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The International Comparative Legal Guide To Mergers & Acquisitions 2011

A practical cross-border insight
into mergers & acquisitions

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1 Relevant Authorities and Legislation

1.1 What regulates M&A?

M&A activities in Croatia are governed by various pieces of legislation. These include:

- the Company Act (Official Gazette 111/93, 34/99, 52/00, 118/03, 107/07, 146/08, 137/09);
- the Capital Market Act (Official Gazette 88/08, 146/08 and 74/09);
- the Joint Stock Companies Takeover Act (Official Gazette 109/07, 36/09) (hereinafter The Takeover Act);
- the Labor Act (Official Gazette 149/09);
- the Competition Act (Official Gazette 79/09);
- the Civil Code (Official Gazette 35/05, 41/08);
- the Leasing Act (Official Gazette 135/06); and
- the Investment Promotion Act (Official Gazette 138/06).

1.2 Are there different rules for different types of public company?

Different rules (more onerous and with public disclosure rules) apply for companies which fulfil one of the conditions set out by the Takeover Act, then for other types of companies.

The Takeover Act defines the Target Company as the joint stock company with a registered seat in the Republic of Croatia, with shares listed in the Regulated Market in Croatia.

The Capital Market Act defines “Regulated Market” as a multilateral system operated and/or managed by a market operator, which satisfies the following requirements:

- a. brings together or facilitates bringing together of multiple third-party buying and selling interests in financial instruments, in the system and in accordance with pre-determined nondiscretionary rules, and in a way that results in a contract in respect of the financial instruments admitted to trading under its rules and/or systems;
- b. is authorised as a regulated market; and
- c. functions regularly in accordance with the provisions of the Capital Market Act, regulating Financial instruments markets.

Also deemed as a Target Company is any joint stock company with more than 100 shareholders and share capital larger than HRK 30,000,000.00.

1.3 Are there special rules for foreign buyers?

Croatian law does not discriminate towards foreign investors, whether legal or natural persons, and, as a principle, offers them equal treatment to that offered to Croatian investors.

The principle of equal treatment of domestic and foreign investment is prescribed by the Constitution of the Republic of Croatia, which provides that “...rights acquired by investment of capital shall not be restricted by law or any other legal act” and “... foreign investors shall be guaranteed free transfer and repatriation of profit and the capital invested”.

The Investment Promotion Act regulates the promotion of investments equally, whether they are domestic or foreign legal entities or natural persons, and it is aimed at stimulating the economic growth, development and implementation of the economic policy of Croatia and its integration into international trade flows by increasing exports and enhancing the competitive ability of the Croatian economy. There are several groups of incentives provided by the Investment Promotion Act, such as tax incentives, custom incentives, or incentives for employment of new employees. The incentive rate depends on the value of investment and the number of newly-opened working places.

However, foreign investments have to be reported to the Croatian National Bank for purposes of gathering data for preparing statistical overviews of foreign investments portfolio.

1.4 Are there any special sector-related rules?

The Takeover Act regulates the takeover procedure where the Target Company meets certain requirements, as explained above under question 1.2.

The Competition Act will be applicable if the takeover raises competition issues. In such a case, the Croatian Competition Agency (hereinafter: “the CCA”) has jurisdiction to issue clearance for the intended transaction or to refuse it.

For transactions in specific fields there are some specific regulatory bodies that might have jurisdiction, e.g. the Croatian National Bank for the banking sector, and the Croatian Energy Regulatory Agency for the energy sector.

The Insurance Act prescribes the obligation to inform the Croatian Financial Services Supervisory Agency (hereinafter: “the CFSSA”) of any acquisition of shares in the amount of 20%, 30%, or 50% of the share capital of the target company.

Media companies are bound by specific merger control requirements with respect to concentration. The parties to the concentration are obliged to submit the notification of intended

concentration to the CCA every time when one or more shares of a media company are acquired, notwithstanding general thresholds prescribed by the Competition Act.

