Croatia

Zoran Vukić

Law firm Vukić and Partners

Ana Bukša

1 Relevant Authorities and Legislation

1.1 What regulates M&A?

The principal body of law regulating corporate aspects of mergers and acquisitions in Croatia is the Companies Act (Official Gazette eds. 111/1993, 34/1999, 121/1999, 52/2000, 118/2003, 146/2008, 111/2012, 125/2011, 68/2013, 110/2015).

There are special rules concerning the takeover of joint stock companies contained in the Act on the Takeover of Joint Stock Companies (Official Gazette eds. 109/2007, 36/2009, 108/2012, 90/2013, 99/2013, 148/2013). Relatedly, the takeovers of publicly traded joint stock companies are regulated in the Capital Markets Act (Official Gazette eds. 65/2018) and the Rules of the Zagreb Stock Exchange and related regulations.

M&A issues are also dealt with in certain sector-specific legislation, such as the Credit Institutions Act (Official Gazette eds. 159/2013, 19/2015, 102/2015, 15/2018), Leasing Act (Official Gazette ed. 141/2013), Factoring Act (Official Gazette eds. 94/2014, 85/2015, 41/2016), Insurance Act (Official Gazette ed. 30/2015), Act on Pension Insurance Companies (Official Gazette eds. 22/2014, 29/2018), *et al*.

Certain M&A aspects of transactions related to pre-bankruptcy or bankruptcy of companies can be found in the Bankruptcy Act (Official Gazette eds. 71/2015, 104/2017) and the Act on Recovery of Credit Institutions and Investment Companies (Official Gazette ed. 19/2015).

1.2 Are there different rules for different types of company?

Special rules apply to publicly traded joint stock companies. These include rules on the takeover bid (optional or mandatory), publication of the takeover bid, IPO process and prospectus, prohibition of joint actions aimed at preventing takeovers, price determination rules, rules for the governing bodies of the target, minority rights, supervisory authority of state bodies and the like.

Companies incorporated and traded outside of Croatia are subject to diminished supervisory authority of Croatian bodies, provided they hold the appropriate authorisations from their relative countries.

The Act on Takeover of Joint Stock Companies applies equally to domestic and EU targets, specifically companies incorporated in Croatia, but traded in another Member State, and companies incorporated in another Member State and also traded outside of Croatia.

1.3 Are there special rules for foreign buyers?

As a rule, foreign buyers are subject to the same regime as domestic buyers.

1.4 Are there any special sector-related rules?

Croatian legislation contains sector-related restrictions regarding the acquisition of the "qualifying holding" in the sense of Article 4, paragraph 1, section 36 of the Regulation (EU) No. 575/2013, i.e. a direct or indirect holding in an undertaking which represents 10% or more of the capital or of the voting rights, or which makes it possible to exercise a significant influence over the management of that undertaking. These apply to credit institutions, investment companies, factoring and leasing companies, and insurance and pension insurance companies. The acquisition of a qualifying holding in a credit institution is subject to prior consent of the Croatian National Bank, which will base its decision on, *inter alia*, the following criteria: reputation of the acquirer, including the reputation of its shareholders or indirect qualified shareholders and their influence on the acquirer; reputation and expertise of the persons it intends to appoint as management of the target; financial status of the acquirer, including the financial of its shareholders or indirect qualified shareholders and their financial impact on the acquirer; ability to meet conditions set out in Croatian and EU legislation; and no indication of money laundering or financing of terrorism practices.

Acquisitions of qualifying holdings in factoring and leasing companies, as well as insurance and pension insurance companies, are subject to the approval of the Croatian Financial Services Supervisory Agency, with the decisive criteria equal to those applying to credit institutions. Further consents are required if qualifying holdings exceed or fall under thresholds of 10%, 20%, 30% or 50% of capital or voting rights.

