The Insolvency Law of Central and Eastern Europe

Twelve Country Screenings of the New Member and Candidate Countries of the European Union and Russia: A Comparative Analysis

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II. Croatia

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1. Introduction

a) Historical Background

With the Bankruptcy Law of 17 May1996,[151] which took effect on 1 January 1997, Croatia has a modern legal regulation that, in particular, also satisfies EU requirements. The new Bankruptcy Law replaces the Law on Enforced Composition, Bankruptcy and Liquidation of 1994, which was a first attempt of adaptation to the abandonment of self-administration and to the introduction of privatisation leading to a Western-influenced ownership system since the end of the end of the 1980s. This law has been reformed by means of three amendments of 12 March 1999, 14 December 2000 and 23 July 2003.[152] The German Insolvency law served as a model for the amendment; the new Croatian Bankruptcy Law is also based on the provisions of the new German Insolvency Law.[153]

[151] Bankruptcy Law, KG "Narodne novine", no. 44/96; the German translation of the Bankruptcy Law was published in: Wirtschaftsrecht der osteuropäischen Staaten [Business Law of the Eastern European States] WOS in the 51st issue, July 1997, and edited by Tomislav Boric.

[152] Laws Concerning the Amendment and Supplementation of the Bankruptcy Law, "Narodne novine", nos. 29/99, 129/00; 123/03; 82/06; 197/03; Government Order 187/04.

[153] M. Dika, Das kroatische Insolvenzrecht [Croatian Insolvency Law], ROW 1998, volume 9, p. 339; for the reliance, particularly of Croatian business and tax law, on the German legal system and as an overview of the new Croatian business and investment law since the system transformation in the early and mid-nineties, see Z. Pokrovac, M. Wenserski, Das deutsche System hat Pate gestanden [The German System Served as a Model], in: Handelsblatt 3.4.1997 issue, p. 24; Z. Pokrovac, M. Tell-Madl, Erfahrungen und Probleme bei der Rezeption deutschen Rechts in Kroatien [Experience and Problems With Respect to the Reception of German Law in Croatia], in: Ost-West Contact 06/1997; Z. Pokrovac, P. Pejic, Gesetzgebung orientiert sich am deutschen Vorbild [Legislation Oriented to the German Model], in: Handelsblatt 1.4.1999 edition, p. 50.

b) Insolvency Practice

In practice, the major difficulties in Croatia result from the long duration of insolvency proceedings (often over two years), and the accumulated backlog of proceedings. For example, there was a backlog of 768 insolvency proceedings at the beginning of 1999, with a total of 992 completed proceedings from the beginning of 1997 (when the Bankruptcy Law took effect) until the beginning of 1999.[154] In this regard the last amendment to the Bankruptcy Law 2003 brought some improvements: Insolvency proceedings (both liquidations and reorganisations) completed with a positive result amounted to 212 cases in 2005, and 179 cases in 2006. At the same time, 630 cases were rejected due to lack of assets in 2005, and 445 cases in 2006.[155]

These amendments concern modification of structure and jurisdiction of the Bankruptcy Court, the legal status of the administrator, some legal remedies, status changes of creditors, possibilities of contesting legal transactions, acceleration of proceedings by introducing deadlines for main decisions and determination of terms for distribution of proceeds.

2. Commencement of Insolvency Proceedings

a) Principles of Procedure

The insolvency proceeding is divided into two stages, the preliminary proceeding and the main proceeding. The existence of a ground for insolvency is examined in the preliminary proceeding. Changes result-

[154] Concerning the cited figures, see the World Bank Report/Croatia Court and Bankruptcy Administration Project of 13 June 2001, Project Appraisal Document, p. 3-6.

[155] Nevertheless, in that period the average total number of operating companies was 71,000, so that the insolvency rate was merely 0.9%.

ing from the Second Bankruptcy Law Amendment also relate to this preliminary proceeding. For the purpose of accelerating the preliminary proceeding, it is now no longer permissible lodge an immediate appeal against the court order on commencement of the preliminary proceeding (Art. 42 para. 1 BL). The main proceeding begins with the court order on commencement. After that, the debtor's assets are collected and realised, the creditor's claims are determined and satisfied or a reorganisation is carried out. The proceeding ends by discontinuation or termination.

The reorganisation proceeding under Art. 213 - 265 BL has two or three stages: 1) the preparatory stage, which is initiated by means of submission of the reorganisation plan and in which a decision is made concerning the permissibility of the plan and the plan is set forth; 2) the plan approval and confirmation stage, in which the plan is discussed at the hearing, voted upon and possibly confirmed, and 3) if appropriate following the confirmation of the plan, the stage of supervision of fulfillment of the plan. In structuring the legal institute of the reorganisation plan, the Croatian legislator was guided by the insolvency plan under the German Insolvency Law.

