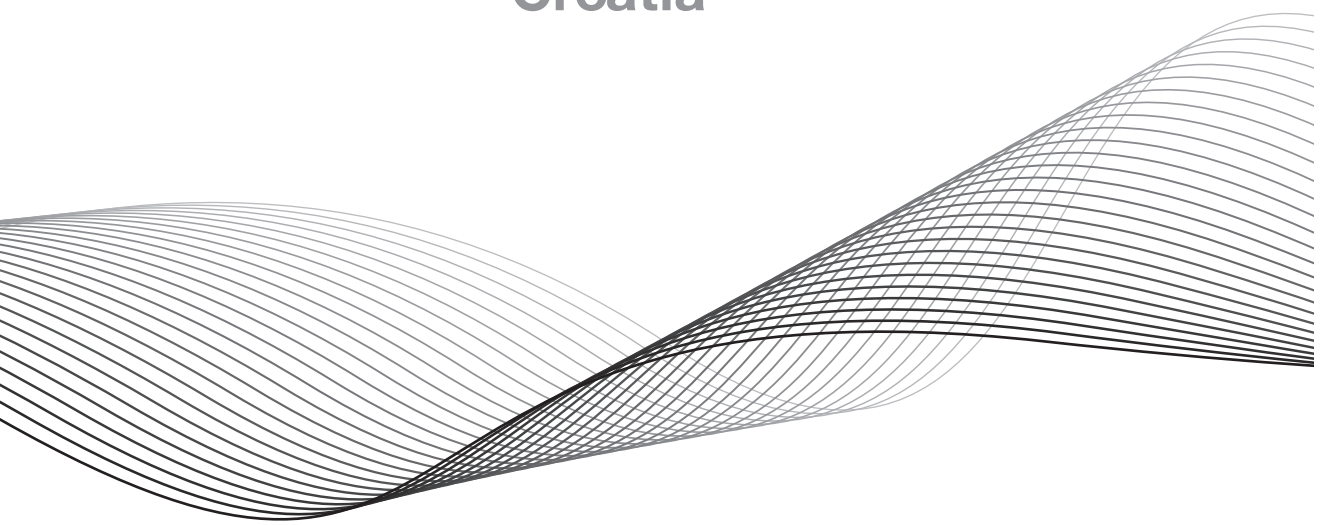
Doing Business

Croatia



BABIĆ & PARTNERS

DOING BUSINESS IN CROATIA

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This book is the result of efforts of Babić & Partners to prepare an illustrative guide to the legal framework for doing business in Croatia. The need for such a guide has been expressed by several of our clients, and in response to such requests, we are presenting this publication as one of the first attempts by a Croatian law firm to prepare an overview of the Croatian legal system with particular focus on business issues.

The publication is intended to give a broad overview of the Croatian legal system and to encompass all legal issues which are generally considered relevant in the context of conducting business. The information included in this publication is for informational purposes only and is not offered as legal or any other advice on any particular matter. This edition of "*Doing business in Croatia*" has been prepared on the basis of laws and regulations which were in force as at February 2013 and may not reflect the most current legal developments.

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We hope the readers of this publication will find it of interest, and we welcome any comments.

Babić & Partners
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TABLE OF CONTENTS:

1. GENERAL OVERVIEW 1
1.1. Geography and Population 1
1.2. Political System 1
1.3. Economic Indicators 1
1.4. Membership in International Organizations 2
1.5. Foreign Investments and Related Requirements 2
2. ESTABLISHING LEGAL PRESENCE IN CROATIA 4
2.1. Forms of Business Entities 4
2.2. Liability 5
2.2.1. Partnerships 5
2.2.2. Corporations 5
2.3. Formation 5
2.3.1. Partnerships 5
2.3.2. Corporations 5
2.4. Corporate Governance 6
2.4.1. Partnerships 6
2.4.2. Corporations 6
2.5. Affiliated Companies 9
2.6. Branch and Representative Offices 9
3. TAXATION 11
3.1. General 11
3.2. Corporate Profit Tax 11
3.3. Personal Income Tax 12
3.4. VAT and Excise Duties 12
3.5. Tax Audit and Penalties 12
3.6. Investment Incentives 13
3.7. Accounting and Audit 13
3.7.1. Accounting 13
3.7.2. Audit 14
4. EMPLOYMENT 16
4.1. Legislative Structure 16
4.2. Employment Contract 16
4.3. Probationary Period 16
4.4. Temporary Employment Agencies 16
4.5. Working Time 16
4.6. Holidays, Days Off and Vacation 17

4.7. Salaries 17
4.8. Termination of Employment 17
4.9. Expatriates Working in Croatia 18

5. REAL ESTATE 19
5.1. General overview 19
5.2. Regulatory 19
5.2.1. Acquisition of Real Estate by Foreign Nationals 19
5.2.2. Registration of Title and Charges 19
5.2.3. Construction Permits 20
5.2.4. Restrictions of acquisition 20
5.3. Taxes 21

6. EXCHANGE CONTROL 22

7. BANKING AND FINANCE 23
7.1. Operation of Banks 23
7.1.1. Sources of Law 23
7.1.2. License and Banking Services 23
7.1.3. Corporate Form and Capital Requirements 23
7.1.4. Management Board Requirements 23
7.1.5. Acquisition of Banks 24
7.1.6. Exposure Limits and Restrictions of Investments 24
7.1.7. Risk Management and Supervision 25
7.1.8. Role of the Croatian National Bank 25
7.2. Operation of Other Financial Institutions 25
7.2.1. Regulatory Authority: HANFA 25
7.2.2. Insurance 25
7.2.3. Investment Funds 26
7.2.4. Pension Funds 27
7.2.5. Investment Services and Investment Activities 27
7.2.6. Other Financial Services 27
7.3. Money Laundering 27

8. SECURITIES 29
8.1. Legislative Structure and Regulatory Authority 29
8.2. Issuance of Securities 29
8.3. Trading in Securities 29
8.4. Prohibited Activities 30

9. COMPETITION LAW 31
9.1. Relevant Legislation 31
9.2. Enforcement 31
9.3. State Aid 32

10. INTELLECTUAL PROPERTY 33
10.1. OVERVIEW 33
10.2. TRADEMARKS 33
10.3. PATENTS 33
11. DISPUTE RESOLUTION 35
11.1. COURTS 35
11.2. ARBITRATION AND ADR 35
12. CONCESSIONS 36
13. PRE-BANKRUPTCY SETTLEMENT AND BANKRUPTCY 37
14. PUBLIC PROCUREMENT 39
15. APPENDIXES 40
15.1. BILATERAL INVESTMENT TREATIES 40
15.2. DOUBLE TAX TREATIES 42

1. GENERAL OVERVIEW

1.1. Geography and Population

Croatia is situated in Central Europe along the eastern coast of the Adriatic, bordering Slovenia, Hungary, Serbia, Montenegro and Bosnia and Herzegovina. It has a maritime border with Italy.

The total area of Croatia is 87,661 m^2, comprising 56,594 m^2 of land and 31,067 m^2 of territorial waters. Croatia has a coastal line of 1,778 km in length and 1,185 islands. According to the preliminary results, at the time of the 2011 census, Croatia had a population of 4.29 million[1]. The capital of Croatia is Zagreb, which has a population of about 800,000. Other major cities are Split, Rijeka, Osijek, Zadar, Šibenik and Dubrovnik.

1.2. Political System

The Republic of Croatia is a parliamentary democracy. The core principles of the Croatian Constitution are freedom, equal rights, national equality, peace, social justice, respect for human rights, the inviolability of ownership, the preservation of nature and the human environment, the rule of law and a democratic multiparty system.

Legislative powers are vested with the Croatian Parliament ("*Sabor*"), the body of people's representatives elected for a term of four years. Executive powers are vested with the Government, which is responsible to the Parliament. Judicial powers are vested in the judiciary, with the Supreme Court of Croatia ultimately ensuring uniform application of law and equality of all citizens. The President of the Republic, who is elected for the term of five years, is the chief of state who represents Croatia at home and abroad. The Constitutional Court supervises the constitutionality of laws and protects the constitutional rights of the citizens.

Croatia is a unitary republic divided into 20 counties ("*županije*") and the City of Zagreb, which constitutes a separate administrative unit.

1.3. Economic Indicators

The national currency of Croatia is the Croatian Kuna (HRK). Kuna is a relatively stable currency, with the annual level of inflation of about 5.2%. The current exchange rates are: 1 EUR = 7.59 HRK; 1 USD = 5.82 HRK; 1 GBP = 8.76 HRK; 1 CHF = 6.20 HRK[2].

[1] Source: Central Bureau of Statistics (http://www.dzs.hr/); preliminary results of 2011 census available at: http://www.dzs.hr/Hrv_Eng/publication/2011/SI-1441.pdf

[2] Croatian National Bank's middle exchange rates applicable on 3 March 2013.

Certain economic indicators for 2012 are set out in the table below[3]:

GDP, billion EUR	33.395
GDP per capita, EUR	10.480
Industrial production growth rate (%)	-5.5
Inflation rate (%)	5.2
Unemployment rate (%)	21.9%
Exports, million EUR	9.582
Imports, million EUR	16.281
Balance of payments – current account, million EUR	-393.9
Consolidated general government balance (as % of GDP)	-5.8
Average monthly gross salary, EUR	1039.77
CNB's discount rate (%)	7
CNB's international reserves (billion EUR, end of period)	11.080
Number of active companies (31 March 2012)	136.239
Number of banks	30
Persons in employment	1.522

1.4. Membership in International Organizations

Croatia is a candidate country for the accession to the European Union.

The Stabilization and Association Agreement between Croatia and the European Community and its member states was signed in 2001 and has come into force on 1 February 2005. Croatia formally closed the accession negotiations on 30 June 2011, and subsequently signed the Treaty of Accession on 9 December 2011. The Treaty of Accession is expected to come into force on 1 July 2013.

Croatia is a member of a number of international and regional organizations, including the United Nations (UN), the World Trade Organization (WTO), the International Monetary Fund (IMF), the World Bank, the European Bank for Reconstruction and Development (EBRD) and the Central European Free Trade Association (CEFTA).

1.5. Foreign Investments and Related Requirements

Croatian corporate law affords national treatment to foreign investors. Foreign investors may establish partnerships, companies or branch offices under conditions applicable to domestic persons. Foreign persons may invest freely under condition of reciprocity, which is presumed. The reciprocity requirement is not applied with respect to investors domiciled in a member state of WTO.

For almost all industries, the Croatian law imposes no restrictions of foreign ownership. Foreign investors are guaranteed free transfer and repatriation of profits and repatriation of the capital invested under the Croatian Constitution. The Constitution stipulates that rights acquired through investment may not be diminished by law or any other legal act.

[3] Source: Central Bureau of Statistics (http://www.dzs.hr), Croatian Chamber of Economy (http://www2.hgk.hr/en), Croatian National Bank (http://www.hnb.hr/eindex.htm), Ministry of Finance (http://www.mfin.hr/en)

Transactions having a character of foreign investment and satisfying certain thresholds (e.g. acquisition of more than 10% of shares of domestic company) have to be reported to the Croatian National Bank. Reporting obligations are placed on the Croatian entities (companies whose shares have been acquired by the foreign investor or Croatian branch office of the foreign investor). The Croatian National Bank may also request such domestic companies or branch offices to fill out a survey form related to foreign investments.

Generally, there are no requirements as to nationality or residence for Croatian company directors or members of other corporate bodies concerning their appointment. There are exemptions to the above rule for particular industries, such as banking.

2. ESTABLISHING LEGAL PRESENCE IN CROATIA

2.1. Forms of Business Entities

The principal law governing business organizations in Croatia is the Commercial Companies Act (CCA). It was enacted in 1993, entered into force in 1995 and was amended in 1999, 2000, 2003, 2007, 2008, 2009 and 2012. The statute is modelled on German and Austrian laws.

The CCA introduces five types of commercial entities:

- general commercial partnership;
- limited partnership;
- joint stock company;
- limited liability company and
- economic interest grouping.

There are two principle types of business organizations - commercial partnerships and corporations. Both commercial partnerships and corporations are legal entities. Among commercial partnerships the law distinguishes between general commercial partnership and limited partnership. The two types of corporations are the joint stock company and the limited liability company.

CCA also recognizes economic interest groupings. The rules on economic interest groupings implement European Community law (EC Directive on European Economic Interest Groupings). It defines an 'economic interest grouping' as a legal person set up by two or more natural persons or legal entities for the purpose of (i) facilitating or promoting their business activities and (ii) promoting or increasing the effect of these activities. An economic interest grouping may not retain profits.

