

**Ruling by the Administrative Court of the Republic of Croatia, No.: Us-5362/2007-10
from November 3, 2010**

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ADMINISTRATIVE COURT OF THE REPUBLIC OF CROATIA

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RULING

The Administrative Court of the Republic of Croatia by means of a council consisting of Judge Dubravko Markt as the president of the council, Smiljan Mikus and Lidija Rostas-Beros as council members, and senior counsel Biserka Spoljar as court reporter, in an administrative case by plaintiff VARTEKS d.d. Varazdin, represented by Board Chairman Zoran Koscec, against a resolution by the accused Agency for the Protection of Market Competition, class: UP/I 430-01/2004-01/42, reg. No. 580-03-07-17-24 from April 4, 2007 in regards to the awarding to state aid, has ruled during a private council meeting held on November 3, 2010 as follows:

I. The claim is granted.

The resolution of the Agency for the Protection of Market Competition, class: UP/I 430-01/2004-01/42, reg. No.: 580-03-07-17-24 from April 4, 2007 will be annulled.

II. This ruling will be published in the »Official Gazette«.

Statement of reasons

On the grounds of the challenged resolution, the accused body gave its consent to Decisions by the Republic of Croatia which contain state guarantees, and which constitute state aid for the restructuring of the plaintiff, and it defined special measures and deadlines for their execution towards the Ministry of Economy, Labour and Entrepreneurship, and prohibited the plaintiff from receiving any form of state aid until December 31, 2007, i.e. from receiving state aid for restructuring in the time period from April 4, 2007 to April 4, 2017 (ten years).

The plaintiff challenges the legality of the resolution of the accused body due to all reasons stipulated by the provisions of article 10, item 1, clauses 1 and 3 of the Administrative Disputes Act. Due to the complexity of this subject, he deems it necessary that the Ministry of Economy, Labour and Entrepreneurship, the Ministry of Finance of the Republic of Croatia and the Croatian Bank for Reconstruction and Development become involved as interested parties. The plaintiff essentially states that the cessation of the guarantees issued on the grounds of a Decision by the Government of the Republic of Croatia on the granting of state guarantees to which the accused body gave its consent only up to December 31, 2007, the Croatian Bank for Reconstruction and Development as the creditor according to the taxatively listed loan agreements and annexes thereof was left without guarantees amounting to HRK 50

million as a security instrument for the listed loan agreements. Moreover, the plaintiff holds that the Croatian Bank for Reconstruction and Development could thus call on him to settle aforementioned loan agreements since due to the cessation of the state guarantee he no longer fulfills the terms and conditions of aforementioned agreements, more precisely, the condition to provide and maintain in effect security instruments, of which one is the guarantee from the Croatian Ministry of Finance, amounting to HRK 50 million plus interest. Thus the plaintiff deems that an irremediable damage and enormous cost could arise for him through the application of the challenged resolution. He also points out that the accused body cannot apply European Community regulations as legal sources due to unbridgeable constitutional and existential conflicts. In that regard he points out that in this concrete case the Stabilization and Association Agreement between the Republic of Croatia and the European Community and its member states could be applicable, as well as the Temporary Agreement on Trade and Related Issues between the Republic of Croatia and the European Community, while the European Community's interpretation criteria, standards and instruments the accused body is referring to, and which are not contained in the text of these international agreements, nor have they been taken over into or published in any other Croatian act or regulation, cannot serve as a legal source. Along with the aforementioned the plaintiff also lists existential conflicts in terms of the direct application of foreign legal sources as well as the lack of knowledge of the foreign language, the inability to have insight into foreign regulations, the lack of knowledge of foreign legal systems and the lack of authorization on the part of bodies of the Republic of Croatia to pass decisions through the direct application of foreign regulations. Moreover, he states that he was not able to participate in or speak his mind in regard to the process that preceded the passing of the challenged resolution, which he deems a severe violation of the rules of procedure. He also holds that the accused body wrongfully interpreted and applied the provisions of the State Aid Act, without acknowledging the objective and meaning that is aimed to be achieved through the provisions of aforementioned regulations, for which he offers an extensive explanation in his claim. He also points out that the accused body wrongfully determined in the challenged resolution that the loan agreements concluded with the Croatian Bank for Reconstruction and Development are loan agreements that were concluded under conditions that are more favorable than market conditions and that they therefore contain state aid, and that it wrongfully determined the value of state aid granted via aforementioned loans. Apart from this, the plaintiff points out that the accused body retroactively applied the Rulebook on the Form, Content and Manner of Data Collection and Record-Keeping in Regards to State Aid to the detriment of the plaintiff and for the needs of the calculation of aid elements. The plaintiff namely claims that aforementioned regulation cannot be applied to the loan agreements he concluded prior to the regulation's coming into effect, i.e. prior to January 29, 2005. As a result, it emerges that the accused body wrongfully applied aforementioned calculation manner for aid elements for loans by the Croatian Bank for Reconstruction and Development granted in 2003 and 2004. Likewise, he also points out that the accused body listed in the challenged resolution measures that have to be met in order to reduce the negative effects of state aid, measures which are not founded in any way on regulations in the Republic of Croatia, nor are they founded on an accurately determined factual situation, which vividly shows how an incorrect conclusion in regards to the factual situation was drawn from wrongfully determined facts. Conclusively he points out that the accused body drafted the challenged resolution on wrongfully and incompletely determined facts, i.e. the thesis that the restructuring process began in 2004 and would last until December 31, 2007, and by listing these and other reasons, the plaintiff proposes that the Court grants this claim and that it annuls the challenged resolution in full.