There are only few amendments concerning the adjudication order and the preliminary proceedings. Firstly, list of documents which the debtor must attach to the petition is extended; secondly, the provision on the amount of the so-called additional fee is amended; third, it is expressly stated when the provisional administrator can be appointed at the earliest; fourth, terminological changes.

b) Scope and Applicability

The parties that have capacity to become insolvent under the Bankruptcy Law are, firstly, all legal entities, as well as the expressly named physical persons (Art. 3 para. 1 BL). However, the scope with respect to legal entities is limited by a number of exceptions. These exceptions can be divided into two categories: some legal entities are absolutely excluded from insolvency, and other are relatively excluded. According to Art. 3 para. 2 BL, the Republic of Croatia, the funds financed by the state budget of the Republic of Croatia, the employee pension and disability funds, sole proprietors and individual farmers, the Croatian Health

Insurance Institute and the units of local self-administration and administration lack the capacity to become insolvent. A relative exception arises for a legal entity whose primary activity is the manufacture of weapons or military equipment or the rendering of services to the Croatian military. Insolvency proceedings can only be conducted in relation to these enterprises if the prior consent of the Defense Ministry is obtained. Consent is deemed to be given if refusal by the Ministry is not received within thirty days of receipt of the bankruptcy judge's notification concerning the commencement of the preliminary proceeding. If the Ministry refuses its consent, the Republic of Croatia is jointly and severally liable for the debtor's liabilities (Art. 3 para. 3 BL).

The Bankruptcy Law is applicable to two groups of physical persons, sole proprietors and individual farmers (individual debtors) (Art. 3 par. 1 BL). However, consumer insolvency is not possible under the Croatian Bankruptcy Law, in contrast to its German model.

c) Grounds for Opening Insolvency Proceedings

Capacity to become insolvent is the major pre-condition for opening the proceeding under the Croatian Bankruptcy Law, because it applies to all categories of debtors and all types of insolvency proceedings (Art. 4 BL). The debtor is insolvent if he is unable on a lasting basis to fulfill his monetary obligations that are due.

According to the original provision, insolvency was presumed if the debtor discontinued his payments for a period of 30 days without interruption. Firstly, the time period was extended by the second amendment. Secondly, a determination that a minimum of one fifth of the amount that should have been able to be satisfied by force of valid payment instruments without further consent by the debtor has not been disbursed from any account of the debtor with any legal entity that performs the payment transactions for the debtor is now sufficient as an

indicator of insolvency in lieu of discontinuation of payments (which was often very difficult to prove)[156] (Art. 4 para. 4 BL).[157]

Art. 4 para. 7 BL provides that the debtor can also file the petition for opening of the insolvency proceeding if he credibly shows that he will be unable to fulfill his obligations on the due date, thus even in the case of imminent illiquidity. Croatian law lists over-indebtedness as an additional ground for opening the proceeding (Art. 4 para. 8 BL). It is presumed that the debtor is overindebted if his assets no longer cover the existing liabilities. As in German law, the two-tier method is applied, so that a negative prognosis of continuation of the debtor's business is required.[158]

d) Persons Entitled and Persons Obliged to File the Petition

Art. 39 para.1 BL provides that the debtor or a creditor is entitled to file the insolvency petition. A creditor can file the petition if he credibly asserts the existence of his claim and the existence of one of the grounds for opening the proceeding. In cases in which the petition is brought by the debtor, he must attach the following documents: a confirmation from the legal entity that performs the payment transactions for him concerning the status of the funds in the account, as well as the unsatisfied claims that are supposed to be satisfied from the account (Art. 39 para. 8 no.1 BL). By the second amendment to Bankruptcy Law, an additional requirement for the debtor was introduced under Art. 39 para. 8 no. 2 BL that the debtor must attach a publicly certified asset inventory according to the provisions of enforcement law.[159] The debtor or the debtor's management are subject to criminal liability for statements in

[156] See M. Dika, Druga novela stečajnog zakona [The Second Amendment to Bankruptcy Law], in: Novosti u stečajnom pravu, p. 43.

[157] For further detail see N. Šepic, stečajni razlozi i prethodni postupak [Grounds for Bankrupcty and Preliminary Proceedings], Novosti u stečajnom pravu, pp. 53-54.

[158] See M. Dika, Das kroatische Insolvenzrecht [Croatian Insolvency Law], ROW 1998, volume 9, p. 342.

[159] Enforcement Law, "Narodne novine", no. 57/96.

the asset list in the same manner as for false testimony in judicial proceedings (Art. 39 para. 8 no. 2 sentence 2 BL).

In addition, a newly introduced provision stipulates that the court will reject the petition as incomplete, if the debtor does not attach the aforementioned evidence; no request of the court to the debtor for submission of the lacking documents is required any more (Art. 39 para. 9 BL). It was clarified that the judge terminates the proceeding if the petitioner withdraws his bankruptcy petition (Art. 40 para. 2 BL). In such case, the petitioner bears the procedural costs that accrue, unless the petition was withdrawn due to the subsequent satisfaction of creditor claims; in that case, the debtor must bear the accrued procedural costs. Since the first amendment to the Bankruptcy Law in 1999, a duty to petition for bankruptcy has also existed for the management bodies which are legal representatives of the debtor and for individual debtors; the petition must be filed within 21 days of the date of insolvency (Art. 39 para. 6 BL). If the parties obliged to bring the petition do not fulfil their duty, they are liable for damages to creditors in accordance with Art. 39 para. 7 BL.

