, the Regulation, legal instrument which is binding and directly applicable under art.288 TFEU, *"establishes a framework for the screening by Member States of foreign direct investments"* (art.1(1)). Therefore, the responsibility of carrying out proceedings and

[70] L. Carcy, The New EU Screening Mechanism for Foreign Direct Investments: When the EU takes back control, page 6, which can be retrieved at http://aei.pitt.edu/103426/1/wp84_carcy.pdf (last accessed 04/20/2022 at 12.52pm)

[71] https://trade.ec.europa.eu/doclib/docs/2021/november/tradoc_159935.pdf, (last accessed 04/20/2022 at 12.52pm

[72] see the note above, Chapter 2. Phase 1 means without opinions by the EC or comments by other MSs

[73] "only the Union may legislate and adopt binding acts" (art.2(1) TFEU)

[74] See having regard no.2, which refers to art.207(2) TFEU

[75] Arts. 4(2) TEU, 346(1)(b) TFEU, which also allow for intra-EU limitations of capital movement

making decisions as to this matter lies exclusively within National Governments, thus respecting the above-mentioned provisions by making sure that their sovereign powers do not conflict with EU law[76].

In principle, since the SMs derogate from a fundamental right[77], the case law of the Court of Justice of the EU (hereinafter, CJEU) states that the grounds for their application must be interpreted strictly[78]. Furthermore, the limitations are subject to the principle of proportionality, therefore these measures must ensure the attainment of a legitimate interest and shall not exceed the least restrictive mean among the equally effective ones[79]. These principles have to be held as valid; however, following the adoption of the Regulation, this piece of legislation itself lays down the conditions for the limitations to the exercise of a fundamental right, provided that it is compliant with the founding Treaties[80].

The next section will explain how the procedure laid out by the Regulation for an effective cooperation of every subject of EU law, thus ensuring the consistency and lawfulness of SM decisions, also taking into account the fact that a FDI in one of the MS paves the way for the access to the Single Market and hence to other MSs' economies, thus potentially affecting their security and public order.

8.1.1 EU requirements for Member States' screening mechanisms

The procedure and final decision of the SM is subject to some procedural requirements. This section examines judicial review and procedural duties the State that apply to to protect the primacy of EU law. As to judicial remedies, art.3(5) of the Regulation enshrines the right to a recourse to national Courts. It should be read in conjunction with art.19(1) TEU and the interpretation thereof given by the Court of Justice of the EU (hereinafter, CJEU), therefore as granting the right to an effective review (capable of granting tutelage to rights, like annulment and redress) to challenge the legality of a measure in front of an impartial Court[81].

The "cooperation mechanism" (hereinafter, "CM") is established and regulated by arts.6 and following the Regulation. First, for any SM a MS puts in place, the MS must notify the Commission of their adoption and subsequent amendments thereto (art.3(7)). Second, the CM applies to FDIs undergoing screening (art.6) and those who are not undergoing screening (art.7). In relation to those under review, the MS in which the investment takes place shall notify the EC and other MSs and provide the information

[76] See also section 8.1.1 and 8.1.2

[77] See below in the section 8.1.2

[78] CJEEC, W. J. G. Bauhuis v The Netherlands State, C-46/76, §2.

[79] CJEU, NL v Direcţia Generală Regională a Finanţelor Publice Bucureşti, C-679/19, §28. See also art.52 of the Charter of the Fundamental Rights of the EU

[80] As it will be seen below, this condition is satisfied. In order to understand this concept, think about art.7(1)(b) of Directive 2004/38/EC which conditions, pursuant to art.21(2) TFEU, the right of residence (for more than 3 months) of EU citizens in other MSs other than the one whose they are nationals under art.21(1) TFEU to the possession of " sufficient resources for themselves and their family members not to become a burden on the social assistance system of the host Member State during their period of residence". Hence, secondary legislation, just like national law vis-à-vis constitutional rights, may further specify conditions under which a right may be exercised or restricted lawfully, also in respect of other conflicting interests and values.

[81] CJEU, Associação Sindical dos Juízes Portugueses, C-64/16, §31

listed in art.9(2) "without undue delay" (art.9(1)), and a list of other MSs whose security or public order may be affected. Furthermore, information must only be used for the purpose for which it was requested (art.10(1)) and processed in compliance with Reg.2016/679/EU (General Data Protection Regulation, also known as GDPR) and national law (arts. 10(2) and 14). Another MS that considers that said investment is likely to affect its security or public order may provide comments.

The Commission may only issue an opinion if another MS' comments or, in absence of comments, if it is either likely to affect security and public order in more than one MS or has relevant information in relation to it. Both comments and opinions must be justified and the intention to provide or issue them must be notified within 15 days from the receipt of the above-mentioned notification and can also be accompanied for a request of additional information, which must be itself justified and strictly necessary. In any case, the comment/opinion must be delivered within 35 days[82]. In order for this mechanism to apply, each comment/opinion (and request of information) is notified to both the EC and the State in which the FDI takes place.

As regards art.7, the CM is analogous[83]. In compliance with the duty of cooperation under art.4(2) TEU, the Member State *"shall give due consideration to comments and opinions"* (arts. 6(9) and 7(7)), therefore they may be taken into account in framing the clearance or prohibition of the FDI screened. Notwithstanding this principle, it is reaffirmed that the MSs are empowered to take the final decision as to permitting or forbidding the investment pursuant to its legislation. In this matter, the metaphor of "MSs still at the helm"[84] can help understand how this framework works.