The CFSSA also supervises acquisitions of Investment funds, leasing companies, as well as the Investment companies. Under the Capital Market Act, before an Investment company completes a merger or a division, it must obtain previous consent from the CFSSA. Further, a written consent issued by the CFSSA is required before a qualified share (where as a result of the transaction the proportion of the voting rights or of the capital held would reach or exceed 20%, 30% or 50%, or the investment company would become an acquirer's subsidiary) in an Investment company is transferred. Under the Leasing Act, before acquiring a share reaching or exceeding 20%, 33% or 50% of voting rights or the capital share in a leasing company, or before closing a transaction which would cause the leasing company to become acquirer's subsidiary, acquirer is obliged to obtain previous consent from the CFSSA.

1.5 What are the principal sources of liability?

The Takeover Act envisages a misdemeanour liability for violation of its provisions, for which it prescribes fines for the bidder and its responsible person. Thus, the bidder (whether a natural person or a legal entity) will be fined with the amount ranging from HRK 50,000.00 to HRK 1,000,000.00, depending on the type of violation, while the responsible person of the legal entity will be fined with the amount ranging from HRK 10,000.00 to HRK 500,000.00.

The Capital Market Act also envisages misdemeanour liability of a legal entity and its responsible person who violate provisions of the Act. A prescribed money fine for the legal entity ranges from HRK 15,000.00 to HRK 1,500,000.00, depending on the type of violation, while the responsible person of the legal entity will be fined with the amount ranging from HRK 5,000.00 to HRK 200,000.00.

In addition to liability for misdemeanour, if the CFSSA establishes that a person who was obliged to publish a takeover bid failed to do so within the legal deadline, the CFSSA will pass a decision on the obligation of such person to publish the takeover bid, and deliver it to the issuer, to the shareholders through the issuer or through the depository, to the depository and to the stock exchange or the regulated public market where the issuer's shares have been listed.

In such case, each issuer's shareholder may, through a competent commercial court, require a mandatory conclusion of an agreement on sale of shares, subject to the conditions according to which the takeover bid had to be published.

2 Mechanics of Acquisition

2.1 What alternative means of acquisition are there?

In case of a takeover according to the Takeover Act, the way of carrying out a takeover is to make a public bid pursuant to the provisions of the Takeover Act. If Takeover Act is not applicable (e.g. because the thresholds are not met), the acquirer can purchase the target's shares either at the stock exchange or off-exchange, in private transactions with the shareholders. Financial assistance rules apply to joint stock companies and no whitewash procedure is available while, on the other hand, for limited liability companies, granting upstream loans is possible under certain conditions.

2.2 What advisers do the parties need?

Due to the complexity of the contemplated transaction and the impact of rather precise formal legal procedures, "usual suspects" being domestic financial advisors and legal advisors are compulsory for completion of the transaction.

2.3 How long does it take?

In a public bid process timelines are as follows.

Within 30 days after the obligation has arisen to publish a takeover bid, the bidder must submit a request to CFSSA for the approval to publish a takeover bid, the bid and other prescribed documents.

The CFSSA must issue a formal decision on the bidder's request to publish the takeover bid within 14 days after the receipt of a duly submitted request.

The bidder is obliged to publish the offer in the period of 7 days following the receipt of the CFSSA's decision approving its publication.

The bid is valid for 28 days after its publication. However, in cases when competing takeover bids are published, the validity period of the bid is extended to match the validity period of the counter-bid. The final validity period of the offer and counter-offer may not be longer than 60 days as of the publication of the first takeover offer. It is important to note that the counter-offer must be published a minimum of 10 days before the expiration of the validity period of the offer, and no later than 28 days before the expiration of the final deadline of 60 days.

In the case that the offer has been changed, its validity period will be extended for 7 days.

The change of the offer must be published at least 10 days before the expiration of the offer's validity period.

2.4 What are the main hurdles?

The issue of control over the management board's actions taken during hostile takeovers is present in practice.

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

The price of shares is determined in accordance with the Takeover Act.

The main principle of the Takeover Act is that the bidder and the persons acting in concert with the bidder are obliged to offer equal price for all the shares of the same class.