Art. 41 para. 2 BL provides that the petitioner must advance a sum designated by the judge to cover the costs of the preliminary proceeding.[160] This duty to pay an advance, as well as the amount of the required sums, continues to be viewed as one of the reasons why petitions for the initiation of insolvency proceedings in Croatia are relatively rare.[161] The fact that the judge rejects the petition by order if the petitioner does not pay the advance within the deadline imposed upon him is new (Art. 41 para. 2 BL). In order to improve the position of the petitioner and in light of the fact that, in some cases, no special efforts are necessary to prove the ground for the opening of the proceeding, the

[160] Particularly concerning employees as petitioners, see M. Dika, Suminarni eliminacijski stečaj insolventnih duznika malog temeljnog kapitala [Summary Bankruptcy Proceeding Concerning the Separation of Insolvent Debtors with Small Capital Stock], in: Novosti u stečajnom pravu, p. 259.

[161] For further details see N. Šepic, Stečajni razlozi i prethodni postupak [Grounds for Bankruptcy and Preliminary Proceedings], in: Novosti u stečajnom pravu, p. 62, who also takes the position that the judges have often requested excessively high advances in order to "block" an impending avalanche of insolvency proceedings.

advance to cover the preliminary proceeding costs is, as of late, generally not required of a creditor who proves that the criterion for opening the proceeding exists by means of confirmation by a legal entity that performs the payment transactions for the debtor (Art. 41 para. 5 BL). Even in that case, however, the creditor is required to furnish the court fee and the supplementary fee for the conduct of the insolvency proceeding (Art. 39 a; 41 para. 5 BL).

Under the BL 2003, the debtor is obliged to attach also the decision on the real estate report or, if the debtor is a company established by transformation of a socially-owned enterprise, the certificate issued by the Croatian Privatisation Fund on real estate (Art. 39 para. 8 BL). Due to the extension of the list of documents to be attached by the debtor to the petition and imposing sanctions if the debtor fails to meet these requirements, it is made unnecessarily difficult for debtors to initiate insolvency.

Under the previous law, the fee for petition amounted to 5,000,00 kuna. By the BL 2003, it is increased to 10,000,00 kuna. Whereas the previous law prescribed that this fee had to be paid also by the Republic of Croatia, local self-government and government units when the same authorities of the previous law), the Republic of Croatia is not obliged to pay this fee under the BL. Debtor's present and former employees filing the petition in connection with their claims arisen from the employment relationship are also not obliged to pay the fee.

3. Institutional Framework

a) Courts

Art. 5 BL provides that the commercial court within whose district the debtor's domicile or location is situated has exclusive subject-matter and territorial jurisdiction over insolvency proceedings in Croatia. The

system of commercial courts consists of nine first instance courts in the cities of Bjelovar, Varaždin, Karlovac, Osijek, Slavonski Brod, Rijeka, Split, Dubrovnik and Zagreb. In addition, there is the Supreme Commercial Court in Zagreb as the second instance.

By the amendments of the Bankruptcy Law 2003, functional jurisdiction within the courts of first instance was radically changed. Under the previous law, the jurisdiction was divided between the so-called bankruptcy council and the bankruptcy judge. The bankruptcy judge could be a member, but not the president of the bankruptcy council. Key decisions on the conduct of bankruptcy proceedings were within the exclusive jurisdiction of the bankruptcy council. Outside the jurisdiction of the bankruptcy council, the bankruptcy judge was authorised to conduct and supervise the proceedings. The bankruptcy council, in its turn, supervised the work of the bankruptcy judge. Under the new BL, the bankruptcy council was abolished and the insolvency proceedings are now conducted by a sole judge (on his functions in the proceedings see Art.17 BL).

By contrast, functional jurisdiction of the court of appeal was not changed: decisions on appeals against the judgments of trial courts in insolvency proceedings are generally met by a panel of three professional judges (Art. 11 para. 7 BL). However, sole judge of the court of appeal is authorised to decide on the determination of territorial jurisdiction (Art. 68 para. 3 of the Code of Civil Procedure, Art. 6 BL) and on conflict of jurisdictions.

b) Administrator

The three amendments from 1999, 2000 and 2003 fundamentally changed the requirements to insolvency administrators. The third amendment to the Bankruptcy Law contained new requirements to qualification and business organisation of insolvency administrators. Art. 20 BL stipulates that only an attorney-at-law, a law firm with a business consultant as partner or a partner in a general partnership registered in the Commercial Register as an insolvency administrator (provided that the partner holds a "high work qualification" (level VII/I) and has passed the state examination for insolvency administrators) can now be appointed as insolvency administrator. This new provision is encountering

strong criticism, particularly among existing insolvency administrators[162]: In particular, criticism is levelled at the mandatory requirement of the association and registration of at least two administrators in a general partnership. Unlike a limited liability company (Croatian: d.o.o.), in which the liability is limited to the nominal capital, liability of partners in a general partnership is extended to their private assets, whereby they are also jointly and severally liable for any errors of other partners. Since, the critics contend, extremely large sums in insolvency proceedings are in most cases the subject matter of dispute, insolvencies are seldom completed without accusations and affairs, for which the administrators are usually blamed, so that the administrators will, from now on, be permanently operating on the brink of losing their personal assets. The new provision is also criticized because it is not explained why attorneys-at-law should be selected as administrators.