Article 11 requires that contact points, which are institutions part of the Government screening FDIs entrusted with the task to ensure the effectiveness of the CM[85], be established by national SMs laws. Through contact points MSs and the EC can exchange information pursuant to the above-mentioned articles via an encrypted system provided for by the Commission.

Eventually, a special law applies to investments likely to affect programs of Union interest listed in Annex I (art.8), which can be amended by a delegated act of the EC in compliance with art.16, cooperation with third countries is not forbidden (art.13) and the Commission must issue a report on the application of the Regulation every five years (art.15).

In the following section the substantive provisions of the Regulation, the ones the above-

[82]For a special regime governing the opinions by the Commission following comments by other Member States, see art.6(7) subparagraph 3. There may also be "exceptional cases" which "require immediate action", which must be justified and allow for comments and opinions to be issued "expeditiously" (art.6(8)).

[83]The sole divergent aspect is that opinions and comments must be expressed within 15 months from the completion of the investment. This can be easily explained by pointing out that there is no decision and hence no need to grant an expeditious answer to the investor. In addition, there is no notification of the investment, since it does not undergo screening.

[84]See note 70, page 6. But at the same time it is noted that "Commission powers are strengthened"

[85]For example art.2ter§3 of Italian Decree-Law 15 March 2021, n.21 establishes it within the Presidency of the Council of Ministers

mentioned procedural requirements are meant to preserve during the exercise of screening powers, are analyzed.

8.1.2 EU suggestions for Member States' substantive test

Pursuant to art.3, *"Member States may maintain, amend or adopt mechanisms to screen foreign direct investments in their territory on the grounds of security or public order"*. Based on this provision, the adoption of such legislation is not mandatory. Nevertheless, the European Commission *"calls upon [..] Member States that currently do not have a screening mechanism [..] to set up a full-fledged"* one[86]. If a Member State adopts such a mechanism, it is bound to respect and apply the procedural and substantive provisions of the Regulation.

In general, in EU law the notion of "capital movement" under art.63 TFEU covers donations[87] and non-monetary[88] resources. In interpreting the scope of this fundamental freedom, the CJEU has always drawn on the non-exhaustive list of capital movement contained in Annex I Directive 88/361/EEC[89]. However, the Regulation[90] applies to mechanisms screening capital movements from third countries *"aiming to establish or to maintain lasting and direct links between the foreign investor and the entrepreneur to whom or the undertaking to which the capital is made available in order to carry on an economic activity in a Member State, including investments which enable effective participation in the management or control of a company"*, therefore the scope of the Regulation is narrower than "capital movement"[91].

The grounds for establishing the screening powers are: *"security and public order"* in respect of the principle of non-discrimination among third countries. These terms are not new to EU law; in fact, they can be found in the TFEU provisions as grounds for limiting the so-called four "fundamental freedoms" of the EU, although they may be worded differently[92]. In addition, they are relevant to our purpose not only because of analogy, but they are applicable since FDI is itself a form of fundamental freedom of the EU[93]. Specifically, art.65(1)(b) TFEU applies[94]. Moreover, the Regulation talks of

[86]Communication from the Commission, Guidance to the Member States concerning foreign direct investment and free movement of capital from third countries, and the protection of Europe's strategic assets, ahead of the application of Regulation (EU) 2019/452 (FDI Screening Regulation), (2020/C 99 I/01), which can be retrieved at https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52020XC0326(03)from=IT. (last accessed 04/20/2022 at 12.52pm)

[87]See C.Herrmann, M. Hoffmann, Investment in the European Union: Competences, Structures, Responsibility and Policy, page 2218 where it is cited CJEU, Persche, C-318/07 , in which the Court regarded a donation to a charity falling under art.56 TEC (now art.63 TFEU)

[88]Ibid., where it is cited CJEU, van Putten, Mook and Frank, Joined Cases C-578- 580/10 where the Court held that the loan of a motor vehicle fell under art.63 TFEU

[89]Ibid., the text of the Directive can be retrieved at https://eur-lex.europa.eu/legal- (last accessed 04/20/2022 at 12.52pm)

[90]see section 1.4 of this paper

[91]see notes in section 1.4 of this paper

[92]For instance, arts. 45(2) and 52(1) TFEU speak of "public order, public security"

[93]See art.63(2) TFEU

[94]See Recital 4 of the Regulation; however, art.65(1)(b) is held applicable also to intra-EU investments. The Regulation must be considered as specifying the scope of application of art.65(1)(b) as to limitations on grounds of public security and public order to investments made by extra-EU direct investors

"likely effect", which, according to some scholars[95], is meant to lighten the burden of proof upon the State in contrast to the case of the requirement of actual effect on public security and public order, thereby further increasing MSs' discretion.

However, as seen above[96], compliance with the Regulation in the first place is now essential in order for a SM to be lawful according to EU law. Art.4 of the Regulation lists objective and subjective factors that may be taken into consideration by the MSs and the EC in determining whether the FDI is likely to affect public security or public order, among which *"critical infrastructure [..] including energy"*, *"supply of critical inputs"* and *"whether controlled by the government of a third country"* appear[97]. From the wording of the provision, it is clear that the State is not bound to consider them. However, relying on this norm is a strong indicator that the screening decision pursues a legitimate interest[98]. It has been argued that the vagueness of some provisions (e.g.what is critical?) and non-exhaustive list of critical activities and inputs may constitute a way to circumvent the strict grounds for FDI screening[99].