The price in the takeover bid must not be lower than the highest price at which the bidder and the persons acting in concert with it have acquired the voting shares in the period of one year before the obligation to publish the takeover bid was created.

However, if the average price of shares realised on the stock exchanges is higher than such price, the bidder is obliged to offer a higher price, calculating the average price for every individual stock exchange as a weighted average of all the prices realised on the stock exchange in the course of three months before the obligation to announce a takeover bid was created.

If the bidder and the persons acting in concert with the bidder have not acquired voting shares in the period of one year before the creation of the obligation, the price in the bid may not be lower than the average price realised on the stock exchanges.

If the bidder or the person acting in concert with the bidder acquires the shares of the target company which were subject to a bid, within one year following the date of expiry of the period for acceptance

of the bid, at a price higher than the one in the bid, it shall be obliged to compensate to the shareholders who have accepted the takeover bid for the price difference within 7 days from the acquisition date. This obligation does not relate to acquisitions of shares in the case of status changes or increase in equity capital of the target company or acquisition of shares of the target company in exchange for the dividend payment.

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

Currently, only cash consideration can be offered. When Croatia enters into the European Union, the provision of the Takeover Act providing for the possibility to offer exchange shares or combined consideration (exchange shares and cash) will enter into force.

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

The Takeover Act prescribes as one of the general principles that issuer's shareholders must have an equal position in the takeover procedure, which means that the offered price must be equal for all shareholders.

2.8 Are there any limits on agreeing terms with employees?

The Takeover Act obligates the management board of the target company to publicise a reasoned opinion on the takeover bid within 10 days following the publication of the bid *inter alia* the opinion on strategic plans of the bidder with regard to the target company and possible repercussions of the implementation of these plans on the employment policy and the labour law status of employees of the target company, as well as on possible changes in the locations of the company's places of business.

Prior to the disclosure of the respective opinion, the management board of the target company shall present that opinion, within 5 days from the day of announcement of the takeover bid, to the representatives of the employees, or where there are no such representatives, the employees themselves, who, within 3 days from the day of the presentation, may give their opinion on the takeover bid.

If the management board of the target company, within the time limit referred to in the previous paragraph, receives the opinion of the representatives of employees on the takeover bid by the date of disclosure of the opinion, it is obliged to enclose it with its own opinion at disclosure.

Provided that the opinion on the takeover bid or the opinion of the employees contains false or misleading information, the persons who have prepared or participated in the preparation of the opinion will be jointly and severally liable to the shareholders for the damage, if they were aware or should have been aware that the information was false or misleading.

The management board of the target company is obliged to deliver the opinion on the takeover bid to the CFSSA, the Regulated Market and Multilateral Trading Facilities on which shares of the target company are admitted to trading, no later than on the same day when it gives publication orders to the publishers.

2.9 What documentation is needed?

The bidder must deliver to the CFSSA the original or the notarised copy of the following documents:

- documents on the legal transactions on the basis of which the

bidder and persons acting in concert with it have acquired shares of the target company in a period of one year prior to the creation of the obligation to announce a takeover bid;

- statement of the bidder and of the persons acting in concert with the bidder that, in addition to the legal transactions referred to in the previous paragraph, they have not concluded any other legal transactions aimed at the acquisition of shares of the target company;
- depository's receipt of the secured consideration for a takeover of all the shares subject to a takeover bid (bank guarantee or deposit of the required amount);
- stock exchange receipt, issued at the request of the bidder, of the average price referred to in question 2.5;
- agreement on share deposit concluded with a depository;
- prior approval of the Croatian National Bank, if bank shares are the subject of a takeover, i.e. prior approval of another competent institution in other cases, as provided for by the law;
- court register certificates, or certificates issued by another appropriate register, indicating the legal form, registered office, business address, list of persons authorised for representation, issued no later than 30 days prior to the submission of the application, if the bidder and the person acting in concert with him is a legal person with a registered office abroad;
- statement appointing a proxy (name, registered office, business address, i.e. first and last name and address) for receiving documents in the Republic of Croatia, if a legal or natural person has a registered office, temporary residence or permanent residence abroad;
- other documents upon the Agency's request; and
- proof of payment of administrative fee and tax.