Investors can generally choose between these types of business entities. However, certain enterprises must take on a particular form. Banks, for example, can only be organized as joint stock companies.

CCA also contains rules on silent partnerships, although these are not considered legal entities. A silent partnership is established by contract. One person (the silent partner) contributes value to the enterprise of another person (the entrepreneur) and on the basis of this contribution participates in the division of profits or losses. Relations between the silent partner and the entrepreneur are regulated by contract. The contract does not affect third parties. With relation to third parties, only the entrepreneur can represent the silent partnership.

Croatian law also recognizes civil partnerships. Civil partnership does not fall under the general discipline of company law. It is a contractual relationship between persons who pursue a common goal. It has no legal personality of its own. There are no formal requirements for the formation of a civil partnership so the agreement between the partners can be deemed to be formed by implication. Given that civil partnership has limited importance in Croatian practice of business law, this overview will only discuss commercial partnerships.

In October 2007 Croatian Parliament enacted the Act on Introduction of the European Company and European Economic Interest Grouping. This statute implements the Council Regulation (EC) No. 2157/2001 of 8 October 2001 on the Statute for a European company (SE) and the Council Regulation (EEC) No. 2137/85 of 25 July 1985 on the European Economic Interest Groping (EEIG) thus creating possibility for incorporation of these two

types of legal entities in the spectrum of recognized corporate vehicles. However, the statute will enter into force only once Croatia fully joins the European Union.

2.2. Liability

2.2.1. PARTNERSHIPS

In a general commercial partnership, partners are jointly and severally liable to creditors of the partnership. In a limited partnership, at least one partner is personally liable for the obligations of the partnership (the general partner) and at least one partner is not liable for the debts of the partnership if he/she has paid in a contribution (the limited partner). The limited partner may be held liable for the partnership's debts incurred before registration.

2.2.2. CORPORATIONS

In neither the limited liability company nor the joint stock company are shareholders liable for the company's debts. There are exceptions to this general rule:

- a shareholder may be held liable for the company's debts in cases of abuse;
- company's promoters are liable for debts incurred before the company's registration; and
- statutory rules may lead to a shareholder's liability for the company's debts (in the context of groups of companies).

2.3. Formation

2.3.1. PARTNERSHIPS

General commercial partnerships and limited partnerships are established on the basis of a partnership agreement. A partnership is not established until it is registered in the register of relevant local commercial court. Registration is made upon filing the application containing particulars required by law together with the partnership agreement.

There are no minimum capital requirements for the formation of a general commercial partnership. If not otherwise provided by the partnership agreement, partners are obliged to make equal contributions. Contributions may be made in cash, kind, labor or services. Registration is not conditional upon partners having made their contributions. Failure to make a contribution can lead to a liability for partnership debts.

The same applies to the general partners of limited partnerships. Limited partners are not obliged to pay in their contribution before the company is registered. The limited partner is not liable for the partnership's obligation if he/she fully paid the contribution undertaken in the partnership agreement. However, failure to pay the contribution in full gives rise to the limited partner's joint and several liability along with the general partners for the debts of the partnership, but only up to the outstanding amount of the contribution.

2.3.2. CORPORATIONS

A limited liability company is established on the basis of notarized Articles of Association. The company may be established by one shareholder on the basis of a notarized Deed of Incorporation. The company is established by registration in the court register upon application to the competent local court.

The minimum share capital of a limited liability company is HRK 20,000 (approximately EUR 2,700). Contributions to the share capital may be made in cash or in kind. Prior to registration, each founder must pay in (i) 100% of its contribution in kind; and/or (ii) at least

25% of his/her cash contribution, provided that the total amount of all cash contributions paid in before registration is no less than HRK 10,000 (approximately EUR 1,350).

In addition, recently enacted (October 2012) Amendments to CCA provide for a possibility of establishing a "simple limited liability company" with a minimum share capital of HRK 10 (approximately EUR 1.30) and not more than three shareholders. Contributions to the share capital of such company may be made only in cash and have to be paid in full prior to registration. The procedure for establishment of a simple limited liability company is based on specific prescribed forms.

A joint stock company is established on the basis of notarized Articles of Association which the promoters adopt. The company may be established by one shareholder on the basis of a Deed of Incorporation. A joint stock company may be established by way of simultaneous incorporation or successive incorporation. In the former, promoters undertake all shares, adopt and execute the Articles of Association and declare the establishment of the company. In the latter, promoters adopt the Articles of Association, undertake a part of the shares and issue a public prospectus for the subscription of shares. In both simultaneous and successive incorporation the company is established by registration with the court upon application by the members of the management board and the supervisory board.

The minimum share capital of the joint stock company is HRK 200,000 (approximately EUR 27,000). Rules for contributions are similar to those applicable to limited liability companies. But unlike the formation of a limited liability company, promoters must submit to the court a report on company's incorporation. In addition, the members of the management board and of the supervisory board, or executive directors and members of the Board of Directors, must audit company's formation. In certain cases, the formation of the company must also be audited by independent auditors appointed by the court.

2.4. Corporate Governance

2.4.1. PARTNERSHIPS

Partnerships do not have bodies entrusted with management or representative authorities. Each partner of a general commercial partnership is authorized and obliged to manage the partnership unless otherwise provided by the partnership agreement. The authority to manage the partnership extends to all actions normally taken in the course of conducting business. An action cannot be taken if a partner authorized to manage the partnership objects to the action. Actions outside normal business can only be taken with the consent of all partners.

The same rules apply to general partners in a limited partnership. Limited partners are excluded from management. They can only object to decisions made and actions taken by general partners outside the normal course of business.

Each partner of a general commercial partnership is authorized to represent the partnership, except where the partnership agreement states otherwise. Such restrictions have no effect on third parties. The same applies to general partners of limited partnerships. Limited partners are excluded from representation.

2.4.2. CORPORATIONS

The mandatory governing bodies of a limited liability company are the shareholders' meeting and the management board. The Articles of Association can include a supervisory board. However, a supervisory board is a mandatory body in a limited liability company, *inter alia,* (i) if the average number of employees in one year exceeds 200, (ii) if specific statutes provide that a company carrying out certain activities must have a supervisory board, or (iii) if the

share capital of the company is larger than HRK 600,000 (approximately EUR 80,000) and the company has more than 50 shareholders.

Joint stock companies can opt for two tier corporate governance structure (comprising of management board and supervisory board) or one tier corporate governance structure (comprising of only board of directors which appoints one or more executive directors).

2.4.2.1. Management Board

The management board of a limited liability or joint stock company consists of one or more directors (with the exception of simple limited liability company which may only have one director). In a limited liability company management board members are appointed by the shareholders' meeting, unless Articles of Association provide otherwise. They can be changed at any time. Management decisions are taken jointly by directors, unless otherwise stated by the Articles of Association.

Only directors are authorized to represent the company. Articles of Association may restrict the representative powers of directors, but such restrictions are only internal and are ineffective towards third parties.

In a joint stock company, management board members and the chairman of the board are appointed by a supervisory board for a term of office not exceeding five years. Appointments may be renewed. Management board members can only be changed by the supervisory board for material cause, including:

- a gross breach of duty;
- the inability to conduct company business; or
- a vote of no-confidence at the shareholders' meeting, unless such vote was made for manifestly arbitrary reasons.

Management board members can only take management decisions jointly, unless Articles of Association state otherwise. A decision based on a minority vote is not valid. Any restrictions to the representative powers provided in the Articles of Association are of internal nature and are ineffective towards third parties.

Only the management board is authorized to represent the company. The management board represents the company jointly, unless the Articles of Association state otherwise.

There are no restrictions on the nationality of the directors of a limited liability or a joint stock company.

2.4.2.2. Supervisory Board (two tier system)

In a joint stock company, members of the supervisory board are elected by the shareholders' meeting. However, Articles of Association may provide that certain shareholders have the right to appoint members of the supervisory board directly. This right can only be granted to specific shareholders or holders of specific shares if they are shares whose transfer requires the company’s consent. Only one third of the supervisory board may be appointed in this manner. Supervisory board members are elected or appointed for a term of office not exceeding four years and all may be elected or appointed repeatedly.

The shareholders' meeting may remove an elected member of the supervisory board before expiration of his/her term of office. This resolution requires a majority vote of not less than 75% of the votes cast unless Articles of Association provide for a larger majority or for additional requirements. If a shareholder made the appointment directly, he/she can revoke the appointed member of the supervisory board.

The supervisory board supervises management of the company. It may inspect the business books and records of the company, treasury, securities and other matters. The board submits a written supervisory report to the shareholders' meeting. In addition, the board can call a shareholders' meeting, and must do so whenever it is in the interest of the company.

The rules governing supervisory board of a joint stock company apply analogously to the supervisory board of a limited liability company.

2.4.2.3. Board of Directors (one tier system)

The choice of one tier system of corporate governance should be expressly stated in the company's Articles of Association. Articles of Association should also determine the number of members of the board of directors.

Members of the board of directors are elected by shareholders' meeting and duration of their mandate is determined by Articles of Association (it cannot exceed 6 years). Articles of Association may provide that certain shareholders have the right to appoint members of the board of directors directly. Appointment, revocation, resignation and liabilities of the members of the board of directors as well as internal structure of the board of directors (e.g. the existence of the particular committees) comply with rules on the supervisory board in the two tier system.

The board of directors is competent for (i) steering the company; (ii) laying foundations for performance of the company's activities; (iii) supervising management of the company and (iv) representing company towards executive directors. The board of directors is obliged (i) to convene shareholders' meeting whenever necessary for the benefit of the company and (ii) to file for bankruptcy in cases of insolvency and over-indebtedness. It is also responsible to ensure due keeping of the company's business books. The board of directors also has an important role in adoption of company's financial statements.

The board of directors appoints one or more executive directors of the company for a term defined in Articles of Association which cannot exceed 6 years. If there are several executive directors one shall be appointed as the chief executive director. Executive directors can be elected among members of the board of directors. However, members of the board of directors which are not appointed as the executive directors shall always remain in majority within the board of directors. Executive director can be revoked by decision of the board of directors at any time. The revocation does not affect contract entered into by and between the company and the executive director.

Executive directors manage and represent the company. Default rule is that the executive directors manage and represent the company collectively, but a different solution can be prescribed in the Articles of Association. The statutory competences of the board of directors cannot be delegated to the executive directors. Provisions regulating status and duties of the executive directors (e.g. their responsibilities and liabilities) generally refer to the rules governing management board in the two tier system.

2.4.2.4. Shareholders' Meeting

In a limited liability company shareholders adopt resolutions at the shareholders' meeting. This is unless all shareholders agree to vote in writing or resolve in writing on a resolution.

The shareholders' meeting decides in particular on:

- the financial reports of the company, the use of realized profits and the covering of losses,
- the ratification of the acts of the members of the management board and supervisory board, if such exist;

- the calls for payments of original contributions and return of additional payments to shareholders;
- the appointment and revocation of members of the management board;
- the election and removal of members of the supervisory board if such exists;
- the division and redemption of shares;
- any measures to check and supervise business affairs; and
- any amendments to the Articles of Association.

The responsibilities of the shareholders' meeting may be extended or reduced as set out in the Articles of Association. Nevertheless, certain responsibilities, such as adoption of resolutions relating to the company's financial reports, the use of profits and covering of losses, as well as resolutions on election and removal of members of the supervisory board, must remain the responsibility of the shareholders' meeting.

In a joint stock company the shareholders exercise their rights at the shareholders' meeting in particular on the following issues:

- the election and revocation of members of the supervisory board, or board of directors, unless they are appointed by particular shareholders directly;
- the allocation of profits;
- the ratification of the acts of the members of the management board and supervisory board or board of directors;
- the appointment of the company's auditor;
- the adoption of amendments to the Articles of Association;
- the decision on the increase or reduction of the company's share capital;
- the appointment of auditors for examination of matters in connection with formation of the company or with the business conduct of the company and determining the auditors' remuneration;
- the decision on listing/delisting of company’s shares; and
- the decision on the dissolution of the company.

2.5. Affiliated Companies

CCA contains extensive rules on affiliated enterprises. The aim of these provisions is the protection of creditors, minority shareholders and the interests of the company.

2.6. Branch and Representative Offices

The branch office is the minimal form of presence that allows parent entity to conduct permanent business in Croatia. Branch offices may conduct activities that form part of the registered activities of the parent entity. A branch office is established by entry in the court register of the competent local court. The parent entity must adopt and notarize resolution on establishment of the branch office. Details of this resolution are listed in CCA. A branch office is not a legal entity. Its operations, rights and obligations are acquired by and for the parent entity.