In conclusion, EU law allows for MS to restrict FDI on broad grounds. Indeed, the CJEU, whose jurisdiction may be activated through the preliminary reference procedure under art.267 TFEU[100], is likely to step in and declare a SM decision unlawful only if the measures constitute disguised means for protectionism or manifestly lack a basis[101]. This conclusion is reinforced by the wide discretion generally granted to MSs in the sensitive area of national security, which is traditionally held as being in the realm of MSs' sovereignty, as also recognized by EU law[102]. However, the burden of proof of the aforementioned *"likely effect"*, which is relatively low if the State relies on art.4 of the Regulation, lies upon the MSs.

9 The SM laws of selected EU countries

This section examines SMs legislation in specific EU MSs that may be particularly useful models for Bosnia and Herzegovina due to relevant features in common with it. In par-

[95] M. Kontak, 'Evaluation of the EU Screening Mechanism and the Question of Reciprocity with China' (2021) 17 CYELP 203, page 213

[96] See above in section 8.1 and note 77

[97] The complete list is: " [..] may consider the potential effects on, inter alia, a) critical infrastructure, whether physical or virtual, including energy, transport, water, health, communications, media, data processing or storage, aerospace, defense, electoral or financial infrastructure, and sensitive facilities, as well as land and real estate crucial for the use of such infrastructure; b) critical technologies and dual use items as defined in point 1 of Article 2 of Council Regulation (EC) No 428/2009, including artificial intelligence, robotics, semiconductors, cybersecurity, aerospace, defense, energy storage, quantum and nuclear technologies as well as nanotechnologies and biotechnologies; c) supply of critical inputs, including energy or raw materials, as well as food security; d) access to sensitive information, including personal data, or the ability to control such information; e) the freedom and pluralism of the media" (para 1, objective criteria) and " [..] may take into account whether b) whether the foreign investor has already been involved in activities affecting security or public order in a Member State; c) whether there is a serious risk that the foreign investor engages in illegal or criminal activities" (para 2, subjective criteria about the person of the investor)

[98] Since now the source for limiting an EU fundamental freedom is an EU piece of legislation, see note 80

[99] See note 95, pages 233 and following where it is criticized an excessively protectionist use of SMs in Germany. By analogy, the ambiguous wording may legitimize this use of SMs, in this regard judicial review and cooperation with the CJEU will be fundamental

[100] That means by national courts raising questions on the application and interpretation of the Regulation

[101] Please note that this is the authors' opinion in the light of the case law in other sectors of EU law, provided that the Court has not rendered any preliminary judgment on the SM Regulation

[102] See the provisions cited in notes 75 and 92, but also other provisions throughout the TFEU (like art.36)

ticular, Germany and Italy share with Bosnia and Herzegovina a federal or quasi-federal structure, while the Czech Republic and Slovakia have in common a comparable territorial extension, population and their administrations face similar challenges posed by the balance among globalization, compliance with EU law and preserving the national interests. Eventually, the Republic of (South) Korea SM framework will be presented since the Asian State has a well-established record of fostering foreign investment, whether direct or non-direct.

9.1 Germany

Germany may be a useful point of reference for Bosnia as it has a federal political structure in which the central Government's competences on security and international trade policy overlap with those of State entities[103]. These features are similar to the overall federal structure of Bosnia and Herzegovina.

The federal structure in Germany is reflected in the SM framework provided for by sec.12 of the Foreign Trade and Payments Act of 6 June 2013 (Außenwirtschaftsgesetz, hereinafter AWG). Under this framework, State entities are represented in the Bundesrat, where they can make comments on the ordinance within four weeks of its promulgation. On the other hand, only the Bundestag, where representatives of the People at the federal level are elected, can revoke the ordinance within four months of its promulgation.

The Federal Republic of Germany enacted its SM in the Foreign Trade and Payments Ordinance of 2 August 2013 and further amendments (Außenwirtschaftsverordnung, hereinafter AWV), issued by the Federal Government, thereby implementing the AWG, as illustrated above.

In the AWV there are two different screenings, one which applies to any sector ("cross-sectorial", secs.55-59a AWV) and one that applies in relation to the sectors listed in sec.60 ("sector-specific", secs.60-62 AWV), relevant for defense-related assets and companies. Notwithstanding this division, sec.55a lists companies operating in some sectors and services relevant for the assessment of a *"likely effect on public order and security"*. Most notably, this list specifies the criteria laid down in art.4 of the Regulation and in doing so grants wide discretion to the competent Minister, provided that the list includes numerous activities to be carried out by the domestic company in order for SM proceedings to be triggered[104].

The scope of application and regulation of the two SMs also differs as to the following element: the cross-sectorial, in compliance with art.2 n.2 of the Regulation, applies if *"a non-EU resident directly or indirectly acquires a domestic company [..] or a stake under section 56"* or *"there are indicators that an abusive approach [..] has been undertaken"*, such as not having offices, staff or equipment within the EU. On the other hand, the sector-specific, in compliance with art.65(1)(b) and 346 TFEU, only applies if it is

[103] see arts.70(1), 73(1)(5) of the Basic Law for the Federal Republic of Germany

[104] sec.55a(1) contains 27 subparagraphs, some of which contain at least two letters, each one listing an activity, while sec.55a(3) contains subjective elements, for which see note 97

assessed that the acquisition under sec.60a *"by a foreigner is likely to impair essential security interest"* or if there are indicators of circumvention as *supra*.