Additionally, if the documents enclosed with the takeover bid are written in a foreign language, their translation into the Croatian language by a certified court interpreter.

2.10 Are there any special disclosure requirements?

As a general principle, the Takeover Act prescribes that the shareholders in the Target Company must have sufficient time and information needed for deciding on the takeover bid.

The rules for determining the price are provided above under question 2.5. Under the Takeover Act, it is mandatory for the bidder to refer to the manner in which the offered takeover price was determined. Also, the management of the Target Company must publicise its opinion on the adequacy of the published bid.

2.11 What are the key costs?

The key cost is the cost of the security payment for shares to which the bid refers (e.g. bank guarantee).

Furthermore, an additional significant cost is the administrative fee in the amount of 0.2% of the price of the shares to which the offer applies (the fee may not exceed 5 million HRK - approximately 675,000 EUR), for the approval of the mandatory offer by CFSSA.

In case of a large number of shareholders, the costs of the Central Depository and Clearing Company (compulsory involvement) could also be significant.

2.12 What consents are needed?

Merger control clearance (if required) should be applied for following publication of the bid, but prior to closing of the takeover procedure, however the application can be submitted also prior to

publication of the takeover bid, if the intention of publishing a takeover bid has been announced.

Depending on the industry, further approvals of competent regulators as indicated under question 1.4 above are required.

2.13 What levels of approval or acceptance are needed?

In case of a mandatory bid, the bidder may only state in the bid that it will not purchase encumbered shares.

In case of a voluntary bid, the bidder may state in a bid that it will not purchase encumbered shares or the shares that will be deposited for the acceptance of the takeover bid if the total number of votes accorded by such deposited shares, together with the total number of votes that the bidder already has, does not exceed certain threshold (to be determined by the bidder, but not lower than controlling thresholds pursuant to the Takeover Act, i.e. 25%) of voting rights accorded by all the issued shares carrying voting rights. In such a case, if an insufficient number of shares is being deposited, the bidder may not purchase and take over the deposited shares.

2.14 When does cash consideration need to be available?

Pursuant to the Takeover Act, the cash consideration has to be paid to shareholders that tendered their shares within 14 days as of the lapse of the offer validity period. In practice, the depository (who will carry out the payment) requires to receive the cash consideration into its account at least 1 business day prior to elapse of this 14-day period.

3 Friendly or Hostile

3.1 Is there a choice?

The Takeover Act does not distinguish between the hostile and voluntary takeover bids. The Act prescribes the obligation of the target's management board and supervisory board to act in the best interest of the target company in relation to the takeover bid, regardless of whether the bid is hostile or voluntary.

3.2 How relevant is the target board?

During the public bid, certain activities of the management board of the target company are limited by operation of the law. As of the date of receipt of the notification, i.e. of the date of announcement of the same, if the management board has not received the notifications until the date of publication of the takeover report, the management and supervisory board of the target company may not, without the approval of the general meeting of the target company:

1. increase equity capital;
2. enter into transactions outside the regular business operations of the target company;
3. act in a manner that could seriously threaten further operations of the target company or enter into transactions that could seriously threaten further operations of the target company;
4. decide on the acquisition and disposal of own shares of the target company or securities conferring rights to these shares; or
5. act in a manner which might result in an impediment to or frustration of the takeover bid.

3.3 Does the choice affect process?

Within strictly formal, legal terms, the choice does not affect the process. However, since the compulsory disclosure rules for publicly listed companies are limited, the choice has certain influence, on a case by case basis, on the success of the bid.

4 Information

4.1 What information is available to a buyer?

All publicly traded companies are obliged to make their financial statements available to the public as well as all other essential/sensitive info (material facts) that might have an impact on the price of the shares. Furthermore, all information relating to the general corporate standing of the company are available in the court register which, due to the publicity principle, is obliged to give access to this info to every person that applied for such an insight.

4.2 Is negotiation confidential and is access restricted?

The mere fact of negotiations taking place ought to be disclosed by the target at the moment when said negotiations achieve the status when they become, in terms of the Capital Market Act, a privileged information, and the issuer is obliged to publicise it.