Beyond the requirements to the qualification and organisation, the third amendment to the BL left the other fundamental provisions concerning insolvency administrators unchanged. Independently of the appointment of the administrator by the bankruptcy judge, the creditors' committee can elect a different administrator, who need not be listed on the list of administrators, at the first or a later meeting (Art. 23 BL). In the case of breach of duty deliberately or by neglect, the administrator must compensate the creditors for the damage in accordance with Art. 28 para. 1 BL. After taking office, he must obtain liability insurance for damage caused as a result of or in connection with the exercise of office without delay (Art. 28 para. 6 BL).

By the amendment to the BL of 2003, new criteria for the determination of remuneration and compensation of costs of the administrator were introduced. According to Art. 29 BL, the judge is authorised to determine the remuneration of the administrator taking in consideration the specific characteristics of the respective proceeding and the total value of the insolvency estate.

[162] Concerning the points of criticism, see,e. g. Vecernji List of 17 September 2003: Stečajni upravitelji u šoku? [Bankruptcy Administators in Shock]).

Details of calculation are regulated in the Government Order.[163] An insolvency administrator receives a progressive fee amounting to a certain percentage (from 2% to 10%) of the sold debtor's assets. It ranges from a minimum of 10,000 kuna (approx. EUR 1,400) to a maximum of 300,000 (approx.EUR 45,000).

A special fund was created to secure the insolvency proceeding costs for the cases in which, due to lack of assets, the costs of proceedings cannot be covered from the proceeds (Art. 39a BL). In practice, it became apparent that, contrary to the original planning, such costs could not be paid from the budget of commercial courts.[164] Therefore, an additional fee amounting to 5,000 kuna (since 30 August 2003 10,000 kuna) is imposed on creditors initiating the insolvency proceeding in regular proceedings (Art. 39a para. 1 BL) and 2,000 kuna in small proceedings with the value of debtor's assets of up to 2,000,000 kuna (Art. 300 para. 5 BL). This additional fee is paid into the account of the competent commercial court. Art. 39a para. 3 BL provides that (former) employees of the debtor who file the insolvency petition on the basis of their outstanding claims for wages are excepted from the duty to pay. The paid-in court fee and the additional fee are costs of the insolvency proceeding, which can be reimbursed to the creditor (Art. 39a para. 4 BL).

c) Creditors' Meeting

The creditors' meeting as a party to insolvency proceedings was not expressly regulated in the Bankruptcy Law until 2000. However, it could be concluded on the basis of the existing provisions that such body already did exist under the Bankruptcy Law 1996. A comprehensive and relatively detailed regulation was introduced in 2000.

[163] Government Order on the Rules on Insolvency Administrator Fees of 25 November 2003 (Uredba o kriterijima I nacinu obracuna I placanja nagrade stečajnim upraviteljima).

[164] See M. Dika, Druga novela stečajnog zakona [The Second Amendment to Bankruptcy Law]), in: Novosti u steajnom pravu, p.41.

Under the effective BL, the creditors' meeting is comprised of all creditors, including a representative of the employees, unless their claims are neglectably small, and, since 2003, of the representatives of the tax administration for public claims. The tax administration represents not only tax claims, but all claims of the state, state budget funds, the Croatian Health Insurance Institute and the Croatian Employment Office. This is a deviation from the general rules of procedure according to which the state is generally represented in the proceedings by the Public Prosecutors Office.

4. Insolvency Proceedings

a) Effect of Commencing the Insolvency Proceeding

aa) Effects of the Petition

The petition itself can lead to protective measures for the debtor's assets.[165] In the court order on the commencement of the preliminary proceeding, the judge can name a provisional administrator, to whom the authority to administer and dispose of the debtor's assets passes in such case (Art. 45 para. 1 BL). The rights and duties of the provisional administrator are strictly modelled on the German Insolvency Law.

Thus, two procedural possibilities are also provided in the Bankruptcy Law: If a provisional administrator is appointed and a general restraining order is imposed on the debtor, the administrator's duties and authority are determined by law, i.e., particularly Art. 45 para.1

[165] For further details see V. Buljan, Predhodni postupak i pravne posljedice otvaranja stečajnog postupka [The Preliminary Proceeding and the Legal Consequences of the Opening of Insolvency Proceedings in Croatian Law], in: Zbornik radova pravnog fakulteta u Splitu, Split 2000, pp. 241-252.

sentence 2 nos. 1-3 and para. 2 BL. If a provisional administrator is appointed without the imposition of a general restraining order on the debtor, the court determines the duties of the provisional administrator. However, they may not exceed the duties under Art. 45 para. 1 sentence 2 and para. 2 (Art. 45 para. 3 BL). The authority to administer and dispose of the debtor's assets also does not pass to the provisional administrator in such case.