One further divergent aspect between the two is that sec.56 provides for differentiated thresholds from 10 to 25% (and also progressive acquisitions of higher percentages) of direct or indirect voting rights, depending on the activities enumerated in sec.55a, that trigger the procedure. Furthermore, sec.56(4) establishes a strict rule for indirect control; indeed, the voting rights of a third company are attributed to the acquirer if it holds the aforementioned percentage of voting rights in the said company. In contrast, sec.60a provides that the relevant threshold is exclusively 10% of voting rights and other rules for counting of voting rights established for the cross-sectorial apply.

As last element of distinction, Sec.58, which does not apply to the sector-specific SM, stipulates that the acquirer may lodge an application for obtaining a certificate of non-objection, which bars the Ministry from initiating the proceedings of its own motion if they are not initiated within two months of the notification. It has a particular significance in the light of legal certainty, for which see also *infra* in this section.

In relation to the aspects in this paragraph, the law is identical, as long as applicable to both categories[105]. First, the Federal Ministry for Economic Affairs and Energy (hereinafter, the "German Ministry") is the body responsible for assessing and carrying out the screening. Second, the transaction concluded without the authorization is null and void, without prejudice to third parties who acquire rights from the subjects benefitting from the invalid transaction[106]. Third, the proceedings may be initiated either on notification by the party upon the reaching of the said thresholds or *ex officio*. Fourth, the exercise of voting rights is prohibited until the decision is issued. Eventually, the final decision, issued by the Government on the basis of the procedure carried out by the Ministry, can be: clearance, prohibition or restriction of voting rights, appointment of a trustee to bring about the unwinding of the acquisition or clearance with the issuing of instructions which are monitored through a report produced by an expert. The decision is always subject to judicial review pursuant to administrative law principles; therefore, the Court may not substitute its own assessment for that of the Ministry. In addition to that, the burden of proof of the aforementioned effect is upon the Government, which also has a wide margin of appreciation in the light of the ambiguous wording.

Different rules apply as to the deadline for the exercise of SMs powers; in fact, the proceedings must conclude within four months, which can be extended to seven if they reveal *"particular difficulty"* or there is a request for information, of the receipt of the documents which the German Ministry mandates to notify pursuant to a general administrative act. Otherwise, a different deadline to open the proceedings of two months starts from when the Ministry *"obtain[s] knowledge of the conclusion of the contract"*, subject to the proviso that no assessment procedure can be opened after more than five years from the conclusion of the contract[107]. In relation to this last rule it is understood

[105] Secs.60a(2),62(2) AWV
[106] Sec.15(1) AWG
[107] Sec.14a AWG

how the possibility of seeking non-objection certificates increases the willingness of the parties to notify the Ministry of the transaction.

9.2 Italy

Italy was chosen as a country relevant for our purposes due to its quasi-federal (regional) framework, in which the Central Government has competence upon national security and public order, but shares "commerce with foreign countries" with Regional Entities[108].

Following the declaration of incompatibility with EU law of "golden shares"[109], the Italian Republic enacted a new SM through the adoption of Decree-Law 15 March 2012, n.21 converted into law, with amendments, by Law 11 May 2012, n.56 and subsequent integrations and modifications[110] (hereinafter, "the Decree"). Indeed, the idea underlying this legislation is that of "golden powers", which will be described below in relation to each sector of interest.

The Decree distinguishes companies operating in: (i) defence and national security (art.1), (ii) holding assets in energy, transports, communications and sectors under art.4 of the EU Regulation (art.2), (iii) 5G technology (art.1bis). In order to precisely detect the concerned undertakings in each of the aforementioned sectors, the President of the Council of Ministers (hereinafter, P.C.M) can adopt secondary legislation (decrees of the P.C.M, hereinafter, d.P.C.M.) upon proposal of the competent Minister. These administrative acts[111] may be updated every three years and are submitted, before their adoption, to the competent Parliamentary Commissions for an opinion[112], thereby preserving a check on the Government's powers.

In relation to the defense sector, the Government in case of *"threat of serious prejudice to the essential interests of defense and national security"* may *"impos[e] specific conditions [..] as to security of supply and information"*, may *"veto the adoption of [..] acts of the organs of the administration of the undertaking [..] which have as effect the modification of ownership or control of assets"* and *"oppos[e] the purchase of shares by a subject other than the Italian State or Italian public entities [..] if the acquirer detains [..] a level of participation to equity with voting rights capable of compromising in the specific case interests of national security"* (so-called golden powers, which can be exercised regardless of public ownership of the enterprise)[113]. As for the last power, art.1§5 provides that for public-listed companies the threshold is 3% and then 5, 10, 15, 20, 25

[108] See art.117§2 letter h and §3 of the Constitution of the Italian Republic, according to the latter "commerce with foreign countries" is a shared competence, which pursuant to §3 of the same article means that the law of the Republic provides for the "determination of fundamental principles" in the matter

[109] By "golden share" it is meant the power to veto the acquisition of shares by individuals in privatised companies in some sectors, as envisaged by repealed art.2 Decree-Law 332/1994, which the CJEU in Commission v Italy, C-326/07 regarded as discriminatory in relation to art.49 TFEU

[110] The Act was amended three times in 2019, once in 2020 and once more in 2022. The consolidated version, in Italian, can be retrieved at https://www.normattiva.it/uri-res/N2Ls?urn:nir:stato:decreto.legge:2012-03-15;21!vig=

[111] The complete list thereof can be found, in Italian, at https://www.governo.it/it/dipartimenti/dip-il-coordinamento-amministrativo/dica-norm-goldenpower/9299, (last accessed 05/06/2022), note that art.2§1ter explicitly recalls art.4 of the EU Regulation

[112] The opinion is not binding and it is considered issued if the Parliamentary Commissions do not provide it within 30 days of its submission

[113] See note 109

and 50 for further share-purchasing.