Foreign businesses can establish representative offices in Croatia for purposes of market research, marketing, information and representation activities. A representative office cannot conduct business in Croatia. The establishment of a representative office must be registered

with the Ministry of Economy. As of date of accession to the EU, companies domiciled in one of the EU member countries will not have to establish representative offices in Croatia in order to perform above mentioned limited activities.

3. TAXATION

3.1. General

In Croatia, taxes are mainly levied on income, sale and specific transactions. Any business income subjects the business, regardless of its legal form, to the obligation of corporate profit tax. An income earned by individuals is subject to personal income tax. Generally, domestic sales and import are subject to Value Added Tax (VAT), other taxes, excise duties and fees.

In most cases, taxes are self-assessed. The tax return should be filed and payment should be made by the taxpayer within term set by the law. The processing of tax returns, entering tax liabilities in tax records, collecting and refunding taxes are the responsibilities of Tax Administration. The administration of taxes in Croatia is vested in the Ministry of Finance. The institutional structure comprises the central Tax Administration in Zagreb and 20 regional offices with approximately 115 branches in the capitals of Croatian counties.

3.2. Corporate Profit Tax

Corporate profit taxpayers are (a) Croatian resident companies and other legal entities engaged in economic activity for the purpose of earning profit; (b) domestic permanent establishments of non-resident entrepreneurs; and (c) individuals who meet certain statutory criteria. Open-end investment funds are not corporate profit taxpayers, while closed-ended funds are.

According to the law, taxpayer has the obligation to make monthly advance payments based on the previous year's corporate profit tax return. The monthly payments may be adjusted by the Tax Authority. Upon its request, a company may be permitted to set its business/financial year differently than the calendar year.

The tax base is the profit generated in a fiscal year, calculated in accordance with accounting regulations and then adjusted pursuant to the profit tax legislation. The tax return must be submitted to the Tax Administration within four months of the end of the tax period, usually by 30 April. The shortfalls at the end of the year must be self-assessed and paid. On the other hand, in case of surplus, the Tax Authority returns the payments on request or carries the surplus into the next taxable period.

The tax base of resident taxpayers is the profit earned worldwide, while the tax base of permanent establishments of non-resident entrepreneurs is the profit earned in Croatia. Profit earned in the sale, liquidation, change of legal form and the split off /de-merger of a taxpayer is also included in the profit tax base.

The corporate profit tax rate is 20%. Tax losses may be carried forward for a maximum of 5 years. There are no carry back provisions. The Croatian law provides for rules on transfer pricing, thin capitalization and interest deductibility. There are no provisions on group taxation.

A withholding tax is levied on certain payments by Croatian residents to non-resident legal entities, including payments of qualifying interest, dividends, capital gains, payments in respect of the use of intellectual property rights, services of market research, tax and business advisory audit and similar. A withholding tax is levied at the rate of 15%, except with respect to dividends and capital gains where the withholding tax is levied at the rate of 12%. Exceptionally, the rate is set at 20% for all services paid to persons having their permanent establishment or headquarters in the countries, other than the EU member states, in which a general or average nominal profit taxation rate is lower that 12.5% and which are included in the list issued by the finance minister. Where a double tax treaty is applicable, such withholding tax may be decreased (see below chapter 15.2 Double Tax Treaties Chart).

3.3. Personal Income Tax

Personal income tax is levied on the worldwide income of Croatian resident taxpayers and the Croatian source income of non-resident taxpayers. Tax rates on income from employment are as follows:

Monthly income (HRK)	Tax rate (%)
0 – 2,200.00 (approximately EUR 289)	12
2,200.01 – 8,800.00 (approximately EUR 1,160)	25
8,800.01 –	40

The taxpayer is entitled to a basic personal allowance of HRK 2,200 per month (approximately EUR 289). The allowance may be increased for dependants, spouse, children and disabled family members.

The rates of tax levied on property income and income from proprietary rights are 12% and 25% respectively. Income from interest and income from grant of stock or stock options is taxed at 40% and 25% respectively, while the income from dividends and capital gains is taxed at 12%. Personal income tax is not payable on interest paid by banks and other savings institutions on saving deposits and accounts.

An individual resident taxpayer is obliged to file an annual tax return by the end of February of the year following the year concerned. Generally, an individual receiving an employment income only, does not need to file the tax return.

A resident taxpayer may request an annual allowance and entitlement to a tax refund on the basis of his/her annual tax return.

3.4. VAT and Excise Duties

VAT taxpayers are individuals and legal entities providing goods and services on a regular basis. VAT is payable on the supply of goods and services within Croatia (including own consumption) and on the import of goods and services into Croatia.

A number of exemptions to VAT exist, including: exports of goods and services, supplies of goods to free trade zones, supplies of goods and services to diplomatic missions and goods and services in transit. Certain types of services are VAT exempt, among them the services of banks, savings institutions, insurance companies, games of chance, etc.

VAT is generally levied at 25%. A 10% VAT rate among others applies to services of accommodation and related agency services, catering as well as to daily and periodical newspapers and magazines. A 5% VAT rate applies to certain categories of goods and services (e.g. bread, milk, educational literature and certain medical supplies).

VAT returns must be filed by the last day of the month following the end of the taxpayer's VAT accounting period. VAT accounting periods are normally monthly, but can be quarterly for some taxpayers.

Excise duties are levied on certain products including tobacco, oil products, alcoholic beverages, soft drinks, beer, coffee, cars, ships, boats and aircrafts.

3.5. Tax Audit and Penalties

Delayed payments of individual income tax or company profit tax are subject to an annual default interest rate (determined on semi-annual basis by increasing the discount rate of the Croatian National Bank applicable on the last day of a six-month period prior to the current six-month period by 5% points, for individuals, or 8% points for legal entities).

Other defaults, such as violations of the corporate profit tax law, may be fined up to HRK 200.000 (approximately EUR 26.300). Recent amendments (July 2012) introduced broad personal liability of the company's directors and shareholders for the company's tax and similar debts (e.g. customs duties). If the competent tax authority establishes that company's directors or shareholders abused their rights to the detriment of the company, it may instate appropriate collection proceedings directly against these individuals.

3.6. Investment Incentives

The Investment Incentives Act which came into force on 1 January 2007 was subsequently replaced with the Act on Investment Incentives and Advancement of Investment Environment which came into force on 10 October 2012. Both statutes have been enacted with a view of boosting greenfield and brownfield investments in Croatia and further harmonizing the legislation with the *acquis*.

The most significant incentives relate to tax relieves and customs benefits. There are several different corporate profit tax relieves which may be granted to eligible beneficiaries depending on the value of investment and the number of newly employed workers. Apart from tax relieves and customs benefits, the law provides for certain additional incentives which mainly relate to recovery of costs accrued for any of the following: (i) new hires; (ii) investment related training of workers; (iii) incentives for capital expenditures related to investment projects; and (iv) work-intensive investment projects.

In addition, Croatian legislation currently provides for several geographically defined investment areas which are subject to various incentives, such as free trade zones, areas of special state concern, mountain areas, etc.

3.7. Accounting and Audit

3.7.1. ACCOUNTING

The Accounting Act has been introduced as a part of EU accession process and in force as of 1 January 2008. Most notably, this statute strives to implement provisions of the Fourth Council Directive of 25 July 1978 based on Article 54(3)(g) of the Treaty on the annual accounts of certain types of companies (78/660/EEC), Seventh Council Directive of 13 June 1983 based on Article 54(3)(g) of the Treaty on consolidated accounts and Regulation (EC) no. 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards.

The accounting methods prescribed in the statute apply to all companies and business entities registered in Croatia. The accounting methods of various institutions, societies, civil associations and non-profit organizations are not subject to this statute, but are regulated by special laws.

The statute classifies entrepreneurs into three categories: small, medium-size and large companies:

A 'small' company is a company that does not meet two of the following three conditions: (i) total assets of HRK 32.5 million (approximately EUR 4.3 million); (ii) gross income of HRK 65 million (approximately EUR 8.5 million); and (iii) average annual number of employees of 50.

A 'medium-size' company is a company that meets two conditions set for small companies, but does not meet two of the following three conditions: (i) total assets of HRK 130 million (approximately EUR 17.1 million); (ii) gross income of HRK 260 million (approximately EUR 34.2 million); and (iii) average annual number of employees of 250.

A 'large' company is a company that meets more than two of the three criteria set for medium-size companies. Moreover, the following types of entities are deemed to be large

companies: banks, savings banks, building society institutions, electronic money institutions, insurance companies, leasing companies, investment and pension funds and their management companies as well as pension insurance companies.

Companies generally have to apply Croatian Financial Reporting Standards which are adopted by local Accounting Standards Board and are largely based on International Financial Reporting Standards (IFRS). All large companies, companies with listed shares or bonds or companies in preparation for such public listings must apply IFRS fully.

Financial statements include: a balance sheet, an income statement, a statement of changes in equity, a cash flow statement and notes to the financial statements. Small companies must prepare and maintain only a balance sheet, an income statement and notes to financial statements. Financial statements of banks, insurance companies, investment funds, pension funds and stockbrokers are subject to further special requirements and regulation. Holding companies within a group of companies must prepare and keep consolidated financial statements.

The default accounting period is a calendar year, but based on special laws, or for their own purposes subject to special approval, companies may use alternative accounting periods.

Financial statements must be in the Croatian language and expressed in domestic currency, kunas (HRK). They must be kept up-to-date and must be archived in original on permanent basis.

All companies must deliver their properly adopted financial statements to the Financial Agency within 6 months from the last day of the accounting period. Financial statements are kept in the publicly accessible Registry of Financial Statements.

3.7.2. AUDIT

The Auditing Act is in force as of 20 December 2005. The Act introduced changes to the previous regime with a view of fully complying with IFRS, including the International Standards on Auditing (IAASB - ISA), as well as to increase independence of audit function and enforce the regulation of audit. The Auditing Act was amended in 2008 and 2012 to further harmonize the legislation with the *acquis*. The 2008 amendment introduced Audit Public Oversight Committee, an independent and autonomous body responsible for public oversight of the Croatian Chamber of Auditors, audit firms, independent auditors and certified auditors.

Consolidated financial reports and financial reports of joint stock companies, limited partnerships and limited liability companies with an annual revenue in previous year exceeding HRK 30 million (approximately EUR 4 million) are subject to mandatory yearly audit. Mandatory audit requirements also apply to banks, investment funds, retirement funds, insurance companies and other companies of special character set by law. In addition, mandatory audit is required for other companies regardless of their size, provided that their parent company is subject to audit obligation.

Limited liability companies and limited partnerships that do not meet HRK 30 million (approximately EUR 4 million) thresholds may in their internal documents opt for an obligation of audit.

Presently, Ministry of Finance recognizes the Chamber of Auditors as the only professional association of auditors in Croatia. An audit can be conducted by certified auditors within registered auditing firms as well as individual auditors provided they are licensed by the Chamber of Auditors. On the basis of reciprocity and in compliance with CCA, foreign audit companies may establish their branch offices in Croatia. The Chamber of Auditors is responsible for supervising audit standards and practices. The supervision of the Chamber of Auditors and of the auditors is vested in the Audit Public Oversight Committee.

The State Audit Office conducts an audit of government accounts and operations and promotes sound financial management and accountability in the government, in compliance with the audit standards of the International Organization of Supreme Audit Institutions (INTOSAI). The Croatian Parliament hears a Report of the State Audit Office annually.

4. EMPLOYMENT

4.1. Legislative Structure

The principal piece of legislation governing labour relations in Croatia is the Labour Code. In addition to this core legislation, labour relations are regulated by: (i) additional Croatian statutes such as legislation on work safety, (ii) Collective labour agreements and (iii) Work by-laws adopted by the employer. The Labour Code provides all workers with minimum guarantees that cannot be superseded by any other agreement between the employer and the worker.

4.2. Employment Contract

The employer is bound to establish an employment relationship through an employment contract or through a confirmation of employment status. Both documents must be produced in writing. Preference should be given to the employment contract. Both the contract and the confirmation must contain particular information as mandated by the Labour Code. Failure to comply with this requirement is sanctioned by fines for the employer.

A short form employment contract is possible provided that the short form contract contains references to relevant provisions of applicable statute, regulation, Collective labour agreement or Work by-laws as allowed by the law. The freedom to contract is limited. Any provision that is contrary to mandatory law shall be invalid. In case of discrepancy between different documents governing employment, the document containing rules most favourable for the worker shall prevail.

As a general rule, employment contracts are made for an indefinite period of time. A fixed term employment contract may also be concluded, but as a default rule such a contract cannot be made for a term exceeding three years, and it may be made for justified reasons only. Breach of statutory provisions on fixed term employment will result in: (i) the employer's liability for fines and (ii) the employment contract being considered employment contract for an indefinite term.