As a result of the second amendment, the authority of the judge to secure the debtor's assets during the preliminary proceeding is substantially expanded with respect to the group of affected persons. E. g. the judge can now take preliminary protective measures under the enforcement law, including measures against the garnishees, if this is viewed as necessary in order to secure the debtor's assets upon the application of the provisional administrator, the creditors or ex officio (Art. 44 para. 6 BL). This means that the court can impose relevant prohibitions on the garnishees, e. g. with respect to the disposal of assets, as far as this is deemed necessary to securing the debtor's assets.[166]

In addition, the acceptance of indebtedness or co-assumption of debt was also modified in the chapter concerning the preliminary proceeding. E. g. the judge consents to the co-assumption of debt in accordance with Art. 50 para. 3 BL if the assuming party promises to satisfy all of the debtor's obligations that are due within a period of two months from the date of the consenting order concerning co-assumption of debt and satisfy the residual obligations already existing at the time of the debt accession on their due date. The changes of acceptance of indebtedness are criticized in the literature due to terminological imprecisions.[167] E. g. it is pointed out that the same section alternates between referring to acceptance of indebtedness (in the unamended provisions) and co-assumption of debt (in the amended provisions). Based on the background of the amendment's intention to replace acceptance of indebted-

[166] See M. Dika, Druga novela stečajnog zakona [The Second Amendment to Bankruptcy Law], p.41, in detail see N. Šepic, Stečajni razlozi i prethodni postupak [Grounds for Bankruptcy and Preliminary Proceedings], p. 65, both in: Novosti u steajnom pravu.

[167] See M. Dika, Druga novela stečajnog zakona [The Second Amendment to Bankruptcy Law], in: Novosti u stečajnom pravu, p. 44.

ness with co-assumption of debt, it is contended that the pertinent provisions must be interpreted in such a manner that they all relate to co-assumption of debt, not to acceptance of indebtedness.[168]

bb) Effects of the Commencement

The effects of the commencement of insolvency proceedings are specified in Art. 88 et seq. BL, which are binding. Contractual provisions that would exclude or restrict the provisions of the BL a priori are null and void (Art. 126 BL). Effects of the commencement apply from the date on which the notice on commencement is posted on the court noticeboard (Art. 88 BL). According to Art. 89 BL, the rights of the management body of the debtor, who is a legal entity, end and are devolved to the administrator. With the commencement of the insolvency proceedings, the rights of the individual debtor to manage and dispose of the assets belonging to the insolvency estate are also devolved to the administrator (Art. 89 sentence 1 and 2 BL).

The insolvency estate is formed with the commencement of the insolvency proceedings. According to Art. 67 para. 1 BL, the insolvency estate comprises all assets owned by the debtor at the time of the commencement as well as any assets acquired during the proceedings. According to Art. 67 para. 2 BL, the insolvency estate is used for covering the costs of the proceeding and to settle the claims of creditors, including secured claims. Those assets of the individual debtor in relation to which execution were prohibited, if the debtor were not a sole proprietor, are not included in the insolvency estate, Art. 68 BL.

The commencement proceedings has numerous other effects in addition to those described above. The most important of these include:

- claims against the insolvency estate that are not yet due become due (Art. 73 BL);
- rights of creditors to separation of assets or similar rights acquired by execution or by temporary restraining order thirty days or less before

[168] M. Dika, Suminarni eliminacijski stečaj insolventnih duznika malog temeljnog kapitala [Summary Bankruptcy Proceeding Concerning the Separation of Insolvent Debtors with Small Capital Stock], Novosti u stečajnom pravu, p.259.

the petition for bankruptcy was filed expire upon commencement (Art. 97 BL);
- An order prohibiting disposals and encumbrances issued against the debtor according to general provisions with the sole intent of protecting certain individuals becomes ineffective once bankruptcy proceedings have commenced, unless these prohibitions were imposed in connection with execution proceeding or with a temporary restraining order (Art. 90 BL);
- The exercise of set-off rights to which the debtor is entitled by law or by contract at the time the petition is filed is generally not restricted after the commencement proceedings, whereby special provisions apply to the set-off of claims that are subject to a condition precedent and are not yet due (Art. 103-105 BL).

Art.110 et seq. BL specifies the effects of the commencement with respect to legal transactions concluded by the debtor before the petition was filed. Here is an overview of some of the most important of these:
- The rent or lease of real estate does not end with the commencement. Those rights concerning the time before the commencement can only be asserted by the other party as a creditor. The rules applying to the termination and cancellation of such contracts are subject to special rules (Art. 115-119 BL);
- Employment or service contracts the debtor entered into as employer do not automatically end with the commencement. However, the commencement is a ground for termination of such contracts. The employment contract may be terminated by the administrator on behalf of the debtor as employer or by the employee, irrespective of the agreed term of the contract or an agreed exclusion of the right to regular notice of termination and irrespective of legal or contractual provisions concerning the protection of employees. The period of notice is one month (in Germany, three months), unless a shorter period is stipulated by law. In the case that the administrator gives notice, the other party is entitled to compensation for premature termination of the employment contract as a creditor (Art. 120 BL). One of the changes introduced by the second amendment concerns the status of wages and other earnings from the employment relationship to which a claim has arisen after the commencement. Such

claims are satisfied in the first priority (Art. 120 para. 7; 87 para. 1 no. 5 BL).

- Offers submitted to or by the debtor become void in the case that they have not been accepted by the date of commencement (Art. 123 BL).

Upon the commencement, all proceedings from which claims of or against the insolvency estate are interrupted. According to Art. 96 BL, the creditors can only assert claims against the debtor in the course of insolvency proceedings. Pending execution proceedings or proceedings aimed at a temporary restraining order must be interrupted, with the exception of such proceedings initiated by creditors with a right to separation or segregation of assets who are entitled to initiate proceedings also after commencement of insolvency proceedings (Art. 98 para. 4 and 5 BL).