1.5 What are the principal sources of liability?

Apart from contractual liability, parties in M&A transactions are subject to strict statutory requirements which are, for the most part, mandatory. Therefore, breaches of such legislation lead to two basic consequences: first, such breaches trigger various authorities of the regulator, including the authority to annul the bid or order the sale of shares; and second, these incur liability for offences of the party in breach. Offences of legal entities are subject to fines in various amounts, depending on the gravity of the offence. These range

between HRK 20,000.00 and as much as 10% of the protected value in case of credit institutions. For example, failure to notify the Croatian Financial Services Supervisory Agency on reaching the thresholds of 10%, 20%, 30% or 50% of capital or voting rights is subject to a fine of 3% to 5% of total turnover of the offending entity, plus a fine ranging between HRK 100,000.00 and HRK 5,000,000.00 for the responsible natural person within that entity. Insider trading and abuse of capital markets are criminal offences, punishable by imprisonment of up to five years.

2 Mechanics of Acquisition

2.1 What alternative means of acquisition are there?

Other than acquiring the shares of the target itself, control over the target may be gained in one of the following ways: acquisition of shares in the majority shareholder or shareholders; merger with the majority shareholder or shareholders; entering into the ownership structure of the company through the increase of share capital; or gaining control of the target through management agreements.

However, relevant legislation applies equally to both direct and indirect acquisitions, which makes the regulatory requirements in both scenarios essentially the same. The decision on the type of acquisition therefore lies mostly in commercial or simply practical terms – tax liability, possibility of a deadlock in the decision-making process, simplicity of procedure, etc.

In the event of restructuring or bankruptcy, there is the possibility of debt-to-equity swaps as a part of the restructuring plan either in pre-bankruptcy or bankruptcy procedure, provided such plan is adopted by the prescribed majorities of votes of all creditors.

2.2 What advisers do the parties need?

In basic M&A transactions, the parties will normally require the assistance of local legal, financial and tax advisers, equally during the due diligence process preceding the transaction itself and during the preparation, carrying-out and registration of the transaction itself. The parties may also need the assistance of advisers with particular technical expertise, depending on the type of business of the target. More complex transactions may require the engagement of investment banks or specialised M&A consultants.

2.3 How long does it take?

The duration of the process varies, and shall depend on the overall complexity of the transaction, the approval requirements for certain types of transactions, and the preparedness of the bidder itself.

The competent authorities may be subject to deadlines in their actions, but these deadlines are, without exception, instructive in nature.

For example, in a takeover of a joint stock company, the bidder must file an application to approve publication of the bid within 30 days from when the obligation to publish arose, or from the date when special approval was granted with the Croatian Financial Services Supervisory Agency. The Agency is to decide within 14 days from the submission of a complete application. The bidder is then obliged to publish the bid within seven days. The bid must have a validity period between 28 and 60 days from publication, following which the price for the shares must be paid in the subsequent 14 days. Therefore, the entire process may take several months before completion.

2.4 What are the main hurdles?

The hurdles to a successful M&A transaction are mainly the formalities entailed (seeking approvals, drafting and producing documents that may have to be notarised, certified, apostilled, translated, etc.), as well the fact that state authorities are the ones who set the pace.

2.5 How much flexibility is there over deal terms and price?

In private companies, the parties are free to agree on any deal terms and price they consider appropriate. They are only restricted from the tax perspective, as the agreed price has to reflect the market value, i.e. it can in any event be taxed according to market value. However, in publicly traded joint stock companies, the Act on the Takeover of Joint Stock Companies regulates the minimum price to be offered in the bid, deadline for payment of acquired shares (see question 2.3 above), as well as the obligation to offer the same price for all shares of the same class included in the bid. The minimum price must be equivalent to the average price of previously acquired shares carrying voting rights or average price of shares in the regulated market, whichever is higher. The bidder is also obliged to prove that it has secured the price amount, either by depositing cash or securities or by providing a bank guarantee.

2.6 What differences are there between offering cash and other consideration?

In private companies, the parties are free to agree on the type of consideration they deem appropriate, subject to the same market value standard. However, consideration which is not in cash may delay the procedure somewhat, due to the requirement of an audit being carried out in such circumstances.