The Takeover Act contains a similar provision, obliging the Target Company to immediately notify the CFSSA of all the procedures or negotiations with the bidder or the persons acting in concert with the bidder, or of the fact that such procedures or negotiations are not underway.

Outside the takeover process the access to the Target Company shareholders is highly restricted: no public offer, or any other invitation addressed to the shareholders, with a view to acquire the shares carrying voting rights of the Target Company is permitted, if such acquisition creates the obligation to announce a takeover bid.

4.3 What will become public?

According to the Capital Market Act, the issuer of securities listed in a regulated market must promptly inform the public of all information pertaining to the issuer, which constitute privileged information. The issuer must conduct this publication as soon as possible, whereby it must ensure that such information is complete, truthful and substantially accurate.

Privileged information is defined as information of precise nature which has not been made public, relating, directly or indirectly, to issued securities which, if it were made public, would be likely to have a significant effect on the prices of those securities or on the price of related derivative financial instruments.

4.4 What if the information is wrong or changes?

The bidder could not "walk away" from the offer in the case of the material adverse change. The target and its officers are liable for accuracy of all material information that was surrendered to the public.

5 Stakebuilding

5.1 Can shares be bought outside the offer process?

In principle, shares (in excess of 25% of the share capital being the control threshold) cannot be bought outside the offer process. The exceptions from the obligation to publish a takeover bid are prescribed by the Takeover Act, and are if the bidder:

1. acquires the shares of the target company by inheritance;
2. acquires the shares of the target company by a division of marital property;
3. acquires the shares of the target company in the equity capital increase procedure, by issuing shares, and the general meeting of the target company, at which the decision is adopted on the increase in equity capital, has approved that the acquirer may acquire voting shares of the target company without the obligation to announce a takeover bid, if such acquisition of voting shares would create an obligation for an acquirer to announce a takeover bid;
4. acquires the shares of the target company which is a bankruptcy debtor in the bankruptcy proceedings;
5. acquires the shares of the target company through a merger of companies, but exclusively in the case where only one of the companies involved in such merger holds the shares of the target company;
6. acquires the shares of the target company through a change of the company's legal form;
7. a legal person acquires the shares of the target company from another legal person whose members or shareholders are, either directly or indirectly, the same persons, or if it acquires the shares through a transfer due to a restructuring within the group;
8. acquires the shares of the target company in exchange for the dividend payments and the general meeting of the target company has approved that the acquirer may acquire voting shares of the target company without the obligation to announce a takeover bid, if such acquisition of voting shares would create an obligation for the acquirer to announce a takeover bid;
9. following the completion of the takeover bid, he acquires the shares of the target company through a transfer between persons who acted in concert in the takeover bid;
10. by the acquisition of shares of the target company, he holds a percentage of voting shares equal to or less than the percentage of voting shares held by another shareholder of the target company, who has announced a takeover bid;
11. as a credit institution, it disposes of the shares, within 6 months from the date when it became a rightful owner of the shares it acquired as a fiduciary creditor; or
12. as creditors, they acquire shares of the companies undergoing rehabilitation, in accordance with the Act on Rehabilitation of Certain Companies.

Further exceptions can be introduced through separate pieces of legislation.

5.2 What are the disclosure triggers?

When a natural or legal person directly or indirectly acquires, exceeds or falls below the threshold of 5%, 10%, 15%, 20%, 25%, 30%, 50% or 75% of votes in the assembly of the issuer of shares, that person or entity must notify in writing the CFSSA and the issuer.

5.3 What are the limitations and implications?

The Takeover Act provides for thresholds, which, if exceeded,

trigger the obligation to publish the takeover offer. These are:

- control thresholds - acquiring of, directly or indirectly, independently or acting in concert, voting shares of the target company, which, together with the shares already possessed, exceed a threshold of 25% of voting shares of the target company;
- additional thresholds - after exceeding a control threshold and announcing a takeover bid, obligation to publish a new takeover bid arises if, independently or acting in concert, through a direct or indirect acquisition of voting shares of the target company, the percentage of voting rights has been increased by more than 10%; and
- final thresholds - notwithstanding the additional threshold, there is an obligation to publish a takeover bid if, after the takeover bid, independently or acting in concert, through a direct or indirect acquisition of voting shares of the target company, the percentage of voting shares has been increased by less than 10%, if as a result of this acquisition, a threshold of 75% of voting rights is exceeded.