The second amendment resolves a controversial question whether the creditors can assign claims against the debtor, and if so, with what legal consequences: If the creditor assigns a claim the notice of which was not given in the insolvency proceedings after the commencement, the assignee of the claim can only have the same rights in the insolvency proceeding that the assignor would also have had, unless otherwise stipulated by law (Art. 78a para. 1 BL). If the creditor assigns a claim notice of which was given in the current insolvency proceedings, the assignee of the claim assumes the legal status of the assignor, unless otherwise stipulated by law (Art. 78a para. 2 BL). An assignment of such claims can only be proven in the insolvency proceedings by means of a public or publicly certified document, or if the creditor confirms the assignment by means of a statement made in court (Art. 78a para. 3 BL). By the amendment of Art. 95 BL, the German provisions of §§ 84, 85 of the Insolvency Law were transferred into the Croatian law. According to the amended provisions of the BL, actions affecting property forming part of the insolvency estate pending for the debtor as plaintiff on the day of commencement of the insolvency proceeding may be recommenced by the insolvency administrator in the name and on behalf of the debtor. Under identical conditions, actions pending for the debtor as defendant can be recommenced by the administrator only if these concern a separate claim or a separate object from the insolvency estate, a separate settlement or liabilities of the insolvency estate. If the admin-

istrator recommences the proceedings and loses the case, the costs of the civil proceeding paid by the creditor are compensated to him from the insolvency estate (Art. 95 para. 3 BL).

b) Rescission and Invalidity

The provisions on rescission and invalidity (Art. 127-144 BL) correspond verbatim to the respective provisions of the German Insolvency Law (§§ 129-147). Legal acts (and failing to act according to Art. 127 para. 2 BL) which were performed before the commencement of insolvency proceedings and are detrimental to the equitable satisfaction of creditors (detrimental treatment of creditors) or benefit individual creditors at the expense of other creditors (preferential treatment of creditors) can be rescinded, whereby the administrator in the name of the debtor and the creditors are entitled to apply for rescission (Art. 127 BL). A legal act is deemed as performed when its legal consequences become effective (Art. 138 BL).

The key provision in the section on rescission and invalidity is Art. 141 BL. Pursuant to this provision, the action for rescission of legal acts can be filed within two years after the commencement and before the end of the insolvency proceeding. The defendant is the person to whose benefit the legal act was performed or against the debtor if he is not the claimant. If the action is sustained, the rescinded legal act has no effect on the insolvency estate and the other party is obliged to transfer all benefits obtained in connection with the legal act to the insolvency estate. The recipient of a gratuitous transaction or of a transaction for a small consideration must return the acquired object only if he is enriched by it, unless he knew or ought to have known about the detriment to insolvency creditors as a result of the transaction. The legal acts of the debtor can be rescinded by an objection in law to an action.

By the second amendment, only the term within which a legal act performed by the debtor to intentionally discriminate the creditors can be rescinded, if the other party knew the intention of the debtor: it was extended from five to ten years (Art. 131 para. 1 BL). The Croatian lawmaker followed here the German law (§ 133 para. 1 German Insolvency Law) which provides extensive protection to the creditors by the exceptionally long term of ten years.

c) Reorganisation

The introduction of a insolvency plan is regarded as the most important aspect of the 1996 bankruptcy law reform in the Republic of Croatia.[169] According to Art. 213 sentence 2 of the Bankruptcy Law, a bankruptcy plan can be used for the purpose of reorganisation in any of the following ways:

- The debtor may be allotted some or all of the insolvency estate in order to continue business activities;
- Part or all of the insolvency estate may be transferred to one or more existing legal entities or to a legal entity to be formed;
- A merger by integration of another legal entity or by forming a new legal entity with one or more other legal entities can be conducted;
- All or part of the debtor's estate may be sold, with or without rights to separation of assets;
- All or part of the debtor's estate may be distributed among the creditors;
- The method of settling the creditors' claims may be determined;
- Settlement or modification of the creditors' rights to separation of assets;
- Reduction or forbearance of the debtor's liabilities;
- Debt-to-equity-swap;
- establishing a surety or other securities to ensure repayment of the debtor's obligations;
- Decision on the debtor's legal liability after the end of insolvency proceedings etc.

The reorganisation procedure acc. to Art. 213-265 of the Bankruptcy Law consists of two or three stages: 1) preliminary proceedings, 2) approval and confirmation of the insolvency plan, and if the plan is confirmed, 3) supervision of the plan implementation. The bankruptcy plan consists of a preparatory part and an implementation part (Art. 215 BL). The preparatory part specifies measures which are yet to be taken or have been taken before the commencement of the insolvency pro-

[169] See J. Garašic, Sadrcaj stečajnog plana (The insolvency plan), in: Novosti u stečajnom pravu (collected volume), pp. 229-257.

ceeding in order to establish a foundation for the intended satisfaction of the participants' claims. The preparatory part must also contain all details on basic regulations and effects of the plan pertaining to the decisions of the creditors in relation to the plan and its confirmation by the court (Art. 216 BL). According to Art. 217 BL, the implementation part specifies how the insolvency plan affects the legal situation of the debtor and the other participants of the proceedings. According to Art. 230 BL, the insolvency plan and all related supplements, modifications and received statements must be submitted to the registry of the competent court for examination by the participants of the proceedings.