In publicly traded joint stock companies, the bidder is equally free to choose cash, substitution of shares or a combination of the two as consideration. However, if consideration is not primarily offered in cash, a cash consideration must exist as an alternative. The shares offered in substitution must be entered into the same segment of the regulated market, or at least a segment with an equivalent degree of transparency, they must be of the same type and class as the shares included in the bid, and they must not be encumbered.

2.7 Do the same terms have to be offered to all shareholders?

In the bid for takeover of a joint stock company, the same price must be offered to all shareholders for the same class of shares (preferred or common stock). If the takeover results in a 95% share, the minority shareholders can be squeezed out with "just compensation". In private companies, this is strictly a commercial matter.

2.8 Are there obligations to purchase other classes of target securities?

The takeover bid must include all classes of securities issued by the target company, which are not already owned by the bidder, apart from encumbered securities if the bidder chooses to exclude them. The bid cannot be conditional upon the class of security the bidder intends to acquire. Under Croatian law, these are preferred and

common stock – both represent equity, but only common stock bear voting rights.

2.9 Are there any limits on agreeing terms with employees?

As a general rule, all employment agreements concluded by the target remain in full force and effect, and the employees retain the same rights they had prior to the takeover. If the target company had a collective agreement in place, it will remain in force pending the conclusion of a new collective agreement, but for one year maximum. In the event of a merger, division, spin-off or takeover of an undertaking, as opposed to the acquisition of shares where the employer remains the same, both parties to the transaction will be jointly and severally liable for any employment-related liabilities arising up to the date of the transaction becoming effective.

2.10 What role do employees, pension trustees and other stakeholders play?

In the event of transfer of employment agreements, employee council and all affected employees must be notified in writing, in a timely fashion and prior to the date of transfer, on the date of transfer of their employment agreements, the reasons for such transfer, the impact this will have on the employees' legal, economic or social position, and envisaged measures concerning such employees.

In the event of a public takeover bid, the employees of the target company must be notified of its publication forthwith and have the right to give their opinion on the takeover bid.

2.11 What documentation is needed?

Documentation requirements vary depending on the type of transaction – is it public or private, is it a merger or an acquisition, and the type of company – a limited liability company or a joint stock company. The required documents can be roughly divided into (a) transaction documents, i.e. documents drafted in the transaction, and (b) acquirer documents, which must be submitted by the acquirer.

In the acquisition of shares in a limited liability company, the transaction documents include the share purchase agreement (in the form of a notarial deed or a solemnised private document), any amendments to incorporating documents (if necessary), plus additional documents such as the list of shareholders. Acquirer documents include identification documents for natural persons, or commercial registry extracts for legal entities, as well as statements on non-existence of debt for public duties in Croatia. In the acquisition of shares of a publicly traded joint stock company, transaction documents include, *inter alia*, the declaration of intent, the bid, the prospectus, application for publication of the bid, share purchase agreements, the takeover report, and the opinion of the target's management.

The acquirer documents in these transactions shall include: documents on legal transactions for the acquisition of previously owned shares in the target; bidder's declaration that no other attempts have been made at acquiring the target shares; the depository's certificate on securing the consideration for the transaction; the certificate of the market regulator on the average price of shares; agreement with the depository for the deposit of shares; prior approval by the Croatian National Bank or the Croatian Financial Services Supervisory Agency or other competent authority, when required; extract from the commercial or other registry for the bidder; statement on appointing an agent for the service of process in Croatia if the bidder is a foreign entity; survey on the fair value of shares; and other documents as may be required by the Croatian Financial Services Supervisory Agency.

In a merger, transaction documents include: the Merger Agreement; the merger report and audit report; decisions of general assemblies/shareholders of both parties to the transaction; decisions on increase of share capital, if required to complete the merger; while acquirer documents are the same as in share acquisitions. Filing of documents is generally subject to payment of administrative or court charges. All documents must be originals or certified true copies. Documents drafted in a foreign language must be translated into Croatian by a certified translator.