The time limit for the exercise of one of the mentioned powers is 45 days of the notification. Then, paragraphs 2, 3 and 3bis restrict the Government's discretion by listing the criteria that must or may (§3bis) be considered in assessing the above-mentioned threat, even though they leave a wide margin of appreciation[114]. Furthermore, the acquisition of the said thresholds implies the obligation to notify the P.C.M within 10 days.

Pending the Government's decision, voting rights are suspended and the deliberations of the assembly with the decisive vote of the "suspected" shareholder are null and void. If the obligation of notification is not complied with, in combination with the invalidity of deliberations mentioned, provided that *ex officio* proceedings may be started and, save when a felony is committed, the individual is subject to an administrative fine[115] which can amount to the double of the value of the operation and no lower than 1% of annual turnover of the non-compliant companies[116]. Moreover, the competent Tribunal, upon request by the P.C.M., may order the acquiring person to sell its shares (art.1§§5 and 8bis).

As to the companies holding assets in the sectors under art.4 of the EU Regulation, a decree of the President of the Council of Ministers[117], after the favorable vote of the Council of the Ministers, may veto the adoption of any act by the undertaking concerned which has, among others[118], *"[..] as effect the modification of the ownership of the said assets [..] in favor of an individual outside the EU"* (art.2§2bis). The said individual is defined as, alternatively (art.2§5bis):

a. whatever physical and legal person not having his residence, legal or administrative seat or center of main activity in the EU or European Economic Area

b. whatever legal person having its legal seat in the EU and controlled[119] by a person under letter *a.*

c. whatever person not fulfilling the requirements of letter *a.* when there are elements

[114]Para 2:" [..] strategic relevance of assets [..], the adequacy of the undertaking's structure to guarantee integrity of national security"; para 3: "in the respect of proportionality and reasonableness [..] adequacy of economic capacity in respect of the continuance of the activities [..], the existence, taking account of official positions of the EU, of links with countries which do not respect democracy and the rule of law [..]"; para 3bis, applicable to non-EU individuals (see the part on art.2 of the Decree), :"[whether] controlled by the Public Administration [..], already engaged in activities which affect the security of one of the MS of the EU [..], serious risk of involvement in illegal activities"

[115]This fine applies for any failure to comply with the decisions adopted pursuant to the Decree

[116]The target company is also liable if it does not abide by the conditions set by the Government

[117]Which must be immediately sent to the competent Parliamentary Commission by excerpt (art.2§3), this rule is applicable also in relation to the defense sector (art.1), thereby granting a check on the Government also in relation to the administrative implementation of the SM

[118]Art.2§2: "which has as effect the modification of ownership [..] of the assets, changing their use, [..] transferral of the seat abroad, [..] winding up the company", art.2§2bis: "[..] in the sectors indicated by paragraph 5 (communications, energy, transports, health, agri-food, financial) even in favor of Italian residents [..]", this last sentence enters into force on the 1st of January of 2023 and applies to control shareholdership, as defined by art.2359 of the Italian Civil Code (hereinafter, I.C.C.), for which see the note below

[119]For the notion of direct or indirect , i.e through controlled or trust companies, control in the Italian legal system, art.2359 of the I.C.C. defines it as alternatively a) ownership of the majority of voting rights (de iure internal control) b) exercise of dominant control in the assembly (de facto internal control, such as through shareholders' agreements or fragmented shareholdership, which allows to appoint administrators) c) contractual dominance which allows to impose strategic choices and the appointment of administrators (external control)

suggesting an abusive behavior (which are not defined, though, in contrast to the German SM[120])

In addition, the other requirement for the veto power to be triggered is that the acts *"give rise to an exceptional situation [..] of serious threat for public interests relating to security and functioning of the network of supply or the plants"*.

For the remaining aspects, such as the criteria for the assessment of the above-mentioned situation and the procedure, the law does not differ from that of the SM in the defense sector. One exception are the percentages of voting shares or equity, whatever the highest, for the SM proceedings to be activated, which do not provide for the 3% threshold[121].

In relation to the undertakings *"aiming to acquire [..] goods and services relating to projecting, realizing, repairing" "services of communication [..] based on the 5G technology [and], other services, goods, activities relevant for cybersecurity, including the cloud technology"* shall notify the P.C.M., before the acquisition, of a an annual plan. This contains detailed information about the notifier, the plan to develop the network and the state of complying with previous conditions imposed by the Government (art.1bis§3) and is repeated every year. Within 30 days, the Government may either consent, also with conditions, or object.

Eventually, every exercise of the "golden powers" is subject to judicial review pursuant to the same principles of administrative law as illustrated above in the section on the German SM. Another useful provision is art.2bis, which mandates that administrative authorities competent for the regulation of a specific sector of the economy[122] collaborate among them and with the Government, also by exchange of information. Its usefulness is due to the fact that these authorities, by virtue of their inspection powers and day-to-day contact with market operators, may possess relevant information on undertakings, which may happen to operate in sectors covered by the Decree, thus helping the Government exercise its powers cognizant of every factual aspect.