After the plan was presented at the registry of the court and the administrator presumes that it meets formal requirements, the judge sets a date for discussion and approval of the plan. Once the creditors and debtor have approved the plan, the judge decides whether to confirm the plan in accordance with Art. 244 BL. According to Art. 246 BL, the judge may reject the bankruptcy plan if the provisions concerning content, preparation or attachments to the plan, approval by creditors or the debtor were substantially violated, unless these formal defects can be cured. The judge may also decide to reject the plan if approval of the plan was gained by an inadmissible method, particularly by preferential treatment of individual creditors. A creditor may apply for the plan to be rejected only if the relevant objections are submitted no later than at the creditors' meeting where the decision on the approval must be made, and if the plan would achieve a less satisfactory outcome for the creditor (Art. 247 BL). According to Art. 249 BL, both the debtor and the creditors may appeal against the court order on the plan.

The confirmed plan is effective towards all participants from the date of confirmation by the court (Art. 250 BL). If the plan specifies that rights to parts of the insolvency estate are to be defined, modified, cancelled or transferred to a limited liability company, the participants' declarations of intent contained in the court order will be considered as proper legal submissions. The same applies to all declarations contained in the court order regarding the assumption of liabilities based on the definition, modification, transfer or cancellation of rights to the insolvency estate, or based on the transfer of business units and shares. This also applies to creditors who have failed to give notice of their claims, and to participants who have appealed against the plan (Art. 250 sentence 1 BL). According to Art. 250 sentence 2 BL, the plan only applies to those

creditors with rights to separation of assets who have approved the plan; this is a deviation from the German Insolvency Law, which has otherwise served as a model for the Croatian rules on reorganisation. According to Art. 254 BL, the judge must terminate the insolvency proceedings as soon as the court order confirming the plan becomes final. As specified in Art. 255 BL, the debtor regains free access to the insolvency estate.

Supervision over the implementation of the plan is only exercised if this is specified by the court order confirming the plan. The court order may further specify that supervision also encompasses the settlement of creditor claims against companies formed after the commencement of insolvency proceedings for purposes of takeover or succession of the debtor's company (takeover company) (Art. 256 BL). The second amendment to the BL modified several of the regulations regarding the insolvency plan. The plan can be used both for reorganisation and liquidation, so that rules on realisation of property and distribution of assets deviating from regulations of the BL can be laid down in the plan and applied if the plan is approved (Art. 214 sentence 1 BL).[170] In keeping with the legislative intention of simplifying insolvency proceedings, the law now prescribes that the creditors shall no longer be divided into groups for the voting on the plan if they are treated equally under the plan (Art. 218 sentence 4 BL).

d) Status of Secured Creditors

Compared to previous regulations, the legal position of creditors with right to separation of assets was strengthened by the 1996 Bankruptcy Law. According to Art. 81-83 BL, creditors whose claims are secured by pledge, right of retention, or a chattel mortgage are entitled to separate and preferential settlement of claims from the proceeds of the sale of the collateral. According to Art. 83 sentence 4 BL, the state and the municipalities as creditors have the same legal status as creditors with rights to separation. Such creditors are also general insolvency creditors if the

[170] See M. Dika, Druga novela stečajnog zakona (The Second Amendment to the Bankruptcy Act), in: Novosti u stečajnom pravu, p.48.

debtor is personally liable to them. However, they are only entitled to their settlement portion of the insolvency estate if they renounced the separate satisfaction, or if separate satisfaction was unsuccessful (Art. 84 BL). In the court order on commencement, these creditors are requested to give notice of their separate rights (e.g., to movable goods or rights of the debtor not entered in registers) to the administrator within fifteen days. The notice must contain the collateral, the nature and origin of this right, and the secured claim. However, if the creditors do not give notice on the rights to separation, they do not automatically lose the right to separate satisfaction (Art. 173a para. 3 BL), but they can lose the right if the right to separation was not registered, the administrator did not know and ought not to know about this righ and the collateral is sold (Art. 174a para. 4 BL).

e) Realisation of Debtor's Property

The provisions on realisation of debtor's property are largely based on the German Insolvency Law. At the report meeting, the creditors may decide on the methods and conditions of realisation of debtor's assets according to Art. 156 sentence 2 BL. After the report meeting, the administrator must immediately realise all the assets belonging to the insolvency estate, as far as this is not contrary to the creditors' decision (Art. 158 BL). In order to accelerate insolvency proceedings, Art. 155a was added by the third amendment to the BL, according to which the judge must call the creditors' committee within six months from the report meeting in order to decide on the further course of the proceedings according to Art. 155a para. 2 BL. By the third amendment to the BL, para. 5 was inserted in Art. 192 BL according to which the judge must arrange the final hearing not later than 2 years after the commencement of the insolvency proceeding, unless exceptional circumstances justify a further delay of this date.