2.12 Are there any special disclosure requirements?

In the process of taking over a publicly traded joint stock company, the bidder must disclose the following information (to be published as part of the bid): name; legal form; seat and business address (or name and address of a natural person as the bidder); scope of business; and basic business and financial indicators. The bidder is also obliged to provide information on other transactions regarding the shares of the target company, as well as documents on these transactions. When the transaction is subject to special approvals, the bidders are obliged to disclose additional information in order to obtain the approval, such as: list of shareholders; financial reports; criminal and offences record; certificate of good standing, etc.

2.13 What are the key costs?

Apart from the consideration for the shares, key costs can be summarised as deposit costs and transfer costs (advisory and notarial fees, administrative and court charges). The final cost amount shall, for the most part, depend on the value of the transaction.

2.14 What consents are needed?

Approvals in sector-specific transactions have been dealt with in question 1.4 above. Also, in the bid process for the takeover of a publicly traded joint stock company, the approval for publication of the bid must be granted by the Croatian Financial Services Supervisory Agency. As far as mergers are concerned, the general assemblies or shareholders of both participants in the transaction must give their consent to the merger. Mergers and acquisitions of companies with an overall consolidated revenue of HRK 1,000,000,000.00 in the year preceding the transaction, or HRK 100,000,000.00 per participant, are subject to approval by the Croatian Competition Agency, to make sure these do not lead to prevention, restriction or distortion of competition in the relevant market.

2.15 What levels of approval or acceptance are needed?

In principle, the transfer of shares in a limited liability company is not subject to any approvals, except when its articles of association provide for the consent of the company for such transfer. This consent may be replaced by a court decision if withheld without reasonable cause, and if the transfer will not cause damage to the company, its shareholders and creditors. In the takeover of publicly traded joint stock companies there is no universally applicable

acceptance threshold, but the voluntary bid may be conditioned by reaching a certain success threshold, which cannot be lower than 25%. In mergers, the general assembly decisions must be reached by a 75% majority.

2.16 When does cash consideration need to be committed and available?

In private transactions, this issue will be governed by the parties' agreement. In the acquisition of shares in a publicly traded joint stock company, the bidder must secure funds to pay consideration prior to filing the application for publication of the bid.

3 Friendly or Hostile

3.1 Is there a choice?

Croatian legislation does not differentiate between a friendly and a hostile takeover.

3.2 Are there rules about an approach to the target?

There is no legislation containing explicit rules about an approach to the target.

3.3 How relevant is the target board?

In private transactions for the acquisition of shares in a limited liability company, the target board plays an important role only if the transaction is subject to the consent of the company. In transactions regarding the takeover of joint stock companies, the management of the target gives its opinion on the proposed transaction, specifically on the type and amount of consideration, future business and strategic plans furnished by the bidder, and offers a conclusion whether it will accept or decline the bid. The management is obliged to provide information on the existence of any agreements with the bidder concerning the bid. In mergers, the board simply has a duty to implement decisions made by the shareholders' meeting.

3.4 Does the choice affect process?

Croatian legislation does not differentiate between a friendly and a hostile takeover, so any such distinction would not affect process.

4 Information

4.1 What information is available to a buyer?

The buyer can obtain basic corporate information on the target by using the Court Register (available at https://sudreg.pravosudje.hr) and the services of the Central Clearing & Depository Company (http://www.skdd.hr) to obtain information on the 10 largest shareholders in a joint stock company. Most legal entities are obliged to publish their financial reports, which can be found at https://rgfi.fina.hr. Publicly traded companies are also obliged to publish their financial reports on their websites and the website of the Zagreb Stock Exchange (http://www.zse.hr). Any indication of bankruptcy or pre-bankruptcy proceedings filed or initiated in respect of the target can be checked at https://e-oglasna.pravosudje.hr/?q=stecajne-objave. The Land Register is also available online, at https://oss.uredjenazemlja.hr.

4.2 Is negotiation confidential and is access restricted?

There is no specific legislation regulating the negotiation process in M&A transactions. In practice, they will be kept confidential by the parties on the basis of a mutually agreed non-disclosure agreement. The extent of access will generally be governed by the parties' agreement, prior to the publication obligations being triggered.