4.3. Probationary Period

An employer has the right to establish a probationary period for a maximum of six months. The imposition of probationary period must be specifically stated in the employment contract. If, in course of probationary period, the employer determines that the worker does not meet criteria established for job position for which the worker was hired, the employer may dismiss the worker without payment of severance and with only seven days' written notice.

4.4. Temporary Employment Agencies

As possible alternative to regular employment structure, worker may be hired through a temporary employment agency. In such case, temporary employment agency is considered to be the worker's employer, and the worker is assigned to work at the assignee on the basis of a secondment agreement between temporary employment agency and the assignee for which the work is performed. An individual may be seconded by the temporary employment agency to the assignee for up to maximum one year in continuum, and cannot be reengaged for at least one month by the same assignee.

4.5. Working Time

As a default rule, regular working time is set at maximum 40 hours a week. In addition, a worker cannot work more than 6 days a week. Maximum regular working time is inclusive of

a mandatory 30-minute daily break. This effectively means that, as a rule, an individual cannot work more than 37.5 hours in a five-day week or 37 hours in a six-day week. Any work in excess of the maximum regular working hours is considered to be overtime work.

Overtime work is subject to a special regime. The labour inspector must be notified of overtime work in particular cases defined by the Labour Code. The labour inspector is authorized to ban overtime work in case it is established that the overtime work adversely affects the workers. Overtime work must be paid, usually at the rate of 150% of the regular hourly rate.

4.6. Holidays, Days Off and Vacation

There are 14 national holidays and non-working days in Croatia, namely: (i) January 1st, (ii) Epiphany (January 6th), (iii) Easter Sunday, (iv) Easter Monday, (v) Labour Day (May 1st), (vi) Corpus Christi (9th Thursday after Easter Sunday), (vii) Anti-Fascist Struggle Day (June 22nd), (viii) Statehood Day (June 25th), (ix) Homeland Thanksgiving Day (August 5th), (x) Assumption of Virgin Mary (August 15th), (xi) Independence Day (October 8th), (xii) All Saints Day (November 1st), (xiii) Christmas day (December 25th), and (xiv) Boxing Day/St. Stephen's Day (December 26th).

The length of days-off (time-off between the work weeks) shall not be less than 24 hours (usually Sunday). Workers working on a Sunday or public holiday are entitled to additional pay as defined by the employment contract, Collective labour agreement and/or Work by-laws.

Workers in Croatia are entitled to the annual leave of at least 4 weeks in a calendar year. A worker is entitled to use his/her annual leave (in full) once he/she has worked for an employer for at least 6 months. The employer must prepare a schedule of annual leaves no later than 30 June of the relevant calendar year and consult with the Works Council, if any on such a schedule. The Labor Code further requires that the employer notifies workers on the schedule of their annual leaves at least 15 days before the annual leave is to start.

4.7. Salaries

Salaries must be paid to the workers at least once a month. As a default rule, employers must pay the salary and other employment-related payments not later than by the 15th day in a month for the preceding month. The salaries may not be lower than the minimum monthly salary established by applicable Croatian laws.

4.8. Termination of Employment

Generally, an employment relationship may be terminated by: (i) mutual agreement of the parties; (ii) the employer or (iii) the worker. The employer may terminate employment contract only on specific grounds provided in the Labour Code (including staff redundancy for business reasons, worker's repeated failure to fulfil his/her duties or worker's gross breach of duties). An at-will termination of an employment contract by the employer is not allowed.

When terminating an employment for any reason, the employers must strictly comply with specific procedures and requirements provided in the Labour Code (such as for example prior consultation with Works Council or other appropriate body). Save where employment is terminated due to gross breach of worker's duties, when terminating the employment the employer is required to observe applicable notice periods and worker's right to severance. The Labour Code provides for minimum notice periods and minimum severance that will prevail in each case where the employment contract diminishes worker's rights.

The Labour Code gives additional protection to a number of specific categories of workers, including members of Works Council or candidates for that position, workers with diminished

working capacity and workers of a certain age. Dismissal of such workers is conditional upon prior consent of the Works Council.

4.9. Expatriates Working in Croatia

The Act on Aliens came into force on 1 January 2012. Any non-Croatian national ("expatriate") must obtain proper immigration permits in order to reside and work in Croatia. Generally, the immigration procedure in Croatia includes three principle steps as follows: (i) obtaining a visa; (ii) registering local residential address; and (iii) obtaining proper permit. Certain actions and even phases in these procedures may run simultaneously.

As a general rule, any expatriate who wishes to enter Croatia requires a visa to do so. No visas are required for, among others, nationals of the EU member states. Visas are normally issued by diplomatic missions or consular offices of the Republic of Croatia. They can also be issued by diplomatic missions or consular offices of the country that has agency contract for issuance of visas with the Republic of Croatia. As a rule, an expatriate is required to personally file an application for a visa together with enclosures, minimum 3 months prior to intended trip to Croatia. A visa is in fact a stamp in a passport and cannot be used as a work permit.

An expatriate's stay in Croatia may be (i) short-term; (ii) temporary or (iii) permanent. An expatriate who has obtained a proper visa or who does not require a visa to enter Croatia may stay (but not work) for short-term in Croatia for a maximum period of 3 months within the given 6-month period. Temporary stay may be approved for various purposes, including for purposes of work in Croatia. An expatriate who was granted permanent stay in Croatia is allowed to work absent having a work permit, but employers must notify local police office of hiring such expatriate within 8 days from the date of hire.

Within 2 or 3 days after the entry in Croatia (depending on the type of expatriate's residence permit) or after the change of address, expatriate must register his/her (new) local residential address with local police office at his/her place of residence. If the expatriate is staying in a hotel, as a rule, the hotel will take care of this registration requirement. Alternatively, if the expatriate leases premises in Croatia, then he/she should personally attend to the registration of residence, accompanied by his/her landlord. Registration of residential address is made on the spot provided that all required documents are presented to the police. Expatriate having permanent residence in Croatia must register change of residential address within 8 days from the change.

Depending on the expatriate's job position, intended duration of stay, and basis of his/her work in Croatia (such as intra-group transfers, employment with local company, or secondment to a local company by a non-Croatian employer), the local company and/or expatriate should apply for expatriate's work or business permit and residence permit respectively. As a general rule, the applications for the relevant permit along with different enclosures should be filed with the local police office. Expatriate is not allowed to commence work prior to obtaining relevant work or business permit.

Presently, expatriate must be personally present when filing application for a business or residence permit because officials usually like to conduct a brief interview with the expatriate for permit issuance purpose. In the practice, permits are usually issued within 45 days from the date the complete application is filed. It should be noted that permits have a limited period of validity (usually one year) and must be renewed within specific deadlines if expatriate's stay/work in Croatia is to be prolonged.

5. REAL ESTATE

5.1. General overview

Unique geographical characteristics of Croatia and improved infrastructure connecting the coastal area with the inland as well as forthcoming EU accession make Croatia an interesting area for foreign investors. However, recession trends and overall murky economic outlook resulted in the decrease of real estate prices and decline in number of real estate development projects.

On the other hand, prospective buyers are looking to benefit from such turn of events. At this point, real estate projects available for acquisition and real estate projects that have been stopped due to financing issues by far exceed demand for such projects. Decisively buyer's market benefits the companies looking to expend their business to Croatia as well as the professional real estate investors. This being said, the low supply of large plots of land (due to their limited number and occurrence of problems related to ownership, such as unresolved title) as well as diminished availability of demanded locations by zoning and planning restrictions (frequently in the coastal area) still largely affect the Croatian real estate market.

In Zagreb, demand for business premises has been continuously decreasing, but the prime projects and locations still attract significant interest. The retail space demand has been presently satisfied by opening of several shopping centres in the city as well as on its outskirts. The coastal area is constructed in only about 15% of its length and offers much potential.

The current tendency of companies to restructure their operations and move production outside urban areas may offer further opportunities for investors. The companies achieve a premium by selling existing urban sites and transferring to cheaper production locations. Additional opportunities may be provided in the near future by the Croatian Government which is considering how to effectively restructure and put into use its real estate portfolio in order to boost the investment and employment cycle.

5.2. Regulatory

5.2.1. ACQUISITION OF REAL ESTATE BY FOREIGN NATIONALS

Non-Croatian nationals may acquire real estate in Croatia provided that two conjunctive requirements are met: (i) that reciprocity exists between Croatia and the foreigner's country of citizenship; and (ii) that prior approval of the Croatian Ministry of Justice for the acquisition is obtained. These requirements do not apply in regard to nationals of EU member states. Also, by way of derogation, a non-Croatian national may acquire real property in Croatia by inheritance (absent prior Ministry's approval) provided that the reciprocity requirement is met.

In addition, above restrictions do not apply to corporate vehicles established in Croatia, even if they are wholly owned by foreign persons. In any case, corporate investors will most likely establish a special purpose vehicle in Croatia to make their investments. The most common type of vehicle is the limited liability company (d.o.o.).

5.2.2. REGISTRATION OF TITLE AND CHARGES

Real estate and rights related to real estate are registered with the Land Registry and the Cadastral Registry.

Under the law, title of ownership over real estate is acquired by entry of the acquirer into the Land Registry. Land Registry is a public record maintained by a Municipal Court competent for the territory where the real estate is located. The entry of acquirer into the Land Registry is made on the basis of appropriate documents, such as a real estate purchase agreement.

The title of ownership as well as encumbrances and interests over real estate (such as ownership claims or leases) are entered into the Land Registry.

Data related to surface area, form, use and occupant of a real estate are entered into the Cadastral Registry. Ownership and other rights *in rem* over a plot are not entered into the Cadastral Registry. Therefore, only the Land Registries are competent instances to check the title of ownership and charges over a real estate.

The law provides for legal presumption that the status of the Land Registry is true and accurate, unless there is proof to the contrary. This means that, as a general rule, a person acting in good faith may rely on the accuracy of the Land Registry and no one may claim that the data entered into the Land Registry are not known to them. However, the rule of reliance on the accuracy and completeness of the Land Registry is subject to certain exceptions. This clearly demonstrates the importance of exercising proper due diligence before acquiring a real estate in Croatia.

5.2.3. CONSTRUCTION PERMITS

The Act on Physical Planning and Construction ("Construction Act") entered into force on 1 October 2007 and was amended in 2009, 2011 and 2012 in order to further harmonize legislation in the area of construction and especially with respect to requirements of energetic efficiency of the buildings and construction materials with the *acquis*. Amendments were also aimed at simplifying construction related administrative procedures and documents.

Generally, applicable regime regarding necessary permits mandates three-step procedure including: (i) location permit as a preliminary document defining the type and the extent of development or reconstruction on a designated plot; (ii) building permit confirming that the main project has been elaborated in accordance with the location permit and that all requirements set forth by the construction laws have been complied with, and (iii) usage permit certifying that the final construction structure complies with technical drawings submitted for the building permit.

The implementation of the Construction Act was aimed to result in reducing the number of permits and associated administrative procedures for the majority of constructions. By way of example, the construction of residential buildings of up to 400 sqm necessitates obtaining of only one administrative permit - decision on construction requirements, while the use of such buildings is possible only upon delivery of the supervising engineer's report to the competent administrative office. Also, the building permit, a document that has involved most of the problems and attracted most of criticism in the old regime, is now necessary only for the buildings of interest to the state and buildings built on territory of two or more counties. More information on construction requirements is available at www.mgipu.hr/default.aspx?id=9367.

5.2.4. RESTRICTIONS OF ACQUISITION

In Croatia, foreign nationals may not acquire ownership of real property in excluded areas (e.g. military), on agricultural land, in protected natural areas, forests or on forest land.

Restrictions of acquisition to coastal land ("*pomorsko dobro*") apply regardless of the investor's nationality, but the investors may be entitled to use such protected state-owned land based on concessions.

The administrative practice showed deterrent to all potential purchasers of real estate located in vicinity of coastal land (islands, first line of buildings). Acquisition of real property owned by a local government unit (municipality or a city) is conditional upon duly conducted public tender proceedings.

5.3. Taxes

Any acquisition of land is subject to the Real Estate Transfer Tax (“RETT“). RETT shall apply to acquisition of buildings constructed before 1 January 1998. For acquisitions of buildings constructed after that date, the so called "double tax regime" applies. Under this “double tax regime” the land element of a building (in practice about 20-30% of the aggregate price) is taxed by RETT and the building erected on land (the remaining 70-80% of the aggregate price) is taxed by the Value Added Tax (“VAT“).

RETT is levied at the rate of 5% on the tax base calculated as the market value of the real estate at the time of acquisition. The market value is determined by the contract or the local tax authorities, depending on which amount is higher. RETT is paid by the acquirer, is due after the execution of the contract and is not recoverable.