In a detailed reply to the claim, the accused body deems that the reasons for the claim are fully unfounded and without valid arguments. It essentially states that the challenged resolution was passed on the grounds of an accurately determined factual situation, through the drawing of an accurate conclusion from the determined facts, and pursuant to the provisions of the State Aid Act and the provisions of the State Aid Decree. The accused body sticks to its claims from the statement of reasons of the challenged resolution, and adds that no irremediable damage and enormous costs would have arisen for the plaintiff from the application of the challenged resolution considering the fact that in this case the other security instruments through which the loan agreements concluded with the Croatian Bank for Reconstruction and Development (apart from the state guarantees) had been secured had not been sufficient for the bank, and that due to the financial difficulties of the plaintiff the Croatian Bank for Reconstruction and Development had requested state guarantees as additional security instruments.

The accused body also points out that consent to state guarantees for loan agreements concluded between the plaintiff and the Croatian Bank for Reconstruction and Development had been given up to December 31, 2007, i.e. until the completion of the restructuring process, since state aid for restructuring cannot continue to exist after a completed restructuring process, and in the concrete case these are state guarantees to the benefit of the Croatian Bank for Reconstruction and Development. It also deems unfounded the plaintiff's claim that it should not have used European Commission regulations as legal sources. State aid determined by aforementioned act and the decree are namely fully founded on the *acquis communautaire* of the European Union. Considering that the plaintiff filed his application for the granting of state aid on December 30, 2004, i.e. during the validity of the Community's Guidelines on State Aid for Rescuing and Restructuring Firms in Difficulty, these are in this concrete case both the applied standards and criteria for the assessment of state aid for restructuring that emerge from aforementioned guidelines from 2004. In regards to plaintiff claims in relation to the violation of the rules of procedure, because he was not enabled to speak his mind during the procedure, the accused body deems that these claims are unfounded. It points out the particularity of an administrative procedure in which state aid is approved, supervised and returned and which is regulated by the State Aid Act as *lex specialis*. One fundamental characteristic of the initiation of a process for the approval of state aid emerges from the fact that in no case the procedure can be initiated by an entrepreneur, i.e. an aid beneficiary, but only by the provider of state aid or the accused body by official duty. Hence the provider, as the initiator of the procedure, decides during the initiation of the procedure about the entrepreneur for which he will submit a proposal in regards to an approval act or the granting of aid, and he will state the state aid value and type. Apart from this, the accused body points out that the plaintiff had been given the opportunity to speak his mind about all important facts and circumstances he deemed could contribute to the solving of the administrative issue concerned, and which had been determined during the procedure concerned, in written form a number of times, whereby the accused body refers to a notification from November 30, 2005, as well as meetings held with the plaintiff with the aim to clarify certain parts of the Restructuring Plan (January 31, 2005, January 12 and February 3, 2006). In regards to claims that pertain to loan agreements with the Croatian Bank for Reconstruction and Development concluded under more favorable conditions than market conditions, the calculation of state aid with state guarantees, and in relation to measures that had to be completed during the restructuring process, the accused body fully sticks to the claims from the statement of reasons of the challenged resolution along with additional explanations. Conclusively, the accused body points out that state aid for restructuring can be

approved exclusively to entrepreneurs in financial difficulties, and by bringing forward these and other reasons, the accused body suggests that the Court reject the claim.

The claim is founded.

Assessing the legality of the challenged resolution within the limits of the request of the claim, whereby, pursuant to article 40, item 1 of the Administrative Disputes Act (»Official Gazette« No. 53/91, 9/92 and 77/92), the court is not bound by the reasons of the claim, this Court deems that the challenged resolution cannot be assessed as lawful.