4.3 When is an announcement required and what will become public?

The Croatian Financial Services Supervisory Agency may require an entity to give an express declaration on the intended takeover if the situation in the capital market indicates a potential takeover, and especially when circumstances indicate the existence of a takeover agreement or there have been significant changes in trading and price of shares in the regulated market, or if that entity has expressed its intent to carry out the takeover in any other way. At the request of the Agency, this declaration must be published without delay. There are no specific rules as to the contents of the declaration.

4.4 What if the information is wrong or changes?

If the takeover bid is missing information that could influence the decision on acceptance, or if this information is false or incorrect, all persons who participated in its preparation will be jointly and severally liable to shareholders for any damage thus incurred. When the obligation for publishing a prospectus is triggered, the persons responsible for the correctness and completeness of information stated in the prospectus are the issuer, bidder, guarantor (when applicable) and persons who assume liability voluntarily. They are jointly and severally liable for any damage that may arise as a consequence of incomplete or incorrect information. If any new circumstances occur after the prospectus is approved and before the expiry of the offer or start of trading, whichever is later, or inaccuracies are found, the issuer or the bidder are obliged to supplement the prospectus with new, accurate and complete information, subject to prior approval of the Croatian Financial Services Supervisory Agency. The Croatian Financial Services Supervisory Agency is not liable for the accuracy of information provided. The special regulations do not provide for the bidder's right to withdraw from the transaction in these cases, but this does not preclude the bidder to challenge the transaction based on fundamental error.

5 Stakebuilding

5.1 Can shares be bought outside the offer process?

In principle, they cannot. From the moment when the obligation to publish the bid was incurred up to the expiry of the bid, the bidder must not acquire, or undertake to acquire in any way other than through the bidding process.

5.2 Can derivatives be bought outside the offer process?

The trading restrictions only apply to shares, i.e. equity shares,

which would mean that trading in derivatives would not be prohibited.

5.3 What are the disclosure triggers for shares and derivatives stakebuilding before the offer and during the offer period?

Reaching, exceeding or falling under the threshold of 5%, 10%, 15%, 20%, 25%, 30%, 50% and 75% of voting rights in the issuer, held directly or indirectly, will always trigger disclosure obligations. These thresholds are not limited to the holding of shares but also to other financial instruments and derivatives. These circumstances must be disclosed to the issuer and to the Croatian Financial Services Supervisory Agency. Any and all documents concerning transactions for the acquisition of shares in the target company preceding the bid must be submitted with the bid to the Croatian Financial Services Supervisory Agency.

5.4 What are the limitations and consequences?

The breach of limitations described in questions 5.1, 5.2 and 5.3 can trigger supervision by the competent authorities, who are authorised, *inter alia*, to invalidate the bid. Also, it will lead to liability for offences.

6 Deal Protection

6.1 Are break fees available?

Break fees are not envisaged in current legislation in force, but nothing suggests the parties to a transaction would be prohibited from agreeing on them.

6.2 Can the target agree not to shop the company or its assets?

There is nothing to suggest that the target would be prohibited from doing so, but this cannot prevent the filing of a competitive bid by an independent third party who is willing to offer a higher price.

6.3 Can the target agree to issue shares or sell assets?

As a general principle, the management of the target is obliged to act in the target's best interest during the takeover process. In this vein, the management cannot increase share capital, enter into transactions outside the scope of regular business operations, act in a way that could jeopardise the business of the target, decide on acquisition or alienation of own shares or financial instruments providing entitlement to such shares, or act in any way that would hinder or disable the bid process, without the consent of the shareholders' meeting reached by a 75% majority.

6.4 What commitments are available to tie up a deal?

There are no such commitments expressly defined in current legislation.

7 Bidder Protection

7.1 What deal conditions are permitted and is their invocation restricted?

Any deal conditions not subject to the limitations and regulations described above are, provided the general principles of acting in good faith are met, permitted.