VAT is assessed at 25% of the tax base calculated as the amount invoiced for the real estate reduced for the value of the land element (in practice about 20-30% of the aggregate price). An acquirer that is VAT registered may recover VAT.

6. EXCHANGE CONTROL

The foreign exchange system in Croatia is regulated by the Foreign Exchange Act and a number of decisions rendered by the Croatian National Bank (*Hrvatska narodna banka;* HNB). Transactions between residents and non-residents in both domestic and foreign currency, transactions between residents in foreign currency and simple transfers of assets to and from Croatia which are not considered transactions, are subject to exchange control regulations.

In general, payments and transfers based on capital transactions are free, provided that the transaction has been duly executed and reported to the competent authorities and that all tax-related obligations in Croatia have been duly settled.

Under Foreign Exchange Act, capital transactions include direct investments, investments in real estate, transactions in securities, transactions in holdings in investment funds, loan transactions, deposit transactions, payments based on insurance contracts and transfers of assets.

Direct investment by non-residents is generally not restricted, and transfer of profits arising from such direct investment is free provided that all taxes have been duly settled. Direct investment in foreign countries by Croatian residents is not restricted either.

Loans given to or received from non-residents may need to be duly reported to HNB.

Non-residents may freely open a bank account in Croatia in both domestic and foreign currency. Residents may freely open a bank account outside Croatia.

Current transactions, i.e. transactions between residents and non-residents which do not fall under the definition of capital transactions, are free.

7. BANKING AND FINANCE

7.1. Operation of Banks

7.1.1. SOURCES OF LAW

The Croatian banking system is governed primarily by the Credit Institutions Act and the Act on the Croatian National Bank (HNB), as well as a number of decisions on banking issued by HNB.

Banking services may be provided by (a) a credit institution established in Croatia which has obtained a license from HNB; or (b) a branch office of a foreign credit institution which has obtained a license from HNB. A credit institution having its registered seat in the Republic of Croatia may, under conditions laid down by the law be established as a bank, savings bank, housing savings bank, or an electronic money institution.

Banking legislation and HNB decisions establish the rules on outsourcing of business activities, banking secrecy, accounting and financial reporting, public disclosure, audit, internal control system, supervision of credit institutions, reporting requirements, special administration and special management, liquidation and bankruptcy of credit institutions, supervision on a consolidated basis and decision-making methods and procedures of HNB.

7.1.2. LICENSE AND BANKING SERVICES

To provide banking services a Croatian credit institution must obtain a license from HNB. Banking services are defined as acceptance of deposits or other repayable funds from the public and granting of loans for own account from these funds. In addition to the license for banking services, the credit institution may apply to HNB for grant of a license to provide core and additional financial services. Core and additional financial services include such activities as issuing guarantees and other commitments, factoring, financial leasing, extending loans, including consumer loans, trading for own account or account of a client in financial markets, making payments in Croatia and abroad, etc.

7.1.3. CORPORATE FORM AND CAPITAL REQUIREMENTS

A credit institution may be established only in the form of a joint stock company. The minimum share capital of a bank is HRK 40 million (approximately EUR 5,270,000), the minimum share capital of a savings bank is HRK 8 million (approximately EUR 1,054,000) and of a housing savings bank is HRK 20 million (approximately EUR 2,630,000). The regulatory capital may not at any time fall below the amount of the required minimum share capital. Regulatory capital consists of the core capital (Tier 1) and additional capital (Tier 2) as well as other forms of capital which may be determined by HNB. The methods of calculation of the regulatory capital are detailed in decisions adopted by HNB.

The capital adequacy ratio of credit institutions is set at 12% minimum. If HNB establishes that a bank has conducted risky business operations, it may establish a higher minimum capital adequacy ratio for that bank.

A credit institution may issue only registered shares. Shares must be paid in full prior to the registration of the establishment or of the share capital increase with the court register. Preference shares may not exceed one fourth of total initial share capital.

7.1.4. MANAGEMENT BOARD REQUIREMENTS

According to the Credit Institutions Act, at least one member of the management board of a credit institution must have command of the Croatian language sufficient for performing this function. All directors must direct the business of the credit institution full time and be

employed with the credit institution. In terms of corporate law, the term of appointment of the management board members is maximum five years with no restrictions on re-appointment.

Banking legislation establishes specific qualification requirements for the members of the management and supervisory boards of banks.

7.1.5. ACQUISITION OF BANKS

The acquisition of a qualifying shareholding in a bank, defined as the acquisition of 10%, 20%, 30% or 50% or more, is subject to the approval of HNB.

HNB is responsible for the protection of free competition in the banking services and financial services markets when provided by credit institutions. The protection is provided by *mutatis mutandis* application of the regulations governing the rules and the system of measures for the protection of market competition. HNB is responsible for assessing of permissibility of every concentration arising from acquisition of shares of credit institutions regardless of the level of income of the participants to the concentration. However, as of the date of accession of Croatia to the EU, Croatian Competition Agency will assume enforcement of antitrust and merger control rules in the banking sector.

7.1.6. EXPOSURE LIMITS AND RESTRICTIONS OF INVESTMENTS

Subject to certain limited exceptions, a credit institution's exposure to one person or to a group of affiliated persons may not be higher than 25% of a credit institution's regulatory capital after application of credit risk mitigation techniques. Also, the exposure to a person who is in a special relationship with a credit institution as defined by the Credit Institutions Act (person in special relationship) may not be higher than 10% of a credit institution's regulatory capital after application of credit risk mitigation techniques. Any transaction which may result in large exposure to one person or to a group of affiliated persons, which is defined as 10% or more of a credit institution’s regulatory capital, as well as any transaction which may increase a large exposure to and over 15% or 20% and for every further 5% of the regulatory capital, as the case may be, must be approved by the credit institution's supervisory board. The sum of all large exposures may not exceed 600% of the regulatory capital. The sum of all exposures to persons in special relationship may not exceed 50% of the regulatory capital. Transactions which may result in exposure or an increase of exposure to persons in special relationship, and change of terms under which such transaction was made are subject to the prior approval of credit institution’s supervisory board except when such transaction is made with a natural person under terms regulated by credit institution’s general operating conditions.

Credit institutions are subject to a number of restrictions on investment:

- a credit institution's investment in tangible assets may not exceed 40% of its regulatory capital;
- a credit institution's total investment in the capital of non-financial institutions (every legal person except credit or financial institutions, ancillary services companies and insurance and reinsurance companies) may not exceed 30% of its regulatory capital;
- investments in a single non-financial institution may not exceed 15% of its regulatory capital.

Investment restrictions indicated above are subject to certain exceptions regulated by the Credit Institutions Act.

Prior approval of HNB is required for a credit institution's (i) gradual or immediate direct acquisition of a shareholding of 20% or more in another legal person, if the shareholding exceeds 10% of its regulatory capital; and (ii) direct acquisition of majority shareholding or

the majority of voting rights in another legal person. Such approval is not required if a credit institution intends to keep directly acquired shares in the trading book.

A credit institution may not extend loans or issue guarantees for the acquisition of its own shares or shares in companies in which it has a shareholding of 20% or more, unless such acquisition is to result in termination of any capital affiliation between the bank and such a company.

7.1.7. RISK MANAGEMENT AND SUPERVISION

Banks are subject to the duty to measure, estimate and manage risks in accordance with criteria defined by the Credit Institutions Act and HNB. Received deposits, including deposits received through its branch offices from abroad, must be insured by the credit institution in accordance with special regulations.

Credit Institutions Act provides for rules on the supervision of banks by HNB and establishes various reporting requirements. Methods of bank supervision as well as the types and procedures of imposing supervisory measures and their implementation are specified in HNB's decisions. Special rules on supervision of groups of credit institutions are established in Credit Institutions Act and HNB's Decision on Supervision of Credit Institutions Group on a Consolidated Basis.

7.1.8. ROLE OF THE CROATIAN NATIONAL BANK

HNB is the central banking authority in Croatia. It is the authority responsible for granting the banking license and it has the power to revoke this license in specific circumstances.

The status, organization and activities of HNB are governed by the Act on HNB. The autonomy of HNB is guaranteed by the Constitution. HNB is responsible to the Parliament. Competences of HNB, beyond licensing and supervision of banks, include establishment and implementation of monetary and foreign exchange policies, holding and management of the international reserves of Croatia, issuance of banknotes and coins, maintenance and management of accounts and granting of loans to banks, as well as the regulation and supervision of the payment system, etc. Activities relating to the banking system are governed primarily by the Credit Institutions Act and the related decisions of HNB.

7.2. Operation of Other Financial Institutions[4]

7.2.1. REGULATORY AUTHORITY: HANFA

Croatian Agency for the Supervision of Financial Institutions (*Hrvatska agencija za nadzor financijskih usluga;* HANFA) supervises non-banking financial institutions.[5]

7.2.2. INSURANCE

The insurance business in Croatia is governed by the Insurance Act and by a number of regulations, decisions and by-laws.

[4] The operation of securities market and related institutions is described in more detail in the chapter on securities (see below 0)

[5] HANFA is responsible for the supervision of: exchanges and regulated public markets, authorized dealers and issuers, brokerage companies, brokers, investment advisors and institutional investors, investment funds, privatization investment funds, pension funds and companies managing such funds, the Central Clearing Depository Company, the Central Register of Pension Insurees, insurance companies, insurance agents and brokers, leasing and factoring companies, to the extent that such activities are not performed by credit institutions.

Insurance services may be conducted by a joint stock insurance company or a mutual insurance company. Insurance services may also be conducted by branch offices of foreign insurance companies. HANFA licenses and supervises Croatian insurance companies and branches of foreign insurance companies in Croatia.

Insurance companies may pursue life insurance or non-life insurance operations. Life insurance operations include life insurance and annuity insurance. Non-life insurance operations are divided into 18 groups, which are further subdivided into classes. Reinsurance may be provided only by joint stock insurance companies or public insurance companies.

The insurance business is commonly conducted through a joint stock insurance company. The minimum capital requirements for the establishment of such a company vary depending on the insurance activity concerned and are, for example: for life insurance: HRK 22.5 million (approximately EUR 2,965,000); for non-life insurance: HRK 15 million (approximately EUR 1,976,000) or HRK 22.5 million (approximately EUR 2,965,000), depending on the group of non-life insurance activity; for reinsurance: HRK 22.5 million (approximately EUR 2,965,000). As of the date of accession of Croatia to the EU, the above mentioned minimum capital requirements will be increased from HRK 15 million to HRK 17.5 million (approximately EUR 2,305,000), and from HRK 22.5 mil to HRK 26.25 million (approximately EUR 3,458,000).

HANFA must approve acquisition of the shares of a joint stock insurance company which results in a shareholding exceeding 15% of the voting shares.

Insurance companies must, at all times, have a regulatory capital sufficient to meet all obligations arising from insurance contracts. Regulatory capital consists of the share capital, safety reserves and other reserves, retained profit and a portion of the profit of the current year, with certain adjustments. The law sets out different minimum regulatory capital requirements for various types of insurance operations.

Insurance companies must reinsure excess of risk with companies which provide active reinsurance in Croatia or abroad.

7.2.3. INVESTMENT FUNDS

Investment funds are governed primarily by the 2005 Investment Funds Act. Investment funds may be established as open-ended funds (which do not constitute a legal entity) or as closed-ended funds (established in the form of a joint stock company). Both open-ended and closed-ended funds are established and managed by fund management companies. The great majority of investment funds in Croatia are open-ended. Investment funds and fund management companies are supervised and licensed by HANFA.

Shares or unit certificates in investment funds may be traded through public offering or private placement. Open-ended investment funds may be established as public offering funds, private placement funds, or private placement funds of high risk capital (venture capital funds). Closed-ended funds may be established only as public offering funds.

The law provides for stringent limitations on the types of investment allowed to investment funds as well as for limits on the investment in the securities of a single issuer. The law also sets out requirements with respect to the minimum capital, the activities of fund management companies, shareholding in fund management companies, qualification criteria for members of management and supervisory boards in fund management companies, risk management, reporting requirements, etc.

As of the date of Croatian's accession to EU, the investment fund regulation will go through substantial overhaul as Croatia will accept European AIFM (Alternative Investment Fund Managers) and UCITS (Undertakings for Collective Investment in Transferable Securities) rules.

7.2.4. PENSION FUNDS

The Croatian pension system consists of three levels: compulsory pension insurance based on generational solidarity (Level 1), compulsory pension insurance based on individual capitalized savings (Level 2), and voluntary pension insurance based on individual capitalized savings (Level 3).