The general terms and conditions for the approval, the supervision of the application and the return of state aid with the aim to preserve entrepreneurial and market freedom, to secure an equal legal position for all entrepreneurs on the market, to encourage economic progress, the social welfare of people and care for economic development and the protection of environment in all regions in the Republic of Croatia, and the application of internationally taken over obligations of the Republic of Croatia are namely defined by the State Aid Act (»Official Gazette«, No.: 47/03 and 60/04).

Thus aforementioned act stipulates that through a resolution as an administrative act the Agency for the Protection of Market Competition: a) gives consent to an act proposal that intend to approve or offer individual aid; b) withholds consent to an act proposal that intends to approve or offer individual aid; c) rejects the request for consent to an act proposal that intends to approve or offer individual aid; d) abolishes consent given to an act proposal that intends to approve or offer individual aid and orders the return of funds used on the basis of approved or given individual aid and e) suspends the procedure (article 9, item 2).

So in the administrative procedure giving consent to Decisions by the Government of the Republic of Croatia which contain state guarantees and constitute state aid for the plaintiff's restructuring in the concrete case, procedural rights listed in the State Aid Act, the State Aid Decree (»Official Gazette«, No.: 121/03 and 50/06) and the General Administrative Procedure Act (»Official Gazette«, No.: 53/91 and 103/96 – Decision of the Constitutional Court of the Republic of Croatia) are applicable.

According to the provisions of article 3 of the General Administrative Procedure Act, administrative areas for which the law prescribes a special procedure are handled pursuant to the provisions of this Act. All issues that are not regulated by special acts are handled according to the provisions of this act. According to the provisions of article 1, item 1 of the same act, state administration bodies and other state organs are obliged to act pursuant to this act when solving rights, obligations or legal interests of persons or legal persons or other parties, directly applying regulations. According to item 2, other legal persons are also obliged to act pursuant to this act when solving administrative issues while exercising public powers. In this case the accused body ignored the basic provisions of the General Administrative Procedure Act.

The provisions of article 49, item 1 of the General Administrative Procedure Act stipulate that a party is a person on whose request a procedure was initiated or against whom a procedure is underway, or who has the right to participate in a procedure to protect his/her rights or legal interests. According to article 50, item 1 of the same act, every physical and legal person may be a party in an administrative procedure. Through the challenged resolution the accused body, amongst other things, prohibited the plaintiff from receiving any kind of state aid until

December 31, 2007 or to receive state aid for restructuring in the time period from April 4, 2007 to April 4, 2017 (ten years).

Hence it should be pointed out here that the principle of hearing a party is one of the basic principles of an administrative procedure. Pursuant to the provisions of article 8, item 1 of the General Administrative Procedure Act, in the passing of a resolution parties have to be given the opportunity to speak their mind in regards to facts and circumstances which are of importance for the passing of a resolution, while pursuant to item 2 of the act, a resolution can be passed without a previous declaration by the party only in cases where this is permitted by the law. The procedure for the passing of a resolution is defined in chapter XI of the act. According to article 135 of the act, prior to the passing of a resolution all facts and circumstances that are significant for the resolution have to be passed, and it has to be made possible for the parties to effectuate and protect their rights and legal interests. This can be done using summary procedure or through a separate examination procedure. Summary procedures are not foreseen by the State Aid Act, nor is this a situation according to article 141 of the General Administrative Procedure Act when a resolution can be passed using summary procedure. Thus in this case a special examination procedure would have to be carried out prior to the passing of a resolution, and potentially a verbal discussion, considering plaintiff objections in regards to the determined factual situation (articles 142 and 149 of the General Administrative Procedure Act).

In regards to the application of rights it should be pointed out that the provisions of article 140 of the Constitution of the Republic of Croatia (»Official Gazette«, No.: 41/01 – corrected text and 55/01 – correction) stipulate that international agreements concluded and affirmed in accordance with the Constitution and published, and which are in effect, constitute a part of the legal system of the Republic of Croatia, and are above the act in terms of legal power. According to this, the Stabilization and Association Agreement between the Republic of Croatia and the European Community and its member states could have been applicable in this case, as well as the Temporary Agreement on Trade and Related Issues between the Republic of Croatia and the European Community, while the interpretation criteria, standards and instruments of the European Community which they accused body refers to and which are not contained in the texts of these agreements, nor have they been taken over and published in any other Croatian act or regulation, cannot serve as a legal source.

Thus the claim should have been granted pursuant to article 39, item 2 of the Administrative Disputes Act and the challenged resolution should have been annulled, with the accused body adhering to the court's legal opinion and its observations in regards to the procedure pursuant to article 62 of above act.

The publication of the ruling in the »Official Gazette« is founded on the provisions of article 17 of the State Aid Act.

No.: Us-5362/2007-10

Zagreb, November 3, 2010

Council President
Dubravka Markt