However, once a bid is published, it will become irrevocable and the bidder will be under an obligation to buy the deposited shares with two exceptions: if there is a published competing bid offering a higher price; or if the target goes bankrupt.

7.2 What control does the bidder have over the target during the process?

The bidder has no control over the target during the bidding process. The legislation, however, imposes certain restrictions on the management of the target described in question 6.3 above aimed at facilitating the transaction and protecting the bidder.

7.3 When does control pass to the bidder?

The bidder gains title over the acquired shares when its title is registered with the Court Register (if the target is a limited liability company) or with the Central Depository & Clearing Company Inc. (if the target is a joint stock company). Title also has to be registered in the shareholder register of the target. In the event of a merger, its legal effects arise upon registration with the Court register.

7.4 How can the bidder get 100% control?

If the bidder, along with its affiliated entities, holds 95% of shares carrying voting rights in the target, the bidder is entitled to take over the minority shares in exchange for just compensation, within three months from the expiry of the bid. Just compensation means the price of the bid, plus any increases if shares were subsequently acquired at a higher price. This procedure is handled by the Central Depository & Clearing Company, Inc.

8 Target Defences

8.1 Does the board of the target have to publicise discussions?

There is no legislation obliging the board of the target to publicise discussions before the obligation to publish a prospectus is triggered. Reporting to shareholders and the supervisory board of the company regarding any discussions concerning a takeover should be done in the best interest of the target and may also be envisaged in the target's bylaws.

8.2 What can the target do to resist change of control?

There are no mechanisms envisaged in legislation for the target to resist the takeover. However, no shareholder, apart from minority shareholders in cases where the bidder owns 95%, is obligated to sell its share in the target.

8.3 Is it a fair fight?

Provided the legal requirements are met, the fight is fair. Any actions not meeting the said criteria are subject to the control of supervisory authorities and may lead to transactions being invalidated or fines being imposed on the offending parties.

9 Other Useful Facts

9.1 What are the major influences on the success of an acquisition?

Apart from commercial implications which are always primary, but not the topic of discussion here, our experience has shown that the greatest influence on the success of an acquisition is owed to the transparency and availability of information furnished by the target company, cooperation between the parties and their respective advisers, availability of documents to be provided by the bidder, as well as efficient communication with the regulatory authorities. Any "skeletons in the closet", or any reluctance to prepare and furnish documents in a systematic and timely fashion, can delay the procedure significantly.

9.2 What happens if it fails?

If the transaction fails without liability of any of the parties involved, each party will have to bear its own costs incurred during negotiations, unless otherwise agreed by the parties.

10 Updates

10.1 Please provide a summary of any relevant new law or practices in M&A in your jurisdiction.

In February of 2018, the legislator made significant amendments to the Credit Institutions Act, thus transposing the provisions of EU directives confirming the authority of the Croatian National Bank to supervise credit institutions with the same or similar risk profiles.

In July of 2018, the Croatian Parliament enacted the Act on Amendments to the Credit Institutions Act. The highlight of this Act is broadening the scope of authority of the Croatian Financial Services Supervisory Agency, particularly in the segment of supervision of financial reports of traded companies. The Agency now has the authority to act if it finds that the financial reports have not been made according to the relevant financial reporting framework, while previously it could only supervise the timeliness of their publication. These amendments are anticipated to have a positive impact on the transparency of the capital market which is to be achieved through, *inter alia*, raising the bar regarding providing services and information on services, as well as the obligation to gather, consolidate and publish standardised trading information. The amendments envisage more frequent notifications to clients, presenting all entailed costs of the investments, securing the most favourable execution for the client, logging communications and business archives. All these measures are being introduced or being made stricter with a view to protect investors.

Apart from this, the legislature in the M&A field has been silent in 2018.

The Croatian public is currently focused on the aftermath of the settlement executed in the extraordinary administration of the Agrokor concern, as well as the search for a strategic investor in shipbuilding which will determine the fate of two major Croatian shipyards currently facing bankruptcy.