Croatian Pension Insurance Fund, a public entity, receives compulsory Level 1 contributions from salaries of all insured persons. Within Level 2, employees pay an obligatory contribution to their account held within a private pension fund of their choice. Such funds are managed by companies established specifically for that purpose (compulsory pension companies). Participation in Level 3 is voluntary. Level 3 funds are managed by voluntary pension companies.

Pension companies may be established as joint stock companies or limited liability companies, in accordance with specific legal requirements.

7.2.5. INVESTMENT SERVICES AND INVESTMENT ACTIVITIES

Subject to certain exceptions, investment services and investment activities may be generally provided by: (i) an investment company established in Croatia which obtained licence from HANFA, (ii) a branch office established in Croatia of foreign investment company which obtained licence from HANFA, (iii) credit institution established in Croatia which obtained licence from HNB, (iv) a branch office established in Croatia of foreign credit institution which obtained licence from HNB.

An investment company may be established and operated in the form of a limited-liability company or a joint-stock company. With certain exceptions, company's management board must consist of at least 2 members and at least one of the members must have knowledge of Croatian language. Depending on the type and scope of investment services and activities in respect of which an investment company applies for licence, minimal initial capital of investment company varies from HRK 200,000 (approximately EUR 26,300) and HRK 6 million (approximately EUR 790,000). Acquisition of shareholding in an investment company surpassing 20%, 30% or 50% is subject to prior approval of HANFA.

Company providing investment services must maintain appropriate organizational requirements and undertake all reasonable steps in order to avoid conflict of interests. The clients are classified as retail or professional clients depending on their knowledge, experience, financial situation and investment objectives. Retail clients have to be provided with a treatment involving a higher level of protection. When client orders are executed, all reasonable steps have to be taken to obtain the best possible result for the clients. In addition, there are statutory rules on maintenance of records, reporting to HANFA and publishing of transactions.

7.2.6. OTHER FINANCIAL SERVICES

The operations of housing savings associations functioning within a government housing incentive scheme is governed by a separate law and, in matters not governed by that law, by credit institutions legislation. Separate legislation also governs privatization investment funds and certain other special types of funds as well as leasing activities.

7.3. Money Laundering

As part of the efforts to combat money laundering and to further harmonize local legislation with the Directive 2005/60/EC, in 2008 Croatia has enacted the Act on Prevention of Money Laundering and Terrorism Financing, which was subsequently amended in 2012.

Central authority for reporting is the Anti-Money Laundering Department (the “Department”) which is attached to the Ministry of Finance. The task of the Department is to (i) gather, analyze, classify and keep data received from all reporting institutions; (ii) forward relevant data to competent state bodies (such as public prosecutor); and (iii) undertake measures for the prevention of money laundering.

Reporting requirements are imposed on various entities, including (i) banks, (ii) savings banks, (iii) investment and pension funds, (iv) Croatian Post Office, (v) investment funds, (vi) organizers of games of chance. Also, there are certain looser reporting requirements imposed on (i) lawyers, law firms and notaries public, (ii) auditing firms and independent auditors and (iii) accountants and tax advisors.

The law provides for detailed rules on information that reporting entities must obtain from their clients with the purpose of establishing the ultimate, beneficial owner of the client.

8. SECURITIES

8.1. Legislative Structure and Regulatory Authority

The primary source of law regulating securities market in Croatia is the 2008 Capital Market Act amended in 2008 and 2009 ("CMA"). CMA implemented various EU legal instruments including, but not limited to the Markets in Financial Instruments Directive (Directive 2004/39/EC of the European Parliament and of the Council), Directive on Investor Compensation Schemes (Directive 97/9/EC of the European Parliament and of the Council) and Market Abuse Directive (European Parliament and Council Directive 2003/6/EC). Other important pieces of legislation include the Investment Funds Act, the Takeover Act, Companies Act, and a number of implementing regulations.

Assurance of proper functioning and supervision of securities market in Croatia is entrusted to HANFA. The most important tasks of HANFA with respect to the securities market are: the supervision of fair trading rules with respect to securities, the supervision over conduct of stock exchanges, authorized dealers, investment funds and other market participants or issuing licenses and mandating measures necessary for proper functioning of the securities market.

The Central Clearing and Depository Company (*Sredisnje klirinsko depozitarno drustvo;* SKDD) is a joint stock company whose shareholders are the Republic of Croatia and other market participants. SKDD is authorized to manage central depository of non-materialized securities as well as to perform clearance and settlement with respect to transactions with securities executed on or outside of a regulated market or a multilateral trading facility.

8.2. Issuance of Securities

Securities in Croatia may be generally placed on the market only by way of public offering which in turn requires preparation of prospectus. The content of the prospectus is defined in detail by relevant regulations. The prospectus must be presented to HANFA for approval. After obtaining the approval of HANFA, the prospectus must be publicized. There are defined statuary exceptions to this rule which relate to e.g. issuance of securities to limited number of investors or solely to professional investors, issuance in the course of initial formation of joint stock companies or share capital increases, share plans for employees, etc.

Generally, foreign issuers may offer their securities to public in Croatia only through an authorized dealer. HANFA may approve a prospectus which lacks certain requirements mandated by Croatian laws if the authorized dealer proves that (i) such requirements cannot be fulfilled in the country where the issuer is seated and where HANFA decides that this will not reduce the possibility of a potential investor to objectively assess the prospects and risks involved in the investment and to make a decision on investment, or (ii) where the issuer is seated in the member state of the EU and such requirements are not necessary in that member state. Furthermore, when the securities are simultaneously issued through public offering in Croatia and in a member state of the EU, HANFA may approve the publication of the prospectus that is approved by the competent authority of that member state.

8.3. Trading in Securities

Trading in securities as a permanent activity may be performed only by authorized dealers. Authorization is granted by HANFA or HNB and may only be given to investment companies and credit institutions (see above 8.2.5.). Among authorized dealers, trading in securities may be performed only by brokers and investment advisors holding a license issued by HANFA.

Organized trading in securities, as well as matching supply and demand of securities may only be performed on regulated market and on multilateral trading facility ("MTF"), based on the authorization of HANFA. The operation of the regulated market in Croatia can be managed only by a stock exchange with its registered office in Croatia. The operation of MTF may be managed by a stock exchange or an investment company subject to certain conditions. A stock exchange may be established only as a joint stock company. A regulated market consists of regular market and official market which imposes more stringent listing requirements.

Where a natural person or a legal entity directly or indirectly reaches, exceeds or falls below the thresholds of 5%, 10%, 15%, 20%, 25%, 30%, 50% and 75% of voting rights in an issuer of shares, it shall notify the issuer and HANFA. Moreover, when the shareholding exceeds 25%, in most cases a mandatory tender offer for the remaining shares must be made.

Clearance and settlement of transactions on securities issued in non-materialized form is performed by SKDD, except if stock exchange or MTF operator chooses clearing and settlement system managed by another operator.

8.4. Prohibited Activities

Croatian laws contain provisions prohibiting insider trading (for insiders as well as other persons who obtain this information without authorization), market manipulation and providing false information. Furthermore, it is prohibited for authorized dealers to execute transactions motivated solely by the purpose of charging commission.

9. COMPETITION LAW

9.1. Relevant Legislation

The primary piece of legislation regulating protection of market competition in Croatia is the 2009 Competition Act. As part of the endeavours to harmonize Croatian laws with the EU legal system, in addition to the Competition Act, Croatian Government has enacted a number of Decrees implementing EU block exemption regulations and certain notices of the European Commission into the Croatian legal system. As of the date of Croatia's accession, EU competition law shall become fully applicable to market conducts that may affect trade between EU member states.

Competition Act regulates all three major fields of the competition law: anticompetitive agreements and practices, dominant positions and merger control. The structure and functioning of the Croatian Competition Agency (the "Agency") as well as certain specific features of competition law enforcement are also regulated by the Competition Act.

Antitrust provisions of the Competition Act are closely modelled after the provisions of Articles 101, 102 and 106 of the Treaty on the Functioning of the European Union, and the Agency pushes the enforcement practice more and more in line with the solutions developed in the EU competition law (e.g. by invoking provisions of the European Commission's guidelines or by using constructions created in the case law of the European Courts). With respect to dominant position, it is interesting to note that the Competition Act provides that the undertaking enjoying a market share in excess of 40% may be in dominant position.

As to merger control, an obligation to notify the business combination exists where the contemplated transaction qualifies as a concentration within the meaning of the Competition Act and where transaction satisfies the statutory turnover thresholds. The following turnover thresholds are prescribed: (i) the combined worldwide annual turnover of all the undertakings concerned is at least HRK 1 billion (approximately EUR 132 million) in the financial year preceding the concentration; and (ii) the aggregate Croatian annual turnover of each of at least two undertakings concerned is at least HRK 100 million (approximately EUR 13.2 million) in the financial year preceding concentration worldwide. For worldwide turnover to be met, at least one undertaking participating in the concentration has to have a seat (i.e. subsidiary) or a branch office in Croatia. In media sector and in banking sector mergers have to be notified regardless of turnover figures. Full function joint ventures that meet the threshold requirement are notifiable.

Notification to the Agency has a suspensive effect on the transaction, but exceptionally, the Agency may allow particular completion activities. After an initial assessment, i.e. within one month following the notification, the Agency can either clear the transaction (tacit approval is possible) or initiate second phase proceedings. The final decision on the concentration has to be rendered within three months after the second phase proceedings have been initiated. Additionally, short form merger control proceedings are possible in the exceptional circumstances (e.g. where no horizontal overlap exists).

9.2. Enforcement

The function of competition watchdog is entrusted to the Agency. The Agency is managed by the Competition Council consisting of five members appointed by the Croatian Parliament for a renewable term of five years. Decisions rendered by the Agency are subject to judicial review before the competent administrative court.

With regard to the procedure of competition law enforcement, the Competition Act contains several provisions regulating the issues of (i) who is entitled to initiate the proceedings, (ii) what documents and information the complaint should contain and (iii) what investigating and

procedural powers the Agency enjoys. The procedural issues not expressly settled by the provisions of the Competition Act are governed by the Code of Administrative Procedure and the Misdemeanours Act.

Agency may impose fines for violations of substantive (and some procedural) provisions of the Competition Act. The fines are calculated on the basis of aggregate annual profits of an undertaking. For serious offences (e.g. abuse of dominant position) they can be up to 10% of the aggregate annual profits achieved in the last year for which the financial reports have been concluded and up to 1% for less serious violations (e.g. failure to notify the Agency of the intended merger). At the same time, fines for undertakings that are not party to the proceedings may range from HRK 10,000 (approximately EUR 1,300) to HRK 100,000 (approximately EUR 13,300). Croatian rules on calculation of fines and leniency programs largely follow relevant EU instruments.

Certain industries are regulated with sector-specific rules and have special institutions monitoring the functioning of the market. By way of example, the Croatian National Bank (HNB) enforces the competition law in the banking sector and does so by *mutatis mutandis* application of the regulations governing the rules and the system of measures for the protection of market competition. However, as of Croatia's accession to the EU, this competence will be vested with the Agency.

9.3. State Aid

At the end of 2005 Croatia has enacted the State Aid Act, which was subsequently amended in 2011. This statute strives to harmonize the state aid area with the rules and procedures accepted within the EU. Subsidies in the field of agriculture and fisheries are expressly excluded from its scope and are regulated by the special laws. The Agency is competent to authorize the state aid schemes and to monitor their execution. It is also authorized to order the return of state aid given in contravention of applicable rules.

10. INTELLECTUAL PROPERTY

10.1. Overview

Intellectual property legislation has recently been amended and brought in compliance with European rules. Intellectual property legislation is contained in several separate legislative acts, including the Copyright and Related Rights Act, the Trademark Act, the Patent Act, the Industrial Design Act, the Act on Geographical Indications and Designations of Origin of Products and Services and the Act on the Protection of Topographies of Semiconductor Products.

Croatia is a member of WIPO and a party to major international treaties relating to intellectual property, such as the Paris Convention for the Protection of Industrial Property.

The Croatian State Intellectual Property Office (*Drzavni zavod za intelektualno vlasnistvo;* DZIV) is vested with the registration and other related proceedings of industrial property rights. However, in case of violation of these rights, commercial courts will have competence.

10.2. Trademarks

Croatian law provides for protection of all marks capable of graphic representation, provided that they are sufficiently distinctive. Protection is obtained through registration of the trademark with DZIV.

Registration proceedings are initiated by filing the application on the prescribed form. The applicant can claim priority rights in accordance with the terms of the Paris Convention. Within three months upon the publication of the trademark in DZIV's Gazette, each interested party can file an opposition to the trademark. If no opposition is filed and other required conditions are met, the trademark is registered with DZIV for the duration of ten years, and may be subsequently renewed.