9.3 Czech Republic

The Czech Republic is another EU Member State that provides an interesting potential model for a future Bosnian screening mechanism. The Check Republic's size, history, and means suggest that it faces many of the same economic and administrative challenges as Bosnia and Herzegovina.

In the aftermath of the COVID-19 pandemic and wave of foreign acquisitions related thereto, the Czech Republic enacted Act No.34/2021[123] to adopt a SM. This new mechanism at least partially reversed years of practices that were perceived as an excessively

[120] See page 40

[121] See the page above

[122] Among others, the Italian Central Bank (Banca d'Italia), the Securities and Financial Markets Authority (Consob) and the Authority of Surveillance on the Market of Insurance (IVASS)

[123] J. Logesova et al, Czech Republic in Foreign Direct Investment Regimes 2022, Third Edition, International Comparative Legal Guides

open FDI policy, especially to China[124].

The Act is similar to the bipartition under German law, with some important differences. Most notably, while the Czech law also distinguishes between sector-specific and cross-sectorial investments[125], the "sector-specific" SM also applies in relation to the media sector (i.e holders of nationwide radio or television broadcast licence or periodicals with average of print run of average 100,000 copies per day in the preceding year) and the operation of critical infrastructure (e.g power plants).

In addition, unlike the German SM, under the Czech legislation, the Ministry of Industry and Trade (hereinafter, the "Czech Ministry") can bring *ex officio* proceedings on grounds of security and public order only as regards the "cross-sectorial" SM or if the party in the "sector-specific" fails to notify the Ministry. The time limits and law on the certificate of non-objection are similar to that of Germany[126]. Meanwhile, the sector-specific SM requires a mandatory consultation, which is voluntary in the cross-sectorial screening. The mandatory consultation is with the Ministry and must occur before the agreement comes into effect.

Some of the differences with the German SM include: there is only one definition of foreign investor for both SMs, i.e a natural or legal person who is not either a citizen of an EU MS, with its seat inside the EU or a legal person directly or indirectly controlled by a person not possessing one of the preceding requirement. Furthermore, the notion of effective control over an economic activity carried in the Czech Republic is even broader given that it captures not only the exercise of at least 10% of voting rights, but also if the level of control enables them to gain access to information sensitive to security or public order of the Republic.

One more divergence is that the time limits for the exercise of SMs powers differ in the case of consultation, in which the Czech Ministry must decide whether to initiate proceedings within 45 days, or if the Czech Ministry considers that the investment requires a Governmental decision (prohibition, clearance with conditions), in which the Czech Ministry must request the resolution within 90, or 120 in difficult cases, days. After the request, the Government must issue its resolution within 45 days. Last but not the least, there is an express framework for consultation with other Governmental and other regulatory entities and the implementation of the transaction before the clearance is sanctioned by up to 1% of the turnover of the offender in the last financial year or, if not applicable, from EUR 2000 up to EUR 2 million.

9.4 Slovakia

In 2021, in an environment similar to that of the Czech Republic, the Slovak Republic established a SM by adopting Act No. 72/2021 Coll., which introduced §§9a-9e into

[124]T. Peragovics, Protection without Protectionism? Foreign Investment Screening in Europe and the V4 Countries Today – A Comparative Analysis, pages 19 and following

[125]See section 9.1, in particular page 40

[126]See section 9.1, in particular pages 39 and 40

Act no.45/2011 Coll[127]. Unlike the Czech mechanism, the scope of the Slovakian SM is stricter and limited to companies operating in the energy, pharmaceutical industry, metallurgy and chemical industry sectors, which are under the responsibility of the Ministry of Economy (hereinafter, the "Slovak Ministry"), which is the sole institution responsible for carrying out examinatory proceedings prior to the final decision, within the competence of the Government as a whole.

The review requires an assessment of *"whether the direct or indirect transfer or transition to another person [..] disrupts the public order or national security of the Slovak Republic or another Member State of the European Union or the interests of the European Union"*. The threshold above which it applies is 10% of voting shares *of the "operator's registered capital or voting rights" or "the person whose possibility to influence the operator's management is comparable to the influence derived from such ownership interest"*. Consequently, the written application for review must be made prior to the conclusion of the agreement (§9a(3)). Pending the decision, which is to be made within 60 days from the notification of application, voting rights are suspended.

In the meanwhile, the Slovak Ministry proposes a decision to the Government, which shall have the final word with an opinion of the Security Council of the Republic. Furthermore, the Government has to evaluate whether *"the transfer or the transition carries more benefits than risks from the viewpoint of public order or national security"* and may also impose conditions. The decision may be withdrawn if the information provided for by the applicant is untrue or incomplete or the conditions imposed are unfulfilled.

The Government's decision can be appealed within 30 days of the receipt by the investor before the Supreme Court. If it is filed, the appeal has a suspensive effect of the decision. Eventually, failure to notify is an administrative breach punished with a fine which can amount from EUR 500 to EUR 50000.

9.5 South Korea

The Republic of South Korea was chosen as a subject of analysis due to the widespread acknowledgement of its friendly environment towards FDI and foreign investment in general[128]. Unlike the frameworks of the EU countries analyzed above, the Asian State has two pieces of legislation governing FDI, namely: the Foreign Investment Protection Act[129] (hereinafter, the "FIPA") and the Foreign Exchange Transaction Act[130] (hereinafter, the "FETA").