The implication of meeting these thresholds is that the obligation to publish a takeover bid, as prescribed by the Takeover Act, arose, and this obligation cannot be averted save in exceptional cases stated above under question 5.1.

6 Deal Protection

6.1 Are break fees available?

Contractual penalties are not prohibited in the Croatian legal environment. Thus, if contracted, break fees are available.

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

The management of the target company must act in the best interest of the target company in the takeover procedure. On the other hand, the shareholders could agree not to shop.

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

The target company could agree to issue shares or sell significant assets, only with the approval of its general meeting, as described under questions 3.2 above.

6.4 What commitments are available to tie up a deal?

All commitments from the shareholders that would not induce the target to undertake any prohibited action (please see question 3.2 above) are permitted.

7 Bidder Protection

7.1 What deal conditions are permitted?

Please see question 6.4 above.

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

Until the bidder has carried out the takeover procedure pursuant to the provisions of the Takeover Act, its shares and the shares of the

persons acting in concert with the bidder do not carry voting rights.

7.3 When does control pass to the bidder?

The hypothetical, abstract control passes with the transfer of shares subsequent to the offer process – on the day when the bid has become successful and shares have been transferred to its account with the Central Depository and Clearing Company.

The actual control passes when the bidder appoints the new Supervisory and Management Board (only available if it acquires more than 75% of the shares of the target).

7.4 How can the bidder get 100% control?

If the bidder got 95% of the shares, the Company Act permits the process of squeeze-out in order to obtain the rest of the shares.

8 Target Defences

8.1 Does the board of the target have to tell its shareholders if it gets an offer?

Only in cases in which the Takeover Act applies, such explicit legal obligation exists.

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

Very little, since the target’s board has to follow the prescribed procedure in the takeover process, as described under question 3.2 above. However, the Takeover Act explicitly permits the target’s board to seek other bidders.

8.3 Is it a fair fight?

It remains to be seen since there have been very few hostile takeovers in Croatia.

9 Other Useful Facts

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

In practice the success depends mainly on the offered price. Also, the general economic environment is an issue that the most of short-term investors tend to consider.

9.2 What happens if it fails?

In case an insufficient number of shares are being deposited (provided that the bid is conditioned), the bidder may not purchase and take over the deposited shares. In principle, the bidder is not entitled to claim any cost back (e.g. fees of the CFFSA, Central Depository & Clearing Company, Deposit Bank etc.).

10 Updates

10.1 Please provide, in no more than 300 words, a summary of any relevant new law or practices in M&A in Croatia.

The new trends and developments in M&A law and practise in Croatia are closely connected with the procedure of adjustment of the Croatian legal system with the *acquis communautaire*.

The Croatian Parliament has enacted the new Takeover Act on 5 October 2007, with amendments adopted in March 2009. The purpose of the latest amendments to the Takeover Act was to adjust the text to the new Capital Market Act, adopted in July 2008, mainly in relation to the scope of application of the Act, in changing the way “Target Company” is defined.

Both Capital Market Act and the Takeover Act were adopted in order to implement the European standards in the field of M&A, and respond to solutions adopted in respective Directives of the European Parliament and of the Council, as well as to the relevant Commission Regulations.

However, a significant part of the Capital Market Act and the Takeover Act (e.g. introduction of exchange shares as consideration in the takeover offer) will enter into force on the day of the Republic of Croatia’s accession to the European Union.

Review of previous practise of the CFSSA in relation to takeover of joint stock companies points out the fact that the overall number of mandatory takeovers vastly exceeded the number of voluntary takeover proceedings conducted in Croatia, both in first three quarters of 2010 and in the preceding period.





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