The registration of the trademark grants its holder the right to prevent others from using the same mark for the same products or services, from using the same or similar mark for the same or similar products or services, if this is likely to result in confusion on the market, as well as from using the same or similar mark for non-similar products or services if the trademark has a distinct reputation in Croatia.

Croatian law specifically allows for registration of the transfer of a trademark, the license of a trademark, the pledge of a trademark and enforcement proceedings over a trademark into the Trademark Register. Also, Croatian laws allow the registration of collective and guarantee marks.

Croatia has acceded to the Madrid Agreement Concerning the International Registration of Marks.

10.3. Patents

Croatian law provides for the protection of all inventions in the field of technology, provided that they are new, that they involve an inventive step and that they are eligible for industrial application. However, the following shall not be considered patentable: discoveries, theories and mathematical methods; aesthetic creations; rules, instructions or methods for performing mental activities, playing games or doing business; presentation of information; computer programs.

Also, the following shall be excluded from patent protection: inventions which concern animal breeds, plant varieties and essentially biological processes for production of plants or animals; human body at the various stages of its formation and development and a simple

discovery of one of its elements; inventions which concern diagnostic or surgical methods or methods of treatment practiced directly on human or animal body, with the exception of products, in particular substances or compositions, used in such methods.

Registration proceedings are initiated by filing the application on the prescribed form. The applicant can claim priority rights in accordance with the terms of the Paris Convention. The registration of a patent grants its holder the right to exclusively exploit the protected invention. However, under certain conditions, compulsive licensing may apply. Croatian law specifically allows for the registration of the transfer of a patent, the license of a patent, and any other relevant changes. A patent may be kept in force for a maximum period of up to 20 years, or up to 10 years for consensual patents.

Croatia has acceded to the Patent Cooperation Treaty. Also, the new Patent Act explicitly provides that European patent application and European patents which are extended to Croatia shall have the same effect as national applications and national patents. However, provisions of the European Patent Convention shall not be directly applicable in Croatia.

11. DISPUTE RESOLUTION

11.1. Courts

Croatian judicial system comprises first instance courts, appellate courts, the administrative courts, High Administrative Court and the Supreme Court of Croatia.

Civil and commercial cases are heard in the first instance by Municipal and Commercial Courts. Municipal Courts are courts of general jurisdiction which, among others, decide civil, family and inheritance law disputes. Commercial cases, such as commercial litigations, intellectual property issues or bankruptcy are handled by Commercial Courts. Appeals against decisions of Municipal Courts are heard by County Courts and appeals against decisions of Commercial Courts are handled by the High Commercial Court. As of 1 January 2012 administrative law issues are in the first instance decided by four administrative courts (in Zagreb, Split, Rijeka and Osijek). Subject to certain conditions, an appeal against administrative court's decision may be lodged before the High Administrative Court. The Supreme Court of Croatia hears recourse against all appellate court's decisions.

Litigation in Croatia is lengthy. It commonly takes several years to resolve a case through the judicial system. Judicial proceedings rely mostly on written argument. Evidence is presented to the court in hearings, which are often prolonged for several times during first instance proceedings. First instance decisions are routinely appealed against to the higher instance.

11.2. Arbitration and ADR

In commercial practice, disputes are increasingly being resolved by arbitration. Arbitration is governed primarily by the Arbitration Act, a statute largely modelled on the 1985 UNCITRAL Model Law on International Commercial Arbitration and in particular on the German implementation of the Model Law.

Most domestic and many international arbitration disputes involving Croatian parties are handled by the Permanent Arbitration Court of the Croatian Chamber of Commerce, the leading arbitration institution in the country. *Ad hoc* arbitration, though fully permitted, is less used in practice. A number of organizations have established specialized arbitration institutions (e.g. the domain name arbitration facility of CarNet, the administrator of the .hr Internet domain, or the Arbitration Court of the Croatian Olympic Committee).

Croatia is a party to the 1958 New York Convention on Recognition and Enforcement of Foreign Arbitral Awards, the 1965 Washington Convention on the Settlement of Investment Disputes between States and Nationals of Other States and the 1961 European Convention on International Commercial Arbitration.

Mediation is increasingly being used as a method of resolving commercial and collective labour disputes. Mediation is regulated by the Conciliation Act, a statute adopted in 2011, which is modelled on EU Directive 2008/52/EC of the European Parliament and of the Council of 21 May 2008 on certain aspects of mediation in civil and commercial matters, the 2001 UNCITRAL Model Law on International Commercial Conciliation and the relevant Recommendations of the European Council on mediation in civil and commercial matters. The mediation of commercial disputes is organized by certain non-for-profit organizations, such as the Conciliation Centre of the Croatian Chamber of Commerce. A number of court-annexed mediation programs have been launched recently.

12. CONCESSIONS

Concessions are generally governed by the Act on Concessions. However, different special laws regulate certain issues in relation to concessions for particular activities or resources.

According to the Concessions Act, a concession can be obtained for commercial use of common or other good of interest for the Republic of Croatia (e.g. water and adjacent land), for public works and for public services. Concession cannot be obtained for exploitation of forest and forest land owned by the Republic of Croatia or for exploitation of other goods designated by special laws. Duration of concessions has to be determined in a manner which shall not restrict market competition more than necessary to ensure amortization of concessionaire investments and reasonable return on invested capital. Concessions are granted by the Croatian Parliament, the Croatian Government, central bodies of state administration, competent bodies of local and regional self-governmental units and legal persons authorized by special law.

A natural or legal person, both domestic and foreign, can obtain a concession. The decision is adopted after conduct of appropriate proceedings regulated by the Concessions Act. The decision may be based on two criterions: (i) the highest offered concession fee, or (ii) economically the most beneficial offer. The latter is determined taking into account the overall elements of the offer including the amount of concession fee, technology used, the aesthetic, functional and ecological elements, the operative expenses, etc. A successful applicant must enter into a separate concession agreement made with the provider of concession. The concession is registered in the register held by the Ministry of Finance.

Various regulations governing specific activities or sectors contain more detailed regulations of concessions. Some of them limit the possibility of obtaining concessions to resident persons or entities only. For example, the Mining Act provides that concessions may be granted only to a company having its registered seat or a branch office in Croatia, registered for such an activity, or to an individual registered craftsman for such an activity in Croatia (with the exception of entities domiciled in EU, after Croatia accedes to the EU). Some other examples of legislative acts regulating concessions for specific sectors include the Electronic Communications Act, the Waters Act, the Maritime Domain and Maritime Harbours Act and the Act on Roads.

13. PRE-BANKRUPTCY SETTLEMENT AND BANKRUPTCY

The Act on Financial Operations and Pre-Bankruptcy Settlement entered into force on 1 October 2012 in an attempt to achieve debt restructuring of companies facing bankruptcy. Insolvent companies have to immediately undertake appropriate measures of financial restructuring towards achieving financial solvency. These measures may include activities such as renegotiating payment terms and amounts of outstanding payables, increases of share capital, debt to equity swaps, etc.

If voluntary restructuring measures fail, the pre-bankruptcy settlement procedure should be initiated within 60 days from the short-term insolvency or within 21 days from insolvency.

A short-term insolvency is defined as a situation where (i) a company is in default for over 60 days with payment of invoices exceeding 20% of the value of total company's short-term obligations recorded in last published financial statements, or where (ii) a company is late for over 30 days with payment of employee salaries and related contributions. Also, a company is presumed insolvent when (i) the company is incapable on a more permanent basis (exceeding 60 days) to fulfil its monetary debts, or when (ii) the company is over-indebted.

The pre-bankruptcy settlement procedure is conducted before the Financial Agency, and the duration of the procedure is limited to 120 days. If the pre-bankruptcy settlement cannot be completed within 120-days deadline, the company shall enter bankruptcy proceedings.

Bankruptcy proceedings in Croatia may be initiated over legal entities and certain categories of individuals, notably sole traders and registered craftsmen. Bankruptcy proceedings may be initiated by any of the company's creditors or by the debtor company itself. Under Croatian law, there are three reasons for filing for bankruptcy: (i) short-term insolvency, (ii) insolvency and (iii) overindebtness. While a short-term insolvency refers to inability of the company to timely fulfil its due monetary obligations within a particular period, insolvency occurs where a company cannot fulfil its due monetary obligations on a more permanent basis. Overindebtness on the other hand, means that a company's assets do not cover its existing liabilities.

The principal players in the bankruptcy proceedings are the bankruptcy judge, the bankruptcy manager, the creditors' assembly and the creditors' committee.

In general, pre-proceedings are conducted prior to opening of the bankruptcy proceedings to confirm whether the conditions for filing for bankruptcy are fulfilled. Once the bankruptcy procedure is opened, it may take two principal courses: towards liquidation of the company or towards the company's reorganization. The creditors' assembly may decide which course the proceedings will take as well as whether the debtor company will continue with its business activities during the bankruptcy proceedings or will cease to conduct business.

In general, the liquidation route is used more frequently in Croatia. The assets of the debtor company are sold separately, and the creditors share the amount acquired through such sales.

The proceeds acquired though the sale of a debtor's assets are divided among the creditors, after the costs of the bankruptcy proceedings and certain other costs incurred by running the business during bankruptcy are covered. Under the law, creditors are placed in different priority ranks, depending on the nature of their claims. The first priority rank is reserved for certain claims of workers of the debtor company. The next priority rank is the general rank in which all claims not belonging to other ranks are placed. Finally, the lowest priority rank is reserved for certain other claims enumerated by the law, such as interest after opening bankruptcy proceedings, penalties, etc.

The Croatian laws also provide for separate settlement of claims of secured creditors. Secured creditors are generally entitled to request separate sale of assets used as security and to priority settlement of their secured claims from the proceeds of such separate sale.

The reorganization route is more complex and therefore less frequently used. After opening of the bankruptcy, the reorganization plan may be submitted by the bankruptcy manager or by the individual debtor. The reorganization plan must be approved by the creditors observing a special voting procedure and certain other restrictions aimed at assuring a fair and equal treatment of all creditors. The approval of the debtor company is required as well, although under certain circumstances this approval will be presumed. A final confirmation of the plan is given by the bankruptcy judge.

Summary bankruptcy proceedings may be initiated by the Tax Administration of the Ministry of Finance. Such proceedings are initiated over every legal person that (i) does not employ any worker, (ii) is in the status of short-term insolvency and (iii) for which conditions for deletion from the court registry have not been met. Depending on each individual case, summary proceedings lead to either faster liquidation of the debtor company or to initiation of the regular bankruptcy proceedings.

14. PUBLIC PROCUREMENT

On 1 January 2012 the new Public Procurement Act came into force. The 2012 Public Procurement Act was modelled on a number of EU instruments including Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for award of public works contracts, public supply contracts and public service contracts, Directive 2004/17/EC of the European Parliament and of the Council of 31 March 2004 coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors, as well as Council Directive 89/665/EEC of 21 December 1989 on the coordination of laws, regulations and administrative provisions relating to the application of review procedures to the award of public supply and public works contracts.

Public Procurement Act regulates conclusion of public procurement contracts and framework agreements for procurement of goods, works or services, legal remedies and the supervisory and other competences of the central state administration body. It applies to procurements executed by contracting authorities (e.g. the state bodies of the Republic of Croatia, local and regional self-government units) and contracting entities equalling or exceeding the amount of HRK 70,000 (approximately EUR 9,200) VAT exclusive.

The procurement may be conducted by (i) public tendering in a public procurement procedure, (ii) selective tendering in a limited procurement procedure or (iii) direct dealing in a negotiated procurement procedure.

All public procurement notices for procurement with the estimated value equalling or exceeding HRK 70,000 (approximately EUR 9,200) need to be published in the Electronic Public Procurement Classifieds of the Republic of Croatia. On the date of accession of the Republic of Croatia to the European Union, public procurement notices for high value procurement (determined in accordance with EU thresholds) shall be published in the Official Journal of the European Union as well.

As a rule, foreign competitors are treated equally as local business entities.

The State Commission for the Supervision of Public Procurement Procedures (the State Commission) is competent to decide on appeals in relation to procedures for conclusion of public procurement contracts, framework agreements and tenders governed by public procurement rules. An administrative dispute against a decision of the State Commission may be initiated before a competent administrative court.

Croatia is participating in the European Public Procurement Network, an international co-operation network of public procurement expert officials creating a reliable and effective forum for an informal co-operation on problem-solving in cross-border public procurement (the Croatian experts web page is available at URL: http://www.publicprocurementnetwork.org/index.php?option=com_contact&view=category&catid=75&Itemid=53).