Art. 164-172 BL contain special regulations on the realisation of collaterals subject to rights to separation. According to these regulations, the judge is obliged to sell real estate subject to the right to separation upon application of the administrator according to the rules of execution proceedings (Art. 164 BL). The same procedure applies to the sale of ships, ships under construction, aircrafts, and, since the second amend-

ment to the BL, also the sale of rights entered in the public registers. The administrator may independently sell movable property of the debtor subject to rights to separation that are in his possession.

There are further special regulations on the protection of creditors from delays of realisation, on the distribution of the proceeds, on the calculation of costs, and on the use of movable property subject to rights to separation (Art. 167-171 BL). According to Art. 172 BL, the creditor has the right to realise property or claim if the administrator is not authorised to do so. One of the main reasons behind the second amendment to the BL to create conditions for a fast and efficient transfer of the debtor's property in order to enable continuation of the existing or changed business activity with the same and/or new employees.[171] For that reason, special regulations on the sale of the debtor's enterprise as a going concern were introduced, which deviate from the general rules of reorganisation on the basis of a plan.[172] The new regulations are contained in Art. 163a-m BL. The sales contract is concluded between the debtor as the seller and the purchaser. The purchaser can also be a foreign physical person or a foreign legal entity.

The administrator must advertise the sale of the debtor's estate as a whole in the law gazette and at least one daily newspaper. According to Art. 163a BL, movable property and claims of the debtor belonging to the insolvency estate are subject to the sales contract, unless they are excluded by the provisions of this article or by contract. E. g. property subject to rights to separation or segregation can be excluded from sale by contract. On the other hand, other objects than those within the insolvency estate can be included in the sales contract, e. g. for example, takeover of employees, goodwill and trading name. The judge may only confirm or reject this contract (Art. 163c BL), but not change its contents; the contractual agreement exists exclusively between the legal parties involved. Every insolvency creditor or creditor with rights to separation is entitled to immediately appeal against the court order.

[171] See M. Dika, Druga novela stečajnog zakona (The Second Amendment to the Bankruptcy Law), in: Novosti u stečajnom pravu, p.47.

[172] For further details see J. Barbic, Prodaja imovine stecajnog duznika kao cijeline, (The Sale of the Debtor's Property as a Going Concern), in: Novosti u stečajnom pravu, pp. 189-227.

f) International Insolvency Law

The 10th chapter of the BL contains detailed regulations concerning international insolvency law. In the course of preparing the draft of the provisions on international insolvency law, the following provisions of foreign laws were considered: draft of the German Insolvency Law (§§ 379-399), the Swiss Federal Law on Private International Law (Art. 166-175), the European Council's "European Convention on Certain International Aspects of Bankruptcy" from 1990, and the European Union's "Convention on Insolvency Proceedings" from 1996.[173] International jurisdiction for opening the insolvency proceedings, the applicable law, the conditions, procedure and effects of the recognition of foreign court orders on opening the insolvency proceedings and of foreign enforcement compositions and other insolvency procedures are regulated in the BL. According to Art. 301 BL, insolvency proceedings against debtors whose centre of main interests is located in Croatia are within exclusive jurisdiction of Croatian courts. It is assumed that the debtor's centre of main interests is where his location is according to the registration. According to the principle of universality, insolvency proceedings concern all assets of the debtor, including those located outside of Croatia (Art. 301 sentence 2 BL). If it can be proven that the centre of the debtor's interests is outside of Croatia, but the debtor is registered in Croatia, the Croatian courts have exclusive jurisdiction for opening insolvency proceedings against this debtor if opening of insolvency proceedings on the basis of the centre of main interests is impossible under the law of the state where the centre of the debtor's main interests is located. Conversely, if the debtor is registered in another country, but his centre of main interests is in Croatia, insolvency proceedings can be opened by a Croatian court in whose district the centre of the debtor's main interests is located (Art. 301 para. 1 and para. 3 BL).

Apart from main proceedings, Croatian courts can conduct territorial proceedings. The regulation of territorial proceedings corresponds to the provisions of the Council Regulation no. 1346/2000. A foreign decision on insolvency proceedings can be recognised if the courts or other state institutions of the foreign country have international jurisdiction in this

[173] See M. Dika, Croatian Insolvency Law, ROW 1998, Volume 9, p. 355.

matter according to Croatian law, the decision is enforceable according to the law of the state where it is made and the recognition does not violate the Croatian ordre public (Art. 311 para. 1 BL).

g) Criminal Offences in Connection with Bankruptcy

The provisions of the BL prevailingly regulate civil liability. An exception constitutes Art. 39 para. 8 BL. According to this provision, the insolvent debtor is required to attach a legally certified inventory of assets to the petition for insolvency proceedings. If the debtor falsifies this list in any way or makes any false statements in the court proceedings, he can be subject to criminal liability. If criminal liability can be proved, general regulations of the Croatian Criminal Code apply.

5. Summary and Perspectives

Problems in connection with the insolvency proceedings in Croatia are by no means caused by the legal regulations. Great parts of the 1996 Bankruptcy Law, supplemented by three amendments of 1999, 2000 and 2003, are based on the German Insolvency Law, and the quality of the law is high.[174] A very positive aspect of the BL is the detailed and comprehensive regulation of the international insolvency law.

[174] Cf. e.g. the assessment in EBRD Legal Indicator Survey: Assessing insolvency laws after ten years of transition; individual country assessments (2000).