[127]The consolidated version can be retrieved at https://trade.ec.europa.eu/doclib/docs/2021/march/tradoc$_1$59517.*pdf* (*lastaccessed*04/20/2022*at*12.52*pm*)

[128]According to a 2013 report by the Organization for Economic Cooperation and Development (OECD), the South Korean score in the FDI Regulatory Restrictiveness Index (ranging from 0, open, to 1, restricted) for the 2010 year was 0,143 and that in the decade leading to 2013 was among the countries whose index decreased the most. For further information see https://www.oecd.org/investment/investment-policy/WP-2013$_2$.*pdf* (*lastaccessed*04/20/2022*at*12.52*pm*), *pages*8 − 11

[129]Formally cited as Act No. 14839, Jul. 26, 2017, its English version can be retrieved at https://elaw.klri.re.kr/eng$_s$*ervice*/*lawView.do*?*hseq* = 44627*lang* = *ENG*

[130]Formally cited as Act No. 14525, 17. Jan, 2017, its English version can be retrieved at https://law.go.kr/LSW/lsInfoP.do?lsiSeq=191033viewCls=engLsInfoRurlMode=engLsInfoR0000

Pursuant to art.2§1 n.4 FIPA, its scope of application extends to foreign investment (hereinafter, FI), defined as, among others[131], *"[w]here a foreigner*[132] *holds stocks or shares [..] of a Korean corporation*[133] *[..] or a company run by a national of the Republic of Korea [..] by any of the following methods*[134] *in order to establish a continuous economic relationship with the Korean corporation or company, such as participating in the management of such Korean corporation or company"*. Art.2§2 of the Enforcement Decree of FIPA[135] further specifies that for the FIPA to apply, the investment must exceed 100 million Korean Won (74.234,72 Euro) and own at least 10% of voting stocks or must entail appointing an executive office, such as a director.

According to the FIPA[136], FI, as defined above, is prohibited in:

i. forbidden sectors (such as postal services and central bank)

ii. restricted sectors (e.g, nuclear plants, radiotelevision and newspapers) if it exceeds 1% of total sales

iii. on grounds of national security by the Ministry of Trade, Industry and Energy (hereinafter "MITE"), after a review by the Foreign Investment Committee[137]

The report[138] of FI shall include, among others, the application for acceptance of the report, supporting documents showing the identity of the investor and that requirements of FI under FIPA are met. Failure to report is punished with a fine not exceeding 10 million Korean won (7.424,01 Euro) or, in case of investment in the defense sector, with up to 1 year imprisonment and order to sell the shares.

If the foreign investment is not caught by the FIPA, FETA applies[139]. The said investment is not subject to approval by the MITE and only gives rise to an obligation to report, which must only include the identity of the investor and the underlying contracts. In cases of failure to report, fines similar to that of FIPA apply[140].

Another interesting aspect of South Korean legislation, which is presumed to have kept

[131] "A loan with maturity of not less than five years [..] which is provided to a foreign-capital invested company by any of the following entities: The overseas parent company of the foreign-capital invested company [..] A foreign investor [..]; Where a foreigner contributes to a nonprofit corporation pursuant to this Act in order to establish a continuous cooperative relationship with the corporation"

[132] Art.2§1 n.1 FIPA :" individual with a foreign nationality [or] a corporation established in accordance with a foreign law"

[133] Art.2§1 n.3 FIPA: "a corporation established in accordance with the Acts of the Republic of Korea"

[134] "Acquisition of stocks, etc. newly issued by the Korean corporation or company run by the national of the Republic of Korea; Acquisition of stocks, etc. previously issued by the Korean corporation or company run by the national of the Republic of Korea"

[135] Presidential Decree No.27972, 29. Mar, 2017., Amendment by Other Act, which can be retrieved at https://investmentpolicy.unctad.org/investment-laws/laws/311/korea-republic-of-enforcement-decree-of-the-foreign-investment-promotion-act

[136] J. Jiang, R. Kim, Korea in Foreign Direct Investment Regimes 2022, third edition, page 3

[137] To which national and local Government officials take part, see art.27 FIPA

[138] To be made before closing, save exceptional circumstances to be justified in the report, including acquisition of listed shares. For the complete list thereof see note 136, page 5

[139] See note 136

[140] If the value of the transaction is below 20'000 US$ only a warning is issued (and repeated violations may lead to the suspension of the transaction), if it is below 1 billion Korean won a fine of maximum 100 million Korean won may be issued, above the latter threshold imprisonment up to 1 year

the number of Investors-State Disputes close to zero[141], is the Foreign Investment Ombudsman hereinafter "FIO")[142]. He/she is chosen among experts of investment law and has the power to handle complaints and proposed legislative amendments. In relation to the SM, the FIO could be useful both in relation to dispute prevention and resolution. Indeed, once received the complaint after the exercise of SMs powers, the Ombudsman, if he/she regards so in the light of the principle of proportionality, could suggest that the MITE authorizes the investment subject to some conditions.

[141] See the report in note 128, page 25

[142] The legal basis for its functioning can be retrieved at https://ombudsman.kotra.or.kr/ob-en/cntnts/i-2642/web.do

Part V
Recommendations

In the light of the aforementioned legal frameworks, we recommend that in setting up its SM Bosnia and Herzegovina observes the following indications:

In relation to what art.70 SAA provides, we generally advise that Bosnia and Herzegovina complies with EU law, and especially with Regulation (EU) 2019/452 (see section 9 of this paper). However, as to the SM legislation, we identified the subsequent aspects in which EU law binds the legislator's discretion:

As to the definition of "foreignness" of the investor. If he/she/it is defined as not possessing Bosnian nationality, the SM shall be confined to the defense sector. While, if defined as a third country national under EU law, the SM could include other economic sectors, provided that the grounds for its activation are respected.

In relation to definition of FDI, it is necessary that it does not cover forms of investment not entailing more generally to maintain or establish a lasting link to the enterprise or entrepreneur or an active involvement in the management of companies, as testified by the acquisition of voting rights in the general assembly of the company's shareholders. In relation to the voting rights, there is a comparative consensus on the activation of SMs upon reaching the threshold of 10%. If the requirement of "active involvement in the management" was not satisfied, Regulation 2019/452 would cease to apply and the limitation on investment will be caught by art.63 TFEU, which requires stricter grounds, at least as regards sectors different from the defense one. Provided that national security concerns under art.346 TFEU might be hardly be invoked to screen FDI in such companies. Applying this recommendation to the Law on the Policy of Foreign Direct Investment in Bosnia and Herzegovina currently in force, the definition of FDI under art.2 thereof[143], if there was an amendment so as to include screening powers in relation to sectors under art.4 of the SM Regulation, should be amended so as to contain a reference of voting rights or, more generally, to active management in the company.

As regards the grounds for scre ening, it is essential that the wording reproduces, with some margin of discretion, that of the Regulation (*"likely effect on security and public order"*) and that the list of art.4 of the Regulation is, implicitly or explicitly, reproduced. However, in order to foster investment in sectors excluded from the scope of the SM and preserve the trust of investors, it might be necessary that secondary legislation specifies the companies and sectors affected. These sub legislative acts might need to be updated in a reasonable time lapse.

As for the cooperation mechanism, it might be advisable that the Entities of BiH (empowered by art.4(b) of the Law on the Policy of FDI in BiH to authorize equity ownership by foreign investors exceeding 49% of equity in companies engaged in sale of

[143] "investment in the newly established company or investment in existing domestic company [..] which may be in cash, goods and rights"

arms, ammunition and public information) enter into voluntary exchanges of information for investments screened with the Commission and other EU MSs so as to allow that SM policies align *in concreto* to that of the EU and that more data is gathered to ensure a thoughtful decision. In order to allow an effective cooperation, it might be recommended that SM powers are not exercised until comments are provided for or if a reasonable interval expires.

About the judicial review of SM decisions, effective remedies to trigger a judgment by an impartial Court in case of violations of the law shall be established. It is recommended that they may not have a suspensive effect thereof (otherwise the address of the decision would be the one establishing the entry into force of the decision, *interim* measures could be an option for situations of clear and present danger to the rights of the investor pending the decision).

In addition, as regards aspects in which there is no EU-bound rules on SM or business related topics:

- *Establish a Business Ombudsman Institution*
  A good example for that is the established Business Ombudsman Institution in Ukraine. Apart from being empowered to investigate alleged wrongdoing by state entities, the institution also publishes systemic reports, which address some of the most pressing systemic issues that negatively affect the investment climate and proposes practical ways to address these issues. These reports are being extensively used by the authorities to improve the existing legislation and procedures that negatively affect the business environment. This demonstrates that the systemic role of the Business Ombudsman Institution has a further impact on the advancement of the reform in the country and that a well-structured and equipped Business Ombudsman Institution could serve as an effective tool of policy dialogue in a country. Recommendations made by the Business Ombudsman are not binding, but the publicity generated by the reports and more generally through the mass media create pressure on public entities and on the enforcement, agencies investigating criminal cases to take action to tackle corruption and rectify other breaches of the legitimate rights of businesses[144].

- *Refer to Investment Policy Framework for Sustainable Development (IPFSD) for negotiating BITs*
  Bosnia and Herzegovina could use the framework as a key point of reference in formulating national investment policies and in negotiating or reviewing IIAs. For example, referring to the sustainable development dimension as outlined in the IPFSD, Bosnia and Herzegovina can negotiate its BITs more thoroughly by adding:

  a. a carefully crafted scope-and-definition clause that excludes portfolio, short-term or speculative investments from treaty coverage
  b. the formulation of the fair and equitable treatment (FET) clause as an exhaustive list of State obligations, e.g. not to

[144]Bosnia and Vina - UNCTAD. (n.d.). page.14, Retrieved from https://unctad.org/system/files/official-document/diaepcb2015d1_en.pdf

i. deny justice in judicial or administrative procedures
ii. treat investors in a manifestly arbitrary manner
iii. flagrantly violate due process

c. the inclusion of carefully crafted exceptions to protect human rights, health, core labor standards and the environment, along with a check-and-balance system that makes sure there is enough policy space whilst avoiding abuse

d. add the option of "no ISDS mechanisms" clauses, or clauses designed to make ISDS the last resort (e.g. after exhaustion of local remedies and the use of Alternative Dispute Resolution mechanisms by the investors)[145]

- *Clarify VAT provisions related to non-residents eligible for VAT refund*
- *Make the procedures and decisions of the Indirect Taxation Authority (ITA) public*
- *Abolish tax on export for companies which export more than 30%*

[145]BTI 2022 Bosnia and herzegovina country report. BTI 2022. (n.d.). Retrieved - https://bti-project.org/en/reports/country-report/BIHpos0