15. APPENDIXES

15.1. Bilateral Investment Treaties[6]

Country	Date of execution	Date of coming into force
Albania	10 May 1993	16 April 1994
Argentina	2 December 1994	1 June 1996
Austria	19 February 1997	1 November 1999
Azerbaijan	2 October 2007	30 May 2008
Belarus	26 June 2001	14 July 2005
Belgium	31 October 2001	28 December 2003
Belgo-Luxemburg Economic Union	31 October 2001	28 December 2003
Bosnia and Herzegovina (applicable to the territory of the Federation of Bosnia and Herzegovina)	26 February 1996	4 August 1997
Bosnia and Herzegovina	23 June 2002	3 January 2005
Bulgaria	25 June 1996	20 February 1998
Cambodia	18 May 2001	15 June 2002
Canada	3 February 1997	30 January 2001
Chile	28 November 1994	15 June 1996
China	7 June 1993	1 July 1994
Cuba	16 February 2001	_____
Czech Republic	5 March 1996	15 May 1997
Denmark	5 July 2000	12 January 2002
Egypt	27 October 1997	2 May 1999
Finland	1 June 1999	1 November 2002
France	3 June 1996	5 March 1998
Germany	21 March 1998	28 September 2000
Greece	18 October 1996	21 October 1998
Hungary	15 May 1996	1 March 2002
India	4 May 2001	19 January 2002
Indonesia	10 September 2002	_____
Iran	17 May 2000	20 July 2005
Israel	1 August 2000	13 July 2003
Italy	5 November 1996	12 June 1998
Jordan	10 October 1999	27 April 2000

[6] Source: Web site of the Ministry of Foreign Affairs and European Integration of the Republic of Croatia

Country	Date of execution	Date of coming into force
Republic of Korea	19 June 2005	31 May 2006
Kuwait	8 March 1997	2 July 1998
Latvia	4 April 2002	25 May 2005
Libya	20 December 2002	21 June 2006
Lithuania	15 April 2008	30 January 2009
Luxemburg	31 October 2001	28 December 2003
Macedonia	6 July 1994	6 October 1995
Malaysia	16 December 1994	20 July 1996
Malta	11 July 2001	10 May 2002
Morocco	29 September 2004	_____
Moldova	5 December 2001	20 March 2007
Mongolia	8 August 2006	_____
Netherlands	28 April 1998	1 June 1999
Oman	4 May 2004	_____
Poland	21 February 1995	4 October 1995
Portugal	10 May 1995	24 October 1997
Qatar	12 November 2001	_____
Romania	8 June 1994	30 April 1998
Russian Federation	20 May 1996	_____
San Marino	7 May 2004	27 July 2005
Serbia	18 August 1998	31 January 2002
Slovakia	12 February 1996	6 February 1997
Slovenia	12 December 1997	8 July 2004
Spain	21 July 1997	17 September 1998
Sweden	23 November 2000	1 August 2002
Switzerland	30 October 1996	17 June 1997
Thailand	18 February 2000	10 August 2005
Turkey	12 February 1996	21 April 1998
Ukraine	15 December 1997	5 June 2001
United Kingdom of Great Britain and Northern Ireland	11 March 1997	16 April 1998
United States of America	13 July 1996	20 June 2001
Zimbabwe	18 February 2000	_____

15.2. Double Tax Treaties[7]

Country	Date of coming into force	Withholding Tax on Dividends	Withholding Tax on Royalties	Withholding Tax on Interests
Albania	05/06/1997	**10%**	**10%**	**10%** (**0%** when the payee is the state or central bank)
Armenia	18/02/2010	**10%** or **0%** (if the beneficiary is a company holding (directly or indirectly) at least 25% of the share capital of the paying company in the period of at least 2 years before dividend paying date, and such dividends are not subject to income tax in the other Contracting State)	**5%**	**10%**
Austria	28/06/2001	**15%** or **0%** (if the beneficiary is a company directly holding at least 10% of the share capital of the paying company)	**0%**	**5%**
Belarus	04/06/2004	**15%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**10%**	**10%**
Belgium	01/04/2004	**15%** or **5%** (if the beneficiary is a company holding (directly or indirectly) at least 10% of the share capital of the paying company)	**0%**	**10%** (**0%** interests arising from: (i) commercial credits; (ii) loans granted for export promotion; (iii) bank loans; (iv) bank deposits or when the payee is the state or central bank)
Bosnia and Herzegovina	22/06/2005	**10%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**10%**	**10%**
Bulgaria	30/07/1998	**5%**	**0%**	**5%**
Canada	23/11/1999	**15%** or **5%** (if the beneficiary is a company controlling (directly or indirectly) at least 10% of the voting rights in the paying company or if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**10%**	**10%**

[7] Source: Web site of the Ministry of Foreign Affairs and European Integration of the Republic of Croatia

Country	Date of coming into force	Withholding Tax on Dividends	Withholding Tax on Royalties	Withholding Tax on Interests
Chile	22/12/2004	**15%** or **5%** (if the beneficiary is a company directly holding at least 20% of the share capital of the paying company)	**10%** or **5%** (compensation for use of industrial, commercial or scientific equipment)	**15%** or **5%** (interests on loans provided by banks or insurance companies)
China	18/05/2001	**5%**	**10%**	**10%** (**0%** if the payee is the state, central bank or state-owned financial institution or interests arise out of loans granted by the state, central bank or a state-owned financial institution)
Czech Republic	28/12/1999	**5%**	**10%**	**0%**
Denmark	22/02/2009	**10%** or **5%** (if the beneficiary is (i) a company directly holding at least 25% of the share capital in the paying company in the period of at least 1 year within which the dividends are published and (ii) pension fund or other similar institution)	**10%**	**5%**
Egypt	_____	**12%**	**12%**	**12%** (**0%** when the payee is the state or central bank)
Estonia	12/07/2004	**15%** or **5%** (if the beneficiary is a company directly holding at least 10% of the share capital of the paying company)	**10%**	**10%** (**0%** if the payee is the state, central bank or a state-owned bank)
Finland	08/10/1991	**15%** or **5%** (if the beneficiary is a company holding at least 25% of the share capital of the paying company)	**10%**	**0%**
France	01/09/2005	**15%** or **0%** (if the beneficiary is a company holding (directly or indirectly) at least 10% of the share capital of the paying company)	**0%**	**0%**
Germany	20/12/2006	**15%** or **5%** (if the beneficiary is a company directly holding at least 10% of the share capital of the paying company)	**0%**	**0%**
Greece	18/12/1998	**10%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**10%**	**10%**

Country	Date of coming into force	Withholding Tax on Dividends	Withholding Tax on Royalties	Withholding Tax on Interests
Hungary	08/05/1998	**10%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**0%**	**0%**
Indonesia	_____	**10%**	**10%**	**10%** (**0%** if the payee is the state government, its local body, central bank, or financial institution controlled by such government)
Iran	30/10/2008	**10%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**5%**	**5%** (**0%** if the payee is the state, central bank or a state-owned bank)
Ireland	30/10/2003	**10%** or **5%** (if the beneficiary is a company directly holding at least 10% of the voting rights in the paying company)	**10%**	**0%**
Island	_____	**10% or 5%** (if the beneficiary is company directly holding at least 10% of the share capital of the paying company)	**10%**	**10%** (**0%** if the interests accrued in one state are realized or used by the government of other state, its authorities, central bank, government-owned financial institution or if interests arise from loans granted by the government of other state)
Israel	01/02/2007	**15%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)*	**5%**	**10%** (**5%** if the interests accrued in one state arise from loans granted by the banks of the other state; **0% (i)** if interests arise from commercial credits; (ii) if interests arise from loans granted by or on behalf of the state)

* Withholding tax on dividends will be paid at the rate of 10% if the beneficiary is a company directly holding at least 10% of the paying company seated in Israel, and the profit out of which the dividends are paid out is taxed in Israel at the rate lower than the general rate of the Israeli profit tax.

Country	Date of coming into force	Withholding Tax on Dividends	Withholding Tax on Royalties	Withholding Tax on Interests
Italy	15/09/2009	**15%**	**5%**	**10%** or **0%** ((i) if the payer is the government of the other state or its local self-government and government body, (ii) if the payee is the government of the other state or its local self-government or government body or any agency or proxy wholly owned by any of them, (iii) if the payee or intermediary is any other agency in relation to loans arising from contracts concluded between states)
Jordan	17/02/2006	**10%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**10%**	**10%**
Republic of Korea	15/09/2006	**10%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**0%**	**10%**
Kuwait	09/01/2003	**0%**	**10%**	**0%**
Latvia	27/02/2001	**10%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**10%**	**10%** (**0%** when a loan is provided or financed by the state, central bank or state-owned financial institution)
Lithuania	30/03/2001	**15%** or **5%** (if the beneficiary is a company directly holding at least 10% of the share capital of the paying company)	**10%**	**10%** (**0%** when a loan is provided or financed by the state, central bank or a state-owned financial institution)
Macedonia	11/01/1996	**15%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**10%**	**10%** (**0%** when a loan is provided or financed by the state, central bank or a state-owned financial institution)
Malaysia	15/07/2004	**10%** or **5%** (if the beneficiary is a company directly holding at least 10% of the share capital of the paying company)	**10%**	**10%** (**0%** when the payee is the state or the central bank)

Country	Date of coming into force	Withholding Tax on Dividends	Withholding Tax on Royalties	Withholding Tax on Interests
Malta	22/08/1999	**5%** (if the dividends are paid by a Croatian company to a Maltese resident) or **Maltese profit tax rate** (if the dividends are paid by a Maltese company to a Croatian resident)	**0%**	**0%**
Mauritius	09/08/2003	**0%**	**0%**	**0%**
Moldova	10/05/2006	**10%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**10%**	**5%**
Morocco	_____	**10%** or **8%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**10%**	**10%** or **0%** (if the payee is the government or central bank)
Netherlands	06/04/2001	**15%** or **0%** (if the beneficiary is a company limited on shares directly holding at least 10% of the share capital of the paying company)	**0%**	**0%**
Norway	08/10/1991	**15%**	**10%**	**0%**
Oman	16/02/2011	**0%**	**10%**	**5%** or **0%** (if the payee is the government, central bank, every state body or institution in major ownership of the government, Oman's General reserve state fund and Oman's investment fund)
Poland	11/02/1996	**15%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**10%**	**10%** (**0%** when the loan is provided or financed by the state, central bank or a state-owned financial institution)
Quatar	_____	**0%**	**10%** (if the beneficiary is resident of the other Contracting State)	**0%**

Country	Date of coming into force	Withholding Tax on Dividends	Withholding Tax on Royalties	Withholding Tax on Interests
Romania	28/11/1996	**5%**	**10%**	**10%** (**0%** if the payee is the state, a state agency or state banking institution, or interests arise from loans guaranteed, secured or financed by a state-owned financial institution)
Russian Federation	19/04/1997	**10%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital (min. USD 100,000) of the paying company)	**10%**	**10%**
San Marino	05/12/2005	**10%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**5%**	**10%** (**0%** if: (i) the payer is the state; (ii) the payee is the state or a state-owned institution; (iii) interests are paid on behalf of the state on loans granted in accordance with inter-governmental treaties)
Slovakia	14/11/1996	**10%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**10%**	**10%**
Slovenia	10/11/2005	**5%**	**5%**	**5%** (**0%** if a loan is granted by the state, central bank or an institution authorized in accordance with international rules on securing and financing international business transactions)
Serbia	22/04/2004	**10%** or **5%** (if the beneficiary is a company holding at least 25% of the share capital of the paying company)	**10%**	**10%**
Republic of South Africa	11/11/1997	**10%** or **5%** (if the beneficiary is a company holding at least 25% of the share capital of the paying company)	**5%**	**0%**

Country	Date of coming into force	Withholding Tax on Dividends	Withholding Tax on Royalties	Withholding Tax on Interests
Spain	20/04/2006	**15%** or **0%** (if the beneficiary is a company limited on shares directly holding at least 25% of the share capital of paying company	**8%**	**8%** (**0%**: (i) interests on bank loans; (ii) interests arising from commercial credits; (iii) interests paid to the state, central bank or a state-owned financial institution
Sweden	08/10/1991	**15%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**0%**	**0%**
Switzerland	20/12/1999	**15%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**0%**	**5%**
Syria	06/02/2009	**10%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**12%**	**10%**
Turkey	18/05/2000	**10%**	**10%**	**10%**
Ukraine	01/06/1999	**10%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**10%**	**10%** (**0%** if the payee is the state, central bank or a state-owned financial institution and interests arise out of loans indirectly financed by the state, central bank or state-owned financial institution
United Kingdom of Great Britain and Northern Ireland	08/10/1991	**15%** or **5%** (if the beneficiary is a company directly holding at least 25% of the share capital of the paying company)	**10%**	**